SCHAEFFLER

Annual Report 2017

Mobility for tomorrow

Leading into the future

Company profile

The **SCHAEFFLER** Group is a global automotive and industrial supplier. Top quality, outstanding technology, and exceptionally innovative spirit form the basis for the continued success of the company. By delivering high-precision components and systems in engine, transmission, and chassis applications, as well as rolling and plain bearing solutions for a large number of industrial applications, the Schaeffler Group is already shaping “Mobility for tomorrow” to a significant degree.

Schaeffler Group at a glance

Key figures

Income statement (in € millions)	2017	2016		Change
Revenue	14,021	13,338	5.1	%
• at constant currency			5.9	%
EBIT	1,528	1,556	-1.8	%
• in % of revenue	10.9	11.7	-0.8	%-pts.
EBIT before special items [1]	1,584	1,700	-6.8	%
• in % of revenue	11.3	12.7	-1.4	%-pts.
Net income [2]	980	859	14.1	%
Earnings per common non-voting share (basic/diluted, in €)	1.48	1.30	13.8	%
Statement of financial position (in € millions)	**12/31/2017**	**12/31/2016**		Change
Total assets	11,537	11,564	-0.2	%
Shareholders' equity [3]	2,548	1,997	551	€ millions
• in % of total assets	22.1	17.3	4.8	%-pts.
Net financial debt	2,370	2,636	-10.1	%
• Net financial debt to EBITDA ratio before special items [1]	1.0	1.1		
• Gearing Ratio (Net financial debt to shareholders' equity [3], in %)	93.0	132.0	-39.0	%-pts.
Statement of cash flows (in € millions)	**2017**	**2016**		Change
EBITDA	2,295	2,293	0.1	%
• in % of revenue	16.4	17.2	-0.8	%-pts.
EBITDA before special items [1]	2,351	2,437	-3.5	%
• in % of revenue	16.8	18.3	-1.5	%-pts.
Cash flows from operating activities	1,778	1,876	-98	€ millions
Capital expenditures (capex) [4]	1,273	1,146	127	€ millions
• in % of revenue (capex ratio)	9.1	8.6	0.5	%-pts.
Free cash flow	488	735	-247	€ millions
Value-based management	**2017**	**2016**		Change
ROCE before special items (in %) [1]	19.9	22.3	-2.4	%-pts.
Schaeffler Value Added before special items (in € millions) [1]	787	939	-16.2	%
Employees	**12/31/2017**	**12/31/2016**		Change
Headcount	90,151	86,662	4.0	%

[1] Please refer to pp. 60 et seq. for the definition of special items.
[2] Attributable to shareholders of the parent company.
[3] Including non-controlling interests.
[4] Capital expenditures on intangible assets and property, plant and equipment.

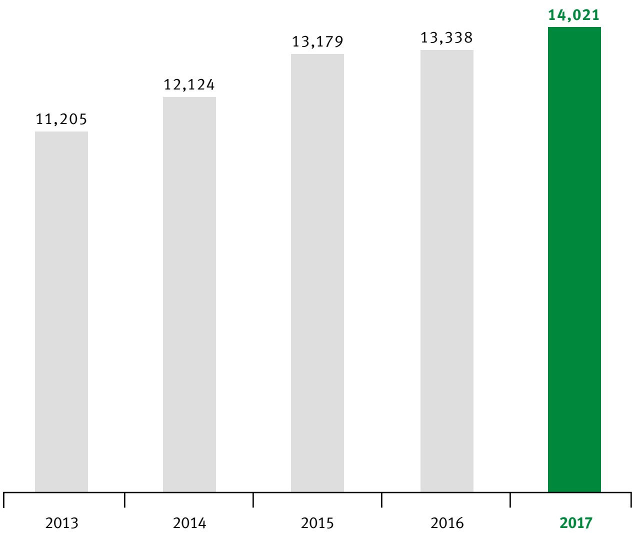
Automotive (in € millions)	2017	2016		Change
Revenue	10,869	10,338	5.1	%
• at constant currency			5.9	%
EBIT	1,283	1,373	-6.6	%
• in % of revenue	11.8	13.3	-1.5	%-pts.
EBIT before special items [1]	1,330	1,481	-10.2	%
• in % of revenue	12.2	14.3	-2.1	%-pts.
Industrial (in € millions)	**2017**	**2016**		Change
Revenue	3,152	3,000	5.1	%
• at constant currency			5.7	%
EBIT	245	183	33.9	%
• in % of revenue	7.8	6.1	1.7	%-pts.
EBIT before special items [1]	254	219	16.0	%
• in % of revenue	8.1	7.3	0.8	%-pts.

Prior year information presented based on 2017 segment structure.
[1] Please refer to pp. 60 et seq. for the definition of special items.

Key financials

Revenue 2013 – 2017

in € millions



Revenue growth vs. prior year

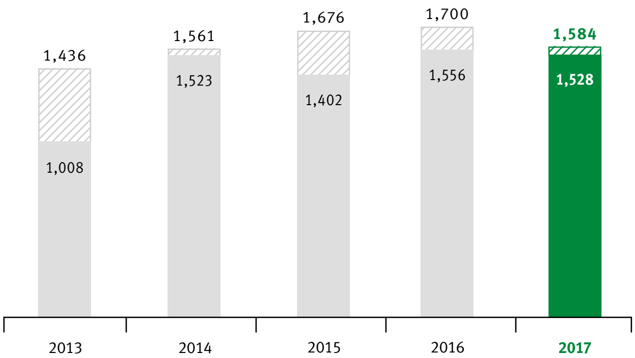
2013	2014	2015	2016	2017
+ 0.7%	+ 8.2%	+ 8.7%	+ 1.2%	**+ 5.1%**

Revenue growth at constant currency

2013	2014	2015	2016	2017
				+ 5.9%

EBIT 2013 – 2017

in € millions



EBIT margin before special items

2013	2014	2015	2016	2017
12.8%	12.9%	12.7%	12.7%	**11.3%**

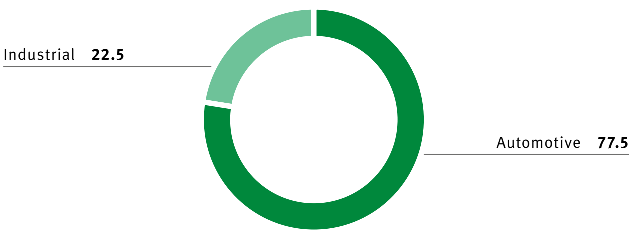
EBIT margin

2013	2014	2015	2016	2017
9.0%	12.6%	10.6%	11.7%	**10.9%**

EBIT before special items

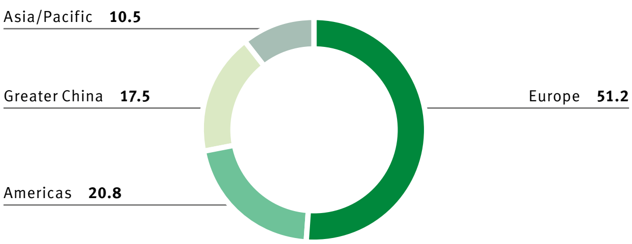
Schaeffler Group revenue by division

in percent



Schaeffler Group revenue by region

in percent by market view



Highlights 2017

Revenue increased significantly, 2017 strong year

Revenue at **EUR 14.0 bn**
(up 5.9% at constant currency)

EBIT margin before special items below prior year

EBIT margin before special items at **11.3%**
(prior year: 12.7%)

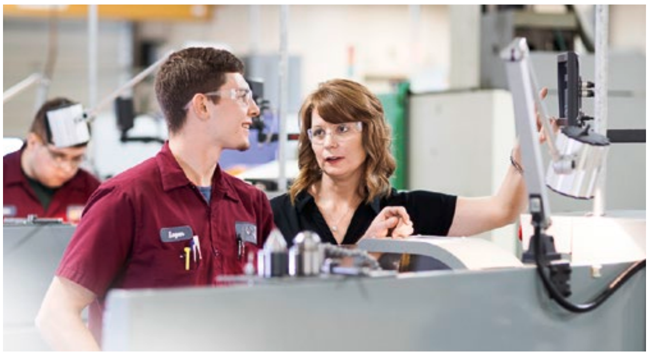
Capital expenditures increased significantly, free cash flow below prior year

Free cash flow at **EUR 488 m**
(prior year: EUR 735 m)

Net income increased by 14.1%

Net income at **EUR 980 m**
(prior year: EUR 859 m)

Leading into the Future



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Navigation aid

Further detail elsewhere in the report

Further detail online

Strategic initiative "Agenda 4 plus One"

Major events in 2017

January

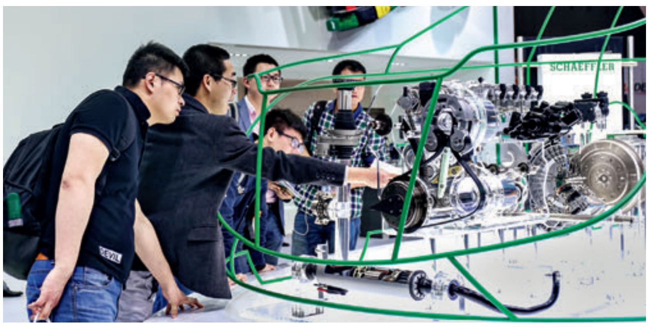
Detroit/USA: Schaeffler presents innovative drive concepts and solutions for the U.S. market at the North American International Auto Show (NAIAS) 2017 in Detroit. The best example is the “Schaeffler High Performance 48 Volt” concept vehicle with a Schaeffler electric rear axle that assists the internal combustion engine driving the front axle. Digital mobility solutions to complement the conventional automotive business are a further theme at NAIAS.

February

Berlin/Nuremberg: Outstanding ideas, courage, entrepreneurial and team spirit, and opportunities for exchanging information: That’s what Schaeffler aims to gain from cooperation with two business incubators. In February Schaeffler and Factory Berlin sign a partnership agreement for what is known as an Innovation Hub. In October the Zollhof Tech Incubator is inaugurated in Nuremberg. With financial support from companies like Schaeffler, this incubator gives IT start-ups the opportunity to further develop and implement their ideas, to exchange information, and to develop a network with science, industry, and investors.

April

Shanghai/China: Mobility requirements for the Chinese market are diverse. At Auto Shanghai 2017, Schaeffler presents products for the electrified drive train that are customized for the Chinese market and ready for volume production.



June

Fort Mill, Wooster/USA: Schaeffler reinforces its activities in the U.S. market. With an investment of approximately EUR 32.5 m, the company creates 105 new jobs at its Fort Mill location in South Carolina. In November, Schaeffler invests more than EUR 51 m to create of new production areas, a shipping center, and office space at its Wooster plant in the U.S. state of Ohio. The Wooster facility now employs nearly 2,000 staff.

July

Buehl: Schaeffler presents and explains its strategic direction and long-term growth perspectives at its Capital Markets Day to some 40 analysts and investors in attendance. As part of its strategy “Mobility for tomorrow”, the company has defined E-Mobility, Industry 4.0, and Digitalization as key opportunities for the future.

Montreal/Canada: Lucas di Grassi is the Formula E Champion 2016/2017, triumphing with Team ABT Schaeffler Audi Sport in the electric racing series. As the exclusive development partner for the powertrain of the ABT Schaeffler FE02, electric mobility pioneer Schaeffler demonstrated foresight by taking on the Formula E commitment three years ago, now celebrating a great triumph in the innovative racing series that has moved into clear focus with automobile manufacturers and the global public.

September

Frankfurt: As part of its strategy "Mobility for tomorrow", Schaeffler presents a comprehensive and sustainable approach at the IAA. This includes the entire energy chain from the generation and storage of energy, through to mobile energy use in eco-friendly vehicle drives.

Schweinfurt: Schaeffler begins the process of remodeling its corporate presentation around the "Schaeffler" corporate brand. Harmonization of the group's brand identity and corporate presentation is part of the "Global Branding" project, one of the 20 initiatives that make up the excellence program "Agenda 4 plus One" with which the company is driving forward its strategy "Mobility for tomorrow". This realignment kicks off at the company's Schweinfurt location.

Chengdu/China: Schaeffler expands its cooperation with Southwest Jiaotong University, intensifying its collaboration in the research and development of axlebox bearings for rail vehicles. The university is now part of the "SHARE" network (Schaeffler Hub for Advanced Research), which consists of cooperation partnerships with universities, institutes, and research facilities and is being consistently expanded.

October

Herzogenaurach: Schaeffler concludes a purchase contract for 100 % of the shares of autinity systems GmbH. The Chemnitz-based IT company specializes in digital machine data recording and evaluation. This acquisition represents a further important step in implementing the Schaeffler Group's Digital Agenda.

Svitavy/Czech Republic: The Schaeffler Group reinforces its lasting course for growth in Eastern Europe with investments worth around EUR 100 m and the creation of 900 new jobs within the next three years. With the new plant in Svitavy, Schaeffler strengthens its distinct manufacturing network in Eastern Europe.

Tokyo/Japan: At the Tokyo Motor Show 2017, Schaeffler presents solutions for a carbon-neutral mobility of the future, taking the entire energy chain into consideration. Electric mobility plays an important and forward-looking role in this mix. Products and systems that meet the new mobility requirements of the Japanese and Southeast Asian markets are presented at the motor show.

November

Langen: Schaeffler announces plans to invest EUR 180 m in building a state-of-the-art assembly and packaging center in Halle (Saale) in Saxony-Anhalt. Spare parts and repair solutions for the Automotive Aftermarket will be assembled and packaged there in an area of about 40,000 square meters.

Dong Nai/Vietnam: Schaeffler continues with the strategic expansion of its manufacturing footprint in Asia/Pacific by building a new plant on a 100,000 square meter property in the Dong Nai province. The investment of around EUR 55 m significantly increases Schaeffler's local manufacturing capacity. The plant will be the first needle roller bearing production site in the region and serves to expand the range of radial insert ball bearings for industrial customers.

December

Herzogenaurach: Schaeffler acquires the remaining 49 % stake in Compact Dynamics GmbH from SEMIKRON International GmbH. The acquisition expands Schaeffler's development capacities and service portfolio in the field of electric drives. Compact Dynamics has experience in the small-volume manufacture of electric motors for cars and light commercial vehicles, as well as for the aviation sector.

Georg F. W. Schaeffler Maria-Elisabeth Schaeffler-Thumann

Ladies and Gentlemen,

2017 was a year of ups and downs for Schaeffler. After a positive start to the year with good business results in the first quarter, the earnings guidance for the full year of 2017 had to be reduced in June. This was due to the second-quarter earnings situation in the Automotive division, which was significantly weaker compared with that of the prior year. However, thanks to the encouraging second half of the year, in which the revenue and earnings situation improved to the extent that the temporary unfavorable impact on earnings in the second quarter was partially offset, Schaeffler was able to achieve its targets for 2017 with regard to growth, earnings, and free cash flow.

Strong brands are becoming increasingly important in global competition. Based on our corporate values “Sustainable”, “Innovative”, “Excellent”, and “Passionate” – Schaeffler is just such a strong corporate brand with which the company positions itself as a global player and technology partner and helps to shape mobility for tomorrow. Accordingly, over the course of the past year the company began the process of remodeling its corporate presentation around the “Schaeffler” umbrella brand in order to emphasize the importance of the corporate brand and to meet global customer and market requirements. This not only improves the image of the company among our customers, potential employees, investors, and the general public – but above all, it also increases the identification of Schaeffler’s employees worldwide with the company. Their enthusiasm for the company and its goals is of fundamental importance, because they form the basis for success. This year’s annual report entitled “Leading into the Future” is dedicated to this important topic.

The world is changing at breathtaking speed. It is an essential component of our corporate culture to not only keep pace with this change, but to always be one step ahead and to think and act in a sustainable and future-oriented way. For this reason, E-Mobility, Digitalization and Industry 4.0 have been defined as key opportunities for the future. In the past year, vital progress was made in these areas, including through new cooperation agreements and acquisitions. Our separate E-Mobility business division was established at the turn of the year in order to highlight and combine Schaeffler’s expertise in the field of electric mobility, and an Industry 4.0 organizational unit was set up, which will handle all activities related to the mechatronics and digital service businesses.

Once again last year, Schaeffler continued to broaden its global presence with new locations and plant expansions in the USA, the Czech Republic, and Germany. Foundation stones were laid for new Schaeffler locations in Vietnam and China. Modern structures, innovative strength, and the ability to constantly improve in all areas form the basis for the company to expand its leading position and open up new business areas and markets.

We would like to extend our sincere thanks to all our business and research partners for their successful cooperation and the trust they have placed in our company. In particular, our heartfelt thanks go to our employees for their continued commitment and creativity. A strong foundation of values and respectful cooperation are very important to us as family shareholders, especially in a world that is becoming more and more digitized.

Yours sincerely

Maria-Elisabeth Schaeffler-Thumann

Georg F. W. Schaeffler

Klaus Rosenfeld
Chief Executive Officer

Ladies and Gentlemen,

It is my pleasure to summarize for you the Schaeffler Group's progress in 2017 in this annual report.

After setting the course for the further development of the Schaeffler Group in 2016 with our strategic concept "Mobility for tomorrow" and its 8 strategic pillars, our Excellence program "Agenda 4 plus One" with its 16 strategic initiatives, as well as the Financial Ambitions 2020 derived from it, in 2017 we were able to record initial successes by implementing our strategy and the various strategic initiatives. In this, we were mainly led by the first of our 8 strategic pillars: "We want to be the preferred technology partner for our customers." This ambition is both an obligation and an incentive for us. It is based on the conviction that the Schaeffler Group with its capabilities and expertise can contribute to making the world a "cleaner, safer, and smarter" place – as is stated in our vision that we formulated in 2016 as the starting point for our strategy development.

Strong growth – Net income increased
For the first time ever, the Schaeffler Group generated revenue of more than EUR 14 billion in 2017. This represents constant currency growth of 5.9 % and means we have exceeded the target we set for ourselves with our guidance for 2017 of 4 to 5 %. Both divisions and all four regions contributed to this strong growth, which is good news and proves that the Schaeffler Group is on track for sustainable growth. Particularly noteworthy is the encouraging development of our Industrial division, which grew by 5.7 % at constant currency in 2017, almost as much as our Automotive division with growth of 5.9 %. I would also like to highlight the above-average performance of our Greater China region over many years. Revenue there rose by around 24 % at constant currency in 2017, making the Greater China region once again our strongest driver for growth.

In accomplishing all this, we did not rest on our successes achieved to date but continued to invest, particularly in the future-oriented areas of E-Mobility and Industry 4.0, without neglecting our traditional core business, however. We continued to gain ground especially in the area of electric mobility. This is reflected not only in the accelerated acquisition of the remaining shares in Compact Dynamics GmbH, but also in the increasing number of customer projects. In addition, the launch of series production in two major projects with Chinese manufacturers at the beginning of this year marks another significant milestone. This clearly confirms that we are on the right track. We will consistently continue along this path. Establishing our globally-oriented separate E-Mobility business division and three competence centers in Buehl, Wooster, and Anting, as well as further expanding our global E-Mobility team, will support us in this. We can also report initial success in realizing our second key opportunity for the future, Industry 4.0. Interest among customers is strong. Effective January 1, 2018, we have set up an independent organizational unit responsible for expanding this important future-oriented business worldwide in which we combine our expertise. Looking for common ground and our decision to become even more flexible and more customer- and market-oriented through our new three-division model and the stand-alone Automotive Aftermarket division are helpful here too.

However, the Schaeffler Group's business is not only made up of E-Mobility and Industry 4.0. We are proud of our core business, which did well in nearly all sectors in 2017. This trend will continue in 2018. One indicator of this is the order intake in our Automotive OEM business, reported externally for the first time in 2017, which increased to around EUR 11.5 billion, or around 1.3 times the revenue generated in 2017. The Industrial division's order book also developed well, especially towards the end of 2017. Thus, all signs are pointing to continued growth.

That brings us to the results for 2017: Even though we were able to grow the Schaeffler Group's consolidated net income to EUR 980 million, which is an increase of around 14 % over the prior year, we can only be partially satisfied with the development of operating results over the course of 2017. With earnings before financial result and income taxes (EBIT) before special items of EUR 1,584 million, our EBIT margin before special items was 11.3 %. This compares to 12.7 % in the prior year. On one hand, the decline in the EBIT margin before special items resulted from temporary operating problems that led to a profit warning and a reduction in our guidance for our EBIT margin before special items from 12 to 13 % to 11 to 12 % in the second quarter. On the other hand, the margin decline is attributable to the additional expenses and investments associated with the implementation of our program "Agenda 4 plus One". These measures are necessary in order to prepare the Schaeffler Group for the future. They will remain with us in 2018 and can be expected to affect our operating profitability. It should not be overlooked, however, that the "Agenda 4 plus One" initiatives and the associated costs and investments over the next few years are designed to generate additional earnings potential that will help to secure the Schaeffler Group's operating profitability in the long term – whether through cost optimization, synergy effects, or revenue increases. This is also the basis for bringing our EBIT margin before special items back to the long-term average of 12 to 13 % and for meeting our Financial Ambitions for 2020, and similarly applies to free cash flow, which amounted to EUR 515 million before cash in- and outflows for M&A activities in 2017.

In this context, I would like to highlight the fact that we have further increased our capital expenditures. In total, the Schaeffler Group invested around EUR 1.3 billion in 2017. This corresponds to 9.1 % of our revenue, a figure well above the medium-term average of 6 to 8 %. We are also proud of the fact that we created around 3,500 new jobs in 2017, approximately 500 of them in Germany. This positive trend has been possible because, being a family business, we think long-term and constantly resort to our proven success factors: Quality, technology, and innovation.

Our net debt continued to decrease over the course of 2017. It currently amounts to approximately EUR 2.4 billion. This corresponds to a net debt to EBITDA ratio for the Schaeffler Group of 1.0x. At the same time, the equity ratio increased from 17.3 % at the end of 2016 to 22.1 %. These indicators demonstrate that the quality of our balance sheet has further improved. Once again, we have regained sufficient financial flexibility to consider selective acquisitions as part of our M&A strategy. This is key to implementing our strategy “Mobility for tomorrow”.

Strategy “Mobility for tomorrow” – “Agenda 4 plus One”

Our strategy “Mobility for tomorrow” is finalized. It is conclusive, and it is understood, accepted, and appreciated by our customers and business partners, as well as by our executives and employees. That is an important prerequisite. However, its implementation is even more crucial. To this end, we launched our Excellence program “Agenda 4 plus One” with 16 strategic initiatives over the course of 2016. Since then we have expanded it to a total of 20 strategic initiatives.

The program “Agenda 4 plus One” owes its name to the fact that it is designed to run for 4+1 years. It is a broad-based approach and we will successfully complete it by the end of 2020. For this purpose, we have set up a program organization that systematically monitors and supports the implementation of the program and each of its initiatives. This also includes regularly determining the implementation status, known as the “completion ratio”. Today, this figure – including the four new initiatives added to the program at the beginning of this year – is around 35 %. This means there is still a lot of work ahead of us.

Equally important as monitoring the progress of implementation are the business cases we have developed for each of the initiatives showing how much extra effort, additional investments, and, of course, additional benefits result from the individual initiatives. This is necessary to demonstrate whether the program pays off financially, which is all the more important because the program encompasses initiatives of very different character: From concrete business initiatives such as “E Mobility” and “Industry 4.0” to initiatives aimed at increasing our operational excellence, designed, for example, to improve and harmonize our groupwide processes (see initiative “Process Excellence”). Enhancing and modernizing our IT infrastructure (see initiative “IT 2020”) is essential to successfully carrying out this undertaking. Of course, “Agenda 4 plus One” also includes our "Digital Agenda", with which we intend to make the Schaeffler Group fit for the digital age and which, together with the “E-Mobility” and “Industry 4.0” initiatives, represents one of our key opportunities for the future. Due to its significance, the “Digital Agenda” practically represents a program within the program.

Addressing all 20 initiatives would be beyond the scope of this foreword. Therefore, I would like to use just one of them as an example that has been of particular interest to us in 2017 and which is of fundamental importance to the Schaeffler Group’s future success: The initiative “Leadership & Corporate Values”.

Leadership & Corporate Values – Leading into the Future

As part of our strategy concept “Mobility for tomorrow”, we agreed in the course of 2016 on four key corporate values based on the “Transparency, Trust, and Teamwork” Leadership Principles adopted in 2014. In 2017, the Executive Board of the Schaeffler Group worked extensively on how to further operationalize this framework and develop it into a conclusive leadership model.

These efforts resulted in our six Leadership Essentials. These are designed and formulated in a way that they can serve as guidelines for all our executives worldwide in their day-to-day management activities. Whether on the shop floor in our plants or at board level, in Germany, or at locations worldwide. Completely in line with our “One Schaeffler” approach. As these Leadership Essentials are particularly important to us, we have decided to choose “Leading into the Future” as the motto for our annual report 2017. See for yourself and read the following interview with Corinna Schittenhelm and myself on the topic of “Leadership”, as well as the details of the six Leadership Essentials on pages i18 to i33 of this annual report.

As members of the Executive Board, we are convinced that we will be able to successfully handle the Schaeffler Group's upcoming transformation process if we lead the way by setting good examples, with a great deal of respect, and the necessary decisiveness. This is especially true in situations in which we cannot always meet all the interests of everyone involved. And this is also true even if we have to accelerate the transformation process further. We want to shape the future, take our employees along on this path, and inspire their enthusiasm for our concept. We will only succeed in this through good leadership. Our new leadership model will therefore become one, if not the decisive factor in ensuring the continued success of the Schaeffler Group in the future. And that is best done together. As One Schaeffler Group. As One team that speaks with One voice.

One Schaeffler – One Team – One Voice
Even though the environment will remain challenging in 2018, we have ambitious plans for the year. On a constant-currency basis, we aim to grow by 5 to 6 % and achieve an EBIT margin before special items of 10.5 to 11.5 %, including the charges resulting from the accelerated implementation of our program "Agenda 4 plus One". On this basis, free cash flow is expected to amount to around EUR 450 million before cash in- and outflows for M&A activities in 2018. In addition, as in the past two years, we intend to pay a dividend of 30 to 40 % of net income before special items. These are ambitious targets – we will do everything in our power to ensure they can be achieved. However, we are not only concerned with short-term financial targets. There's even more to it: We want to prepare the Schaeffler Group for the challenges ahead of us. We want to further improve our image internally and externally, continue to invest, and, above all, create secure and sustainable jobs. We will only be able to do all this if we play an active role in shaping the major changes in the markets and regions in which we operate. If we join forces, continue to grow together, speak with one voice, both within and outside, and act as one Schaeffler Group, as a strong automotive and industrial supplier. That means: "One Schaeffler – One Team – One Voice". That's our goal, and that is what we stand for. In the best interest of our customers, our business partners, and our employees worldwide. And in your interest, of course!

Ladies and gentlemen, dear shareholders, 2017 was a challenging year. We grew faster than expected, especially in the second half of the year. Our net income increased by approximately 14 % compared to the prior year. And despite its reduced level, our EBIT margin of 11.3 % is still favorable compared to our competitors. We have made investments, achieved a great deal, and are working to secure our future. Naturally, this is not always easy. And of course, 2017 has also made us aware of the fact that we have to take an even more forward-looking approach. This also holds true for expectations placed on us from outside. However, that does not change the fact that we are on the right track. Why? Because we combine long-term thinking with innovative strength and orientation toward the future. Because we know what we are capable of. And because we trust in our four core values that characterize the Schaeffler Group as a family business: "Sustainable", "Innovative", "Excellent", and "Passionate".

On this note, and on behalf of all members of the Executive Board of the Schaeffler Group, I would like to extend my sincere thanks to our family shareholders, to the members of the Supervisory Board, and to you for your constructive and trustful cooperation in 2017. Special thanks go to our now more than 90,000 employees around the world whose excellent and hard work generated the successes of 2017. I look forward to continuing our collaboration in the future.

Yours sincerely,

Klaus Rosenfeld
Chief Executive Officer

Executive Board

Dr. Yilin Zhang
Regional CEO Greater China

Matthias Zink
CEO Automotive OEM

Klaus Rosenfeld
Chief Executive Officer

Prof. Dr. Peter Pleus
CEO Automotive OEM

Bruce Warmbold
Regional CEO Americas

Prof. Dr.-Ing. Peter Gutzmer
Deputy CEO and Chief Technology Officer

Andreas Schick
Regional CEO Asia/Pacific

Dr. Stefan Spindler
CEO Industrial

Corinna Schittenhelm
Chief Human Resources Officer

Dietmar Heinrich
Chief Financial Officer

Oliver Jung
Chief Operating Officer

Jürgen Ziegler
Regional CEO Europe

Michael Söding
CEO Automotive Aftermarket

Leading into the future

Reacting faster and with more agility – this is becoming a critical success factor for companies in the digital age. With its new understanding of leadership, Schaeffler is preparing for new challenges such as electric mobility and Industry 4.0.

At the beginning of the 20th century, Antarctica was still “Terra Nova”, uncharted territory of which most people had only vague ideas. On December 14, 1911, Roald Amundsen became the first person to reach the South Pole, and afterwards he and his team returned to their Norwegian homeland safe and sound. The success of the polar explorer was not only the result of a sophisticated strategy, but was above all due to its consistent implementation under his leadership. For example, in the face of many doubts he decided in favor of an anchorage that was much closer to the geographical South Pole than that of his rival Robert Scott, whose expedition tragically failed.

Schaeffler also needs to conquer new territory. After all, the automotive industry and all of the suppliers’ other target industries are facing radical change. Schaeffler reacted to this situation at an early stage with its strategy “Mobility for tomorrow”. But what is true of every journey applies here as well: The approach alone is of little avail if it isn’t implemented correctly. The Schaeffler Group therefore launched the excellence program “Agenda 4 plus One” as part of its strategy. It is designed to not only increase the company’s customer focus, operational excellence, and financial stability, but in order to also improve competitiveness and increase corporate value in the long term, the Agenda explicitly addresses the topic of “leadership and talent management”. One of now 20 group-wide initiatives included in the program is entitled “Leadership & Corporate Values”.

At the heart of the initiative are Schaeffler’s values, leadership principles, and Leadership Essentials. The values of the listed family company were revised two years ago with the involvement of a great number of employees:

- **Sustainable:** A long-term view and continuity will foster the growth of the Schaeffler Group, thereby enabling a future worth living.
- **Innovative:** For (nearly) every problem there is a solution. If not, we will create one!
- **Excellent:** We develop solutions that are of the highest quality based on our extensive expertise.
- **Passionate:** Our biggest driver is our passion for innovative technologies and joint success with our customers.

These values form the basis for all of Schaeffler’s entrepreneurial activities and are the starting point for a new leadership culture that, on one hand, promotes speed and dynamism so that the new challenges can be met, but at the same time also preserves the company’s identity on the other. It is the task of every leader at Schaeffler to ensure in their areas of responsibility that these values are brought to life. Three Leadership Principles are derived from this:

- **Transparency:** Decisions and objectives are transparent for employees at all times. This includes open dialog and constructive feedback at all levels.
- **Trust:** Dealing with each other is based on mutual respect and trust.
- **Teamwork:** Achieving excellent results requires the expertise of all employees which they actively contribute in result-oriented teams.

Sustainable
A long-term view and continuity will foster the growth of the Schaeffler Group, thereby enabling a future worth living.

Innovative
For (nearly) every problem there is a solution.
If not, we will create one!

Excellent
We develop solutions that are of the highest quality based on our extensive expertise.

Passionate
Our biggest driver is our passion for innovative technologies and joint success with our customers.

Corporate values

Leadership Principles

Leadership Essentials

Our Corporate Values – sustainable, innovative, excellent, and passionate – provide identity and direction for all employees and are the components of Schaeffler's DNA. They describe who we are and who we want to be in the future, based on our heritage. Our Corporate Values are not only our internal benchmark, but also describe how we want to be perceived by others.

Our Leadership Principles define our aspiration and what the results of leadership should feel like: We want to work in an organization that is characterized by trust, transparency, and teamwork.

Our Leadership Essentials specify critical leadership behaviors by describing how people at Schaeffler lead and drive the business success. They help our leadership in making better trade-off decisions in everyday business and thus make our organization stronger.

»Our future viability also depends on whether we succeed in establishing a leadership style that allows sufficient freedom.«

CORINNA SCHITTENHELM,
Chief Human Resources Officer

Our Leadership Principles represent a goal for good leadership. Since the end of 2017, they have been accompanied by six Leadership Essentials that describe how executives at Schaeffler should act. Every action and every decision in day-to-day business must be measured against these essentials. This applies not only to leaders with disciplinary responsibilities, but to anyone who assumes leadership – for example in projects such as the development of a product for volume production or the introduction of a new IT standard.

These Leadership Essentials play a key role in the further development of Schaeffler. It was therefore clear from the outset that if they were to have the desired effect, they could not simply be dictated by the Executive Board. Hence, they were developed using a multi-stage process which started with individual interviews with leaders from all hierarchical levels that were conducted by Human Resources. Additionally, an online employee survey was conducted. The results in brief: For Schaeffler to be well prepared for the challenges of the future, leadership concepts must change. Leadership should no longer concentrate mainly on problem-solving instructions, but rather the further development of the company's own employees should become the focus of attention. To develop Leadership Essentials in line with this understanding, workshops were held in all regions during the first half of 2017. Based on the results of these workshops, the company's top management discussed the Essentials at the annual executive meeting before they were ultimately adopted.

Late 2017 saw the company-wide implementation of the Leadership Essentials, accompanied by targeted communication measures throughout the group. Their objective is that not only executives, but all employees worldwide should know and understand the new guidelines. In order to give the necessary weight to this topic, CEO Klaus Rosenfeld holds many personal discussions at various locations, including with junior management staff. An employee survey on the subject of leadership is carried out to check whether the communication goals are being achieved. With the introduction of its Leadership Essentials, Schaeffler is also changing the standards by which the performance of executives is measured. While the focus has so far been on achieving agreed-upon targets, annual perfomance appraisal meetings will in future also cover how targets are reached.

The new Leadership Essentials are also intended to help maintain Schaeffler's attractiveness as an employer for specialists and managers in the long term. "For young talents, it matters whether their own manager is promoting their development", says Corinna Schittenhelm, Chief Human Resources Officer. "Our future viability also depends on whether we succeed in establishing a leadership style that allows sufficient freedom."

However, Schaeffler employees are not the only ones who benefit from the new leadership culture – it especially hold benefits for customers as well. Schaeffler's business is constantly growing more complex: The company currently develops complete electric axle drives and intelligent, self-monitoring bearings for industrial applications. This is only possible if all players within the company *connect for success* (p. i22). Furthermore, globalization is increasing prosperity in all regions of the world – and with it the quality demands of customers. These can only be met in a global production network if courageous decisions are made locally and employees *take on responsibility* (p. i24). Since innovation cycles are becoming ever shorter in the digital age, a technology leader such as Schaeffler must introduce new forms of work and innovative processes. In particular, the cooperation with start-ups and business incubator forums can help *drive the change* (p. i26). However, experiments are unacceptable when it comes to keeping promised delivery deadlines to customers – for example, because

OUR LEADERSHIP ESSENTIALS

Connect for success
We all have both the aspiration as well as the responsibility to continue Schaeffler's success story. We aim to excel to the top in certain businesses and maintain our position where we are already leaders. This is only possible if we cooperate seamlessly across our regions, businesses, and functions.

Manage for results
Result orientation is part of our DNA. This "promise and deliver" attitude is something we need to keep and further build on. A stronger focus on customer requirements and increased efficiency will be vital in serving their articulated and anticipated needs.

Take on responsibility
Every day, leaders are required to make decisions, with varying degrees of difficulty and risk. Taking and standing by those decisions is an essential component of leadership that should be carried out consistently.

Care for people
The commitment and expertise of our employees are key to the future success of our company. Therefore, we need to ensure that our leaders not only help their teams to develop new skills, but also provide an inclusive working environment that encourages and acknowledges creativity.

Drive the change
In recent years, our industry has experienced incredible technological development at an ever-increasing pace – a trend that is set to continue. Therefore, all leaders need to drive innovation and engage our employees to develop and implement new ideas.

Empower your team
Leaders need to be able to focus on the most important tasks at hand. To realize our maximum potential, we need to empower others and we have to trust in them to do a good job.

production or even just a car would come to a standstill without a certain spare part. *Manage for results* (p. i28) is therefore a key guideline for Schaeffler's business activities. New technologies such as electrified drives or digitally interconnected industrial solutions require solid training and ongoing further education for employees. *Care for people* (p. i30) therefore means that Schaeffler must also use the highest international standards of vocational training and education. The boss as sole decision-maker cannot cope with an increasingly complex world, especially not when volume production of an innovative product is launched at a new plant and many technical and organizational challenges must be met at the same time. The ability to *empower your team* (p. i32) therefore becomes a key qualification.

The examples on the following pages show that the six Leadership Essentials have already been brought to life at Schaeffler today. Thus, a crucial prerequisite for conquering uncharted territory – whether in electric mobility or Industry 4.0 – is now in place.

»Leadership requires courage«

The implementation of the newly defined leadership essential guidelines is a top priority for Schaeffler's management. Chief Executive Officer Klaus Rosenfeld and Corinna Schittenhelm, Chief Human Resources Officer, discussed the topic of what characterizes good leadership.

"Leading into the Future" is the guiding theme of Schaeffler AG's annual report for 2017. What do you mean by that?

KLAUS ROSENFELD (KR): As is the case with many other companies, the rapidly changing market conditions and competitive environment we are currently experiencing require that we realign the Schaeffler Group for the future. Our strategy concept "Mobility for tomorrow" and the excellence program "Agenda 4 plus One" with its 20 initiatives serve as the basis for this further development. Any major transformation requires the involvement of a suitable leadership model. Having laid the necessary foundations for that internally in 2017, it was time to communicate the leadership issue to the outside world. This is why we chose "Leading into the Future" as the motto for our annual report.

"Leadership & Corporate Values" is one of the central initiatives within our "Agenda 4 plus One" and you, Ms. Schittenhelm, are responsible for it. What's it all about?

CORINNA SCHITTENHELM (CS): The "Leadership & Corporate Values" initiative launched at the beginning of 2017 is a central component of our transformation program. In order to have our employees successfully accompany us in the upcoming change process, we provide a framework for our executives that shows them what we understand good leadership to be and how this should be reflected in day-to-day management behavior. Our six Leadership Essentials, and the behavioral examples embodied therein, describe what constitutes excellent leadership at Schaeffler. What do we expect from our executives? How do we want them to behave and how do we lead our employees into the future? By holding workshops in all regions of the Schaeffler world and involving executives from all levels, we jointly examined where we are already excelling at the present time and where we need to improve. Based on the results of this interactive and global collaboration, six Leadership Essentials have been defined, including the associated behavioral descriptions.

In addition to the six Leadership Essentials, the Schaeffler Group's leadership model also includes three superordinate Leadership Principles. How does that fit together?

KR: When I was appointed Chief Executive Officer, a sign was needed that things were going to change. I was mainly concerned with trustful interaction, fewer silos, increased transparency, and more teamwork. On this basis, we created the triad of "transparency, trust, and teamwork." This was the starting signal, so to speak, for the cultural change we initiated in 2014. Since this triad has lost none of its relevance even today, we have included it in our leadership model as so-called Leadership Principles. In this way, these principles complement our new Leadership Essentials.

»As a manager, it is important for me to encourage my employees, position them according to their strengths, and support them.«

CORINNA SCHITTENHELM,
Chief Human Resources Officer

Without any doubt, leadership is also a cultural issue. This cannot be achieved without a foundation of values. What values does the Schaeffler Group stand for?

KR: Schaeffler is a family business that is shaped by its founders' and shareholders' way of working and thinking. We want to preserve and cultivate this foundation of values. When developing our strategy concept "Mobility for tomorrow," we therefore agreed on four key corporate values: "Sustainable," "Innovative," "Excellent," and "Passionate." These four values form the eighth pillar of our strategy. They are also the basis for the "Leadership & Corporate Values" initiative.

Back to business: The Schaeffler Group now has more than 90,000 employees. What are you doing to ensure that the six Leadership Essentials are indeed brought to life at Schaeffler worldwide?

CS: Human Resources supports the worldwide implementation of the new leadership concept. The Leadership Essentials will be reflected in all HR processes and tools. For example, they play a crucial role in the selection and development of executives. And we gear all management training courses toward the defined essentials. In addition, we are currently testing the introduction of what is known as upward feedback. During the course of a moderated workshop, employees provide feedback to their own superiors about how they experienced their behavior over the past year, measured by the Leadership Essentials. Furthermore, workshops are currently being held to make the Leadership Essentials and the associated leadership behavior tangible at all management levels. And of course, the picture would not be complete without appropriate consequences. In our annual Global Talent Reviews, we will now be discussing and evaluating leaders according to the desired behavior – so now how they achieve their results is also important. This is how we align our HR processes and tools to the newly defined Leadership Essentials. But this is still no guarantee for a change in management culture that is a living and breathing entity! Whether all this will be successful ultimately depends on each individual leader and on as many good role models as possible.

It will take time to sustainably anchor the new Leadership Essentials in the company. How much time are you allowing for that and when should the process be completed?

CS: The implementation of our "Leadership & Corporate Values" initiative is planned for 2020. But of course, clearly the implementation of a new leadership culture will not end on a particular date. It's an ongoing process. Our executives are expected to constantly measure their leadership behavior against the defined essentials and align it accordingly. In 2017, our focus was on defining and developing the Leadership Essentials; from now on, we will turn our attention to communicating and implementing this new understanding of leadership. This will include the described adjustment of HR processes and tools. Additionally, we must also enable our executives to embrace and display the new, desired leadership behavior – on a permanent basis.

If you want to make a lasting change, you must have thought about the prerequisites too. What are you doing to make your initiative a success?

CS: The key lever for me is that every individual executive considers the question of what the Leadership Essentials in his or her own area of responsibility mean for him or herself. To what extent do I myself live up to this claim, and where can and do I want to change my behavior? We have initiated two measures to kick off this process of self-reflection: One is a workshop involving executives and their direct employees. These workshops, which incidentally first started at board level, reflect on how good the respective team already is in implementing the essentials. The second measure is the so-called "Leadership Roadshow," in which members of the Executive Board exchange views on the implementation of the Leadership Essentials with executives at all levels in the regions and divisions. As the Executive Board, we make it absolutely clear how important this issue is to us and that this is not a short-term course of action. And we learn from other executives about their perception and ideas on leadership – and what we can improve together.

»For me, being a role model, showing respect, and having courage are the three fundamental elements of good leadership. These same elements are equally important when facing major transformations.«

KLAUS ROSENFELD,
Chief Executive Officer

What role does communication play in this context?

KR: Communication plays a vital, if not decisive, role. Those who don't like to communicate have a hard time leading people well. Leadership communication should always be direct, clear, and provided with minimal delay. And it should be consistent. Among other things, we regularly send out notifications from the CEO to all employees. The contents are agreed upon beforehand by the Executive Board. What counts for us here is: "One Schaeffler – One Team – One Voice."

But leadership always has a personal element. How would you describe your own leadership style?

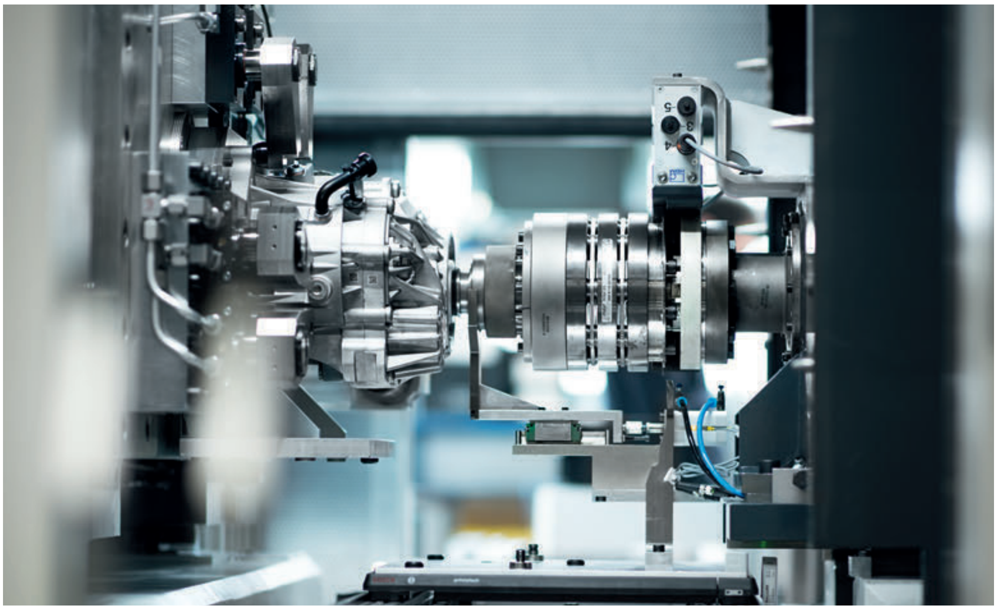
CS: As a manager, it is important for me to encourage my employees, position them according to their strengths, and support them. I communicate my expectations very clearly – but I rarely tell them how to proceed. In my opinion, employees can develop only if they are given the scope to do so. A recent upward feedback confirmed this leadership behavior, reflecting that I am authentic and approachable and that I allow my employees a lot of freedom in handling their tasks.

In times of major changes, a CEO has a special leadership responsibility. How do you deal with that? What is your concept of good leadership?

KR: According to my understanding, leadership must always center on people. This can only be done with a certain amount of empathy. In addition, the person bearing leadership responsibility should be a good role model. Great respect for those who want or have to be led is a vital part of leadership. This is not always easy, especially in day-to-day business. But it is an inseparable prerequisite for successful leadership. Leadership also requires courage. The courage to take on responsibility and make decisions. Especially uncomfortable decisions. For me, being a role model, showing respect, and having courage are the three fundamental elements of good leadership. These same elements are equally important when facing major transformations.

CONNECT FOR SUCCESS

Countdown for the electric axle



»We have received very positive feedback from our customer regarding our collaboration.«

MICHAEL BERGER,
Project Manager

Production of the first transmission module for an electric axle drive was launched at the end of December 2017. It is thanks to the close collaboration between Schaeffler engineers from Germany and China that the project succeeded despite the tight schedule.

Michael Berger and Chen Peng are separated by about 8,700 kilometers as the crow flies. But the two project managers share a common mission: launching volume production of Schaeffler's first electric axle drive for a Chinese customer. They talk on the phone almost every day and have seen each other in person dozens of times. "We have received very positive feedback from our customer regarding our collaboration," says Berger, who assumed project management responsibility for the development of the electric axle drive at Schaeffler three years ago. He didn't have any China-related experience, but he knew right from the start: "I need my Chinese colleague, not only as an interface with regard to the customer, but also to manage local R&D activities in Anting near Shanghai."

Collaboration between the two teams in Anting and Herzogenaurach enabled Schaeffler to rapidly respond to customer requests. For instance, it allowed components to be analyzed on site within just two days following driving tests. The company's best experts were involved in evaluating the results of such returns analyses. Software development was carried out on a transnational basis as well: While Chinese Schaeffler experts took part in the customer's winter tests, Schaeffler Engineering programmers from Werdohl contributed their knowledge and expertise behind the scenes. They had previously developed the functional software, working closely with colleagues from Buehl, who were responsible for the gear shifting actuator.

Collaboration was also particularly important in terms of production planning. After all, the axle drive envisaged for China is a high-tech product in every respect. It features a shiftable two-speed gearbox, which allows the electric motor to be used even at high driving speeds. What would place the highest demands on manufacturing precision in a "normal" car poses an even greater challenge when it comes to electric driving. If there were any audible noise, this would not be drowned out by the internal combustion engine. A large part of the production facilities had to be developed from scratch by Schaeffler's own Special Machinery department, because the company had never before manufactured such a drive system. As a result, it was decided at an early stage: Production launch will take place in Herzogenaurach, and only when everything is running smoothly will the machines be relocated to the Taicang plant in China.

For Berger, working collaboratively does not mean avoiding conflicts for the sake of harmony, but rather ensuring that roles are clearly defined. "It is completely clear to me that our Chinese colleagues do everything they can to satisfy our customer," he says. "But it is also important to keep an eye on the interests of the company as a whole." In his opinion, there's only one thing that helps in such cases: Reaching for the phone and developing a common strategy for action.

TAKE ON RESPONSIBILITY

Quality made in India

Zero defects. Such an ambitious goal can be achieved only if someone takes responsibility for it. Just like Jayanta Nath, who works at the Vadodara plant, Schaeffler's largest location in India, which manufactures industrial bearings to the highest standards of quality.

QUALITY ASSURANCE AT SCHAEFFLER'S VADODARA PLANT

10%

increase in quality in Vadodara each year

The industrial bearings from Vadodara in India are regarded as the vanguard for manufacturing quality in Asia throughout the group.

Making decisions. For Quality Manager Jayanta Nath, this is part of his day-to-day business. The demands regarding the manufacturing quality of components are increasing as a result of ever more efficient vehicles and industrial installations and, on top of this, they are also subject to constant change. This is also true for the bearings produced by around 2,000 employees at Schaeffler's Vadodara location, about 400 kilometers north of Mumbai. Destined for wind turbines, machinery, aircraft, and rail vehicles, they must leave the factory in perfect condition to guarantee heavy-duty performance with minimal maintenance requirement. Demands on quality today are more stringent than ever before.

When it comes to especially challenging projects, Nath therefore sets up a "Quality War Room", a central area where all threads converge during volume production launch. Here, an interdisciplinary team consisting of production, quality assurance, maintenance, and process engineering specialists continuously analyzes the manufacturing process and directly develops solutions for any problems that arise. For example, they decided to install a camera system to ensure that every bearing contains the correct number of rolling elements. As a result, the industrial bearings from Vadodara production are regarded as the vanguard for quality in Asia.

"There are two ways to prevent a mistake," explains Nath, "the first is preventing it right from the outset. The second comes into play should the first method fail: If an error does occur nevertheless, it must be detected in good time." For Nath, who has been working as an engineer at Schaeffler for around three years, this means above all that he must constantly work on optimizing the manufacturing quality and strive for improvement. Schaeffler has established this in its "Fit for Quality" initiative. Thirteen teams in Vadodara are working to improve the quality of every single process step and procedure.

They are supported by Schaeffler's corporate quality management, with whom Nath coordinates on a monthly basis. The success of this work is evaluated, for instance, by means of key performance indicators on customer complaints and internal non-conformity costs. One result: For several years now, the defect rate in Schaeffler's largest Indian plant has decreased by ten percent annually.

Taking on responsibility: For Nath, this means making decisions, even if it takes courage and willingness to accept a certain risk. "The biggest challenge in decision-making is by no means the danger of choosing the wrong direction," says Nath, "but rather, it's not making decisions at all." And if executives can convincingly explain these decisions to their team, there's a good chance that everyone involved will embrace them. In Nath's opinion, this is the best prerequisite for success.

Innovation cycles are becoming shorter and shorter, technical progress is accelerating. Established technology leaders must speed up their processes. Here they can learn a thing or two from start-ups. Prof. Dr. Tim Hosenfeldt brings Schaeffler together with incubator centers in Nuremberg and Berlin.

DRIVE THE CHANGE

Room for new ideas

Digitalization, interconnection, new business models: In a world that is changing faster than ever before, technology leaders such as Schaeffler are facing new challenges. Many of the processes that have been in place thus far are proving to be too slow as the pace of innovation keeps gaining momentum. However, the path to innovation is long and ranges from identifying key issues to marketing the finished solution. Many obstacles must be overcome along the way. For Tim Hosenfeldt, this is the reason why companies themselves must change as well.

In his role as Senior Vice President Corporate Innovation at Schaeffler, Hosenfeldt wants to drive these changes forward. One important goal in this regard is to transform the findings acquired through applied research into marketable products. With the "Schaeffler Hub for Advanced Research" (SHARE) established at universities in Karlsruhe, Erlangen-Nuremberg, Singapore, and Chengdu, Schaeffler has laid the foundation for rapid knowledge transfer. To create room for new ideas within the company, Hosenfeldt also relies on learning from the fast and agile approach of start-ups.

He has identified the new "Zollhof Tech Incubator" in Nuremberg as a suitable location for this mission. The digital start-up center sees itself as the nucleus of innovation and is focused on fledgling business enterprises in the IT scene, which meet here with large companies from the region. Schaeffler is a founding member of Zollhof and not only rents out inexpensive workspace to start-ups, but also participates in scene events such as hackathons and so-called "TechSpace Hackdays", where young companies present the prototypes of new products. "With their fresh and uncomplicated approach, start-ups in particular often offer impressively simple solutions," emphasizes Hosenfeldt.

Breaking out of one's own four walls: This also applies to Schaeffler's commitment to Factory Berlin. For about a year now, Schaeffler has been a partner of what is Germany's first and largest start-up campus. On more than 16,000 square meters of office space, young start-ups can get together with established technology companies. "Here, our project teams glean many ideas from other disciplines on common topics such as digitalization, sensor technology, machine learning, and urban mobility," reports Hosenfeldt. "At the Factory, they also acquaint themselves with new forms of collaboration which do not stop at traditional company boundaries."

Despite all the technology, it is always ultimately people who implement innovations. "The necessary changes cannot be effected within a company from the outside," stresses Hosenfeldt. "You have to kindle people's enthusiasm for new ideas, bring them on board, and make them ambassadors of change." To achieve this objective, the project teams from Corporate Innovation work closely with the individual Schaeffler departments across all divisions. This is the only way to turn an idea into a marketable and successful product.

MANAGE FOR RESULTS

In the right place at the right time

Being able to deliver at all times is the key to success in the automotive aftermarket. But only those who ensure transparency will achieve perfect results along the complex supply chain.

Michael Junker finds the term “spare parts” totally insufficient when it comes to describing the products offered by Schaeffler’s Automotive Aftermarket. “We offer complete repair solutions,” explains Junker, who is responsible for managing the global supply chain in the Automotive Aftermarket division. One solution, for example, means not merely supplying just one individual double clutch, but also including along with it the necessary accessories such as guide sleeves, snap rings, or engagement bearings to form a complete package. And customers can even order the appropriate tool set from Schaeffler. No repair shop appointment should take longer than planned – even though Schaeffler itself does not supply repair shops. Its customers are distribution companies and the aftermarket divisions of vehicle manufacturers. “Our mission is to accurately estimate demand in order to be able to deliver at all times without building up large inventories.” This is easier said than done, because the individual components contained in a repair solution are manufactured both by Schaeffler plants and external suppliers. The lead time from order to delivery is at least 30 days, while the call-off can take place within just a few days or even hours as an express delivery.

Managing the overall process is extremely complex, as Michael Junker and his team have to rely on many internal and external stakeholders. A sophisticated system of key performance indicators is just an essential management tool. “It’s not enough, however, to define some indicators,” says Junker. “To ensure that everyone is working in the same direction, we must make these indicators transparent across all levels of management and include them in an overall system.” This is especially important in challenging situations. “In such situations especially, we as a management team focus on the key indicator in question. For example: What is our current warehouse performance? Ultimately, this has always led to success.”

CENTRAL HUB

180 million euros is the sum the Automotive Aftermarket division is investing in the construction of a new assembly and packaging center in Halle (Saale).

40,000

different items for passenger cars, light and heavy commercial vehicles, and tractors pass through the process.

Three essential process steps:

1 › 2 › 3

1. Combining individual components to form a repair solution
2. Packaging
3. Shipping

For Junker, a focus on results also requires an open error culture. “As an organization, we can draw the right conclusions and constantly continue to develop further only if we communicate errors openly and transparently and do not point our fingers at others.” Part of this continuous development is a 180-million-euro investment in a central assembly and packaging center in Halle (Saale), which will allow customers to benefit from even faster deliveries. In addition, Michael Junker is working on improving forecasting quality by using intelligent analysis tools – not in the context of complex large-scale projects, but through small yet continuous steps. “This is the only way to find out what works and what doesn’t,” he says. Sustainably good results are the product not only of current perfect processes, but also of constantly challenging and fine-tuning these processes.

CARE FOR PEOPLE

Systematic talent development

Schaeffler's plant in Wooster, Ohio, has been designated as a center for advanced e-mobility. Beyond machines and systems, this requires highly qualified employees. Which makes it a task for Carrie McKelvey, who heads the Schaeffler Academy at the plant with programs modelled on the German apprenticeship system.

»The company's goal is to find the right people and provide opportunities to enhance their skill sets.«

CARRIE MCKELVEY,
Head of Schaeffler Academy

Spearheading the transition into the age of electric mobility: This is the new focus at Schaeffler's manufacturing plant in Wooster, Ohio. Currently, the facility primarily manufactures torque converters and lock-up clutches for automatic transmissions. Beginning in 2018, however, Wooster will also be producing hybrid modules for a major U.S. automobile manufacturer. To that end, Schaeffler is investing approximately 60 million dollars to expand the site's manufacturing capacity and add office space. However, it is equally important to invest in the 2,000 employees who work at Wooster. After all, new technologies also require new qualifications, for example in the field of electrical engineering.

Carrie McKelvey has experienced the importance of continuous training in her own career. After graduating from college, McKelvey joined Schaeffler in Wooster in 2000, where she completed the rigorous Leadership Training program. Today, McKelvey is the head of the local Schaeffler Academy, where she is responsible for the on-site training and qualification of employees – which is a process that begins at a surprisingly early age. McKelvey and her team regularly visit Wooster-area high schools to kindle the young students' enthusiasm for Schaeffler's preparatory "Pre-Apprentice" program. Over the course of a year, selected students are able to make numerous visits to the Wooster plant, giving them hands-on insights into professional life. Upon graduation, they can enter into a three-and-a-half-year apprenticeship program that teaches them trades such as tool and die maker, machine repair and electrical maintenance. "Such training programs, which cover both theory and practice, are not yet widespread in the USA," says McKelvey. "This gives us the opportunity to attract the brightest talents to our company and systematically develop their skills."

Through the Schaeffler Academy, McKelvey is also able to offer college students the "Cooperative Education Program". This "integrated degree program", which curriculum is comparable to Germany's combines formal university studies with a substantial amount of practical experience. This career-development model is in high demand, as evidenced by the 150 students who actively participate in the program each year. Of course, learning does not end once a full-time position has been secured. The Schaeffler Academy offers customized professional development programs and workshops for all employees. Internal training can take place either on the job or outside the usual working environment in half-day or full-week intensive training sessions.

"The company's goal is to find the right people and provide opportunities to enhance their skill sets," says McKelvey. Now that Wooster is helping to lead Schaeffler into the age of electric mobility, this applies more than ever.

EMPOWER YOUR TEAM

Teamwork for thermal management modules

Josef Kořístek sets up a new production line for thermal management modules at Schaeffler's new Svitavy plant in the Czech Republic in 2017. Teamwork is called for – from individual employees to team and production leaders right up to the plant management.

Building production facilities, eliminating growing pains, allocating staff as needed: Setting up a new production facility is a multifaceted project. This is also true for regard to Schaeffler's new plant in Svitavy, Czech Republic, which is located about 220 kilometers east of Prague. For segment managers such as Josef Kořístek, two things are particularly important in this context. Firstly, always keeping track of things and setting the right priorities: What should be done next? And secondly, it is crucial to master the challenges ahead by working together as a team.

One of the first tasks for Kořístek and his team is to construct a production line for thermal management modules to be used in engines made by a major Japanese automobile manufacturer. The modules control heat distribution in the engine. The goal is to heat up the right areas in the engine as quickly as possible and thus reduce fuel consumption and the engines' CO_2 emissions. Several thousand of these modules are to be manufactured in Svitavy every day and then shipped to Japan.

»We need an environment in which everyone can say what's on their mind.«

JOSEF KOŘÍSTEK,
Segment Manager

Kořístek gets to work. He sets up the production line in collaboration with assembly and injection molding specialists, works through the individual production steps with colleagues from quality assurance, discusses logistics processes with material requirement planners, and gradually puts together the team together with his production manager. “Our job was to set up production from scratch to comprise three shifts, each consisting of 30 people, all within a relatively short period of time so that we could supply the volumes our customer needs,” reports Kořístek. “This sort of thing only works if everyone gets involved, from myself, to production and team leaders and every single employee, also including the corporate departments, which take care of employee training and education.”

For Josef Kořístek, teamwork means one thing above all: Trust and mutual respect. To build trust, each individual employee must feel that they are taken seriously. “We need an environment in which everyone can say what's on their mind,” emphasizes Kořístek. “It is particularly important to talk about things openly from the very beginning and not to conceal anything, for example because there is not enough time for discussions .” That's why Kořístek meets with each of his employees once a month to discuss the work and tasks ahead. In addition, every quarter there is a round-table meeting with all employees to explain such things as the three-month plan for production or the bonus system, for example.

Kořístek's next goal is to introduce the 5S method. This is a systematic approach that allows employees to design their own workplace in such a way that they can concentrate optimally on value-adding activities. It is up to every individual to decide how they wish to implement this concept. Kořístek is convinced that teams work best when all members feel they are involved.

Schaeffler on the capital markets

In its second year since the listing in October 2015, Schaeffler AG's communication with the capital markets focused especially on further expanding investor relations, increasing transparency toward capital market participants, and communicating its strategy.

1.1 Events 2017

Second investment grade rating from Fitch

On April 25, 2017, rating agency Fitch Ratings published its first rating of Schaeffler AG. Fitch assigned a rating of BBB- (investment grade) to Schaeffler AG with a stable outlook. The bonds were also rated BBB-. Thus, Schaeffler AG is now rated by three rating agencies – Fitch, Moody's, and Standard & Poor's.

Dividend increased to 50 cents per common non-voting share

On April 26, 2017, Schaeffler AG's annual general meeting passed a resolution to pay a dividend of EUR 0.49 per common share (prior year: EUR 0.34; special dividend EUR 0.15) and EUR 0.50 per common non-voting share (prior year: EUR 0.35; special dividend EUR 0.15) to Schaeffler AG's shareholders for 2016. This represents a dividend of 34.1% of net income attributable to shareholders before special items, falling within the dividend payout ratio of 30 to 40% planned by the company.

Earnings guidance for 2017 reduced

On June 26, 2017, the Board of Managing Directors of Schaeffler AG decided to reduce its guidance for the EBIT margin before special items from previously 12 to 13% to 11 to 12% for the business year 2017. This was due to a substantially lower earnings development in the Automotive division in the second quarter of 2017 compared to the prior year. At the same time, the guidance for free cash flow for 2017 as a whole was reduced from approx. EUR 600 m to approx. EUR 500 m. The company confirmed its revenue guidance for the full year 2017. Schaeffler AG continued to expect its revenue to grow by 4 to 5% excluding the impact of currency translation.

"Agenda 4 plus One" with three key opportunities for the future

The Schaeffler Group's Strategy Dialog held on July 10 to 13, 2017, was devoted to the "Agenda 4 plus One" transformation program and the related strategic decisions. One of these was the decision to create an independent **E-Mobility** business division bringing together all products and system solutions for hybrid and pure battery-electric vehicles as of January 01, 2018. Further, the company is setting up an additional competence center for E-Mobility in China, alongside the existing German E-Mobility competence center in Buehl, to accommodate the increasing importance of the Chinese market in the field of E-Mobility. In the Industrial division, the entire industry-specific business with mechatronic systems and digital services as well as the required related components have been combined in an independent organizational unit **Industry 4.0** since January 01, 2018. The strategic decisions were made based on the model of an integrated automotive and industrial supplier and the company's strategy "Mobility for tomorrow" with its three key opportunities for the future – E-Mobility, Industry 4.0, and Digitalization.

Dietmar Heinrich new CFO

At its meeting on July 17, 2017, the Supervisory Board of Schaeffler AG appointed Dietmar Heinrich (previously Regional CEO Europe) to the Board of Managing Directors. On August 01, 2017, Dietmar Heinrich took up his role as Chief Financial Officer of Schaeffler AG, replacing Dr. Ulrich Hauck. The Supervisory Board also decided to extend the contract of Dr. Stefan Spindler, CEO Industrial, for a term of five years ending on April 30, 2023. Jürgen Ziegler was appointed to the Schaeffler Group's Executive Board effective August 01, 2017, succeeding Dietmar Heinrich as Regional CEO Europe.

Schaeffler AG's second capital markets day

On July 20, 2017, Schaeffler AG held its second Capital Markets Day at the Buehl location. The company explained its strategic direction as well as its long-term growth perspectives to 40 investors and analysts. Schaeffler emphasized the key points of its equity story for 2017 which is based on three essential drivers: (1) above-market revenue growth in the Automotive division, (2) continuous profitability improvement in the Industrial division, and (3) strong free cash flow generation to finance further organic growth. Schaeffler AG also reinforced its targets for 2017 and confirmed its Financial Ambitions 2020. The Schaeffler Group intends to grow its revenue – excluding the impact of currency translation – by an average of 4 to 6% per year over the coming years. Further, it plans to generate an EBIT margin before special items of 12 to 13% and free cash flow before cash in- and outflows for M&A activities of approx. EUR 900 m in 2020. On this basis, the company is aiming for earnings per share of approx. EUR 2.00 in 2020. In addition, the group intends to continue to improve the quality of its balance sheet by 2020 and to pay dividends amounting to 30 to 40% of net income before special items to its shareholders.

One Schaeffler India

On August 30, 2017, the Schaeffler Group announced its intention to merge its three subsidiaries in India – Schaeffler India Ltd. (previously FAG Bearings India Ltd.), INA Bearings India Private Ltd., and LuK India Private Ltd. The merger is subject to the required local regulatory approvals and the consent of the minority shareholders. The transaction is expected to close in the third quarter of 2018. The objective of the transaction is to simplify the existing structure, reduce complexity, and create a strong Schaeffler entity in India in order to better realize the potential for future growth in India. The company will be known as "Schaeffler India Limited" and remain listed. The transaction increases Schaeffler AG's indirect interest in Schaeffler India Ltd. from currently approx. 51% to approx. 74%.

IR team strengthened

Renata Casaro assumed the position of Head of Investor Relations of the Schaeffler Group on October 01, 2017. Renata Casaro has over 25 years' experience in equity, currency and interest rate markets and joins the Schaeffler Group from her previous position as Head of Investor Relations of a consumer products manufacturer.

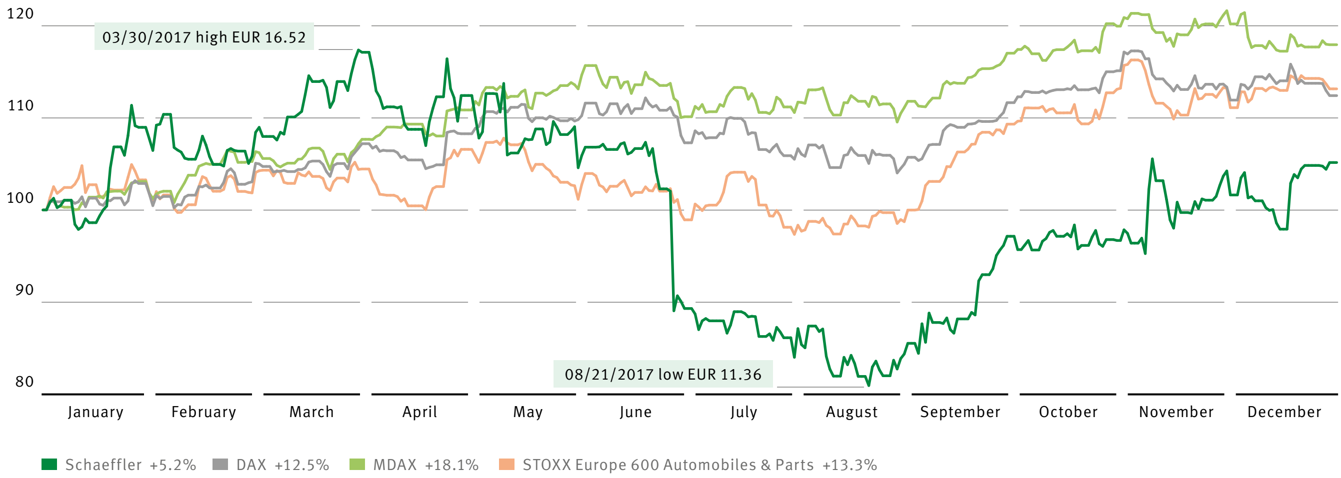
Automotive Aftermarket becomes third division

At its meeting on October 05, 2017, the Executive Committee of the Supervisory Board of Schaeffler AG accepted the proposal of the Board of Managing Directors to separate the Automotive Aftermarket from the Automotive division of Schaeffler AG and to set it up as a third stand-alone division as of January 01, 2018. As a consequence, the Schaeffler Group will divide its business into three divisions – Automotive OEM, Automotive Aftermarket, and Industrial.

On that basis, the Supervisory Board of Schaeffler AG decided to appoint Michael Söding to become member of the Board of Managing Directors of Schaeffler AG effective January 01, 2018. He has assumed responsibility for the Automotive Aftermarket business at board level. Previously, Michael Söding had been Head of Automotive Aftermarket within the Automotive division since 2009.

The three divisions of the Schaeffler Group will in future be managed from decentralized divisional headquarters located in Buehl, Langen, and Schweinfurt. The Automotive OEM division will be headquartered in Buehl. The new Automotive Aftermarket division will be managed from Langen. The Industrial division continues to be located in Schweinfurt. The corporate head office of the Schaeffler Group is in Herzogenaurach.

Schaeffler share price trend 2017
in percent (12/31/2016 = 100)



Source: Bloomberg (closing prices).

Execution of M&A strategy continued

On October 04, 2017, the Schaeffler Group concluded a purchase agreement for 100% of the shares in autinity systems GmbH. The Chemnitz-based IT company specializes in digital machine data recording and evaluation. The acquisition represents another important step in implementing the Schaeffler Group's Digital Agenda and is part of the M&A strategy adopted by the company. The M&A strategy supports the strategy "Mobility for tomorrow" by targeting additional technological capabilities for Industrial and Automotive in seven strategic focus areas.

One year after acquiring a majority interest in Compact Dynamics GmbH, the Schaeffler Group acquired the remaining 49% interest in this company from SEMIKRON International GmbH on December 12, 2017. Compact Dynamics GmbH based in Starnberg is a development specialist in the field of innovative electric drive concepts with a focus on high-performance drives and integrated lightweight construction in small volume production and motor sport applications. The acquisition expands Schaeffler's expertise in the field of electric motors and power electronics for developing and manufacturing electric drives.

1.2 Capital market trends

2017 was characterized by significant gains in the global capital markets, with both the Dow Jones Industrial Average (DJIA) and the Deutsche Aktienindex (DAX) rising to new all-time highs. The main drivers of these increases were the continued expansive policy of the central banks, a recovery of the oil price, and a robust global economy. Exchange rates remained highly volatile, with the euro rising by nearly 15 cents against the U.S. dollar (December 31, 2017: USD 1.20).

The DAX rose by a total of 12.5% in 2017 and closed the year at 12,918 points. This index reached its annual and all-time high of 13,479 points on November 03, 2017. The MDAX was up 18.1% in 2017, rising significantly more than the DAX. While the Euro STOXX 50 increased by 6.5% over the course of the year, it was outperformed by the European sector index, the STOXX Europe 600 Automobiles & Parts, which rose by 13.3%. The DJIA increased significantly in 2017, rising by 25.1% on the back of, among other things, the solid performance of technology equities. The Japanese Nikkei 225 index was up 19.1% by the end of the year.

In early 2017, the global capital markets were still characterized by uncertainties driven by the U.S. elections, the elections in the Netherlands, and the debate surrounding the withdrawal of the United Kingdom from the EU. However, these uncertainties dissipated over the course of the quarter. While the DAX closed the first quarter of 2017 up 7.2% (compared to December 31, 2016), the Nikkei 226 dropped slightly. The DJIA rose by 4.6%, temporarily reaching an all-time high.

Political uncertainty gradually declined in the European Union during the second quarter of 2017, resulting in an overall positive mood in the markets. As a result, the DAX continued its upward trend and temporarily reached its all-time high of 12,889 points on June 19, 2017. However, it lost most of these gains toward the end of the quarter.

Rising geopolitical tension was among the factors keeping global equities markets flat initially in the third quarter of 2017. Positive macroeconomic data and robust company results, however, helped drive share prices up considerably toward the end of the quarter. The DJIA temporarily rose to a new all-time high of 22,413 points on September 20, 2017.

Buoyed by a robust economy, the major global indexes made further gains in the fourth quarter of 2017. The increasing likelihood of comprehensive tax reform in the U.S. also proved a positive influence on the global capital markets. In contrast, the rising euro exchange rate and the persisting geopolitical tension were largely disregarded, especially in Europe. While the DAX and the Euro STOXX 50 maintained their high third-quarter closing level and reached new all-time highs of 13,479 and 3,697 points, respectively, in early November 2017, the DJIA and the Nikkei 225 continued to rally, reaching new all-time highs of 24,838 and 22,939 points, respectively, shortly before the end of the period.

The corporate bond market experienced a positive overall trend in 2017. The iTraxx CrossOver (5 year maturity), an indicator of credit risk in the European high yield market, closed at 233 points on December 31, 2017, compared to 288 basis points on December 31, 2016. The iTraxx Europe (5 year maturity), an indicator of risk in the European investment grade market, also did well. On December 31, 2017, it had dropped to only 45 basis points from 72 basis points on December 31, 2016. Thus, the trend in the bond markets was similarly as strong as that in the equities markets.

1.3 Schaeffler shares

Schaeffler AG's common non-voting shares have been listed on the stock exchange since October 09, 2015. A total of 166 million common non-voting shares are listed for trading.

Schaeffler shares – base data

ISIN	DE000SHA0159
German securities identification number (WKN)	SHA015
Stock symbol	SHA
German stock exchange	Frankfurt Stock Exchange (Prime Standard)
Index	MDAX
Share type	Common non-voting
Number of common non-voting shares as at December 31, 2017	166,000,000
Free float	100% [1]

[1] Approximately 24.9% of total share capital of 666 million common and common non-voting shares (consisting of 500 million common shares and 166 million common non-voting shares).

Schaeffler shares – overview

Schaeffler AG's share capital consists of a total of 666 million shares, including 500 million common shares held by IHO Verwaltungs GmbH that are not listed on the stock exchange. 166 million common non-voting bearer shares have been widely held since April 05, 2016. Thus, the free float amounts to approx. 24.9% of Schaeffler AG's total common and common non-voting share capital.

Schaeffler AG intends to continue to pay a dividend of 30 to 40% of consolidated net income before special items to its shareholders. Both common and common non-voting shares carry dividend rights. Common non-voting shares carry a preferential right to profits consisting of a preferred dividend of EUR 0.01 per share.

The Board of Managing Directors and the Supervisory Board will propose a dividend for 2017 of EUR 0.54 per common share and EUR 0.55 per common non-voting share to the annual general meeting. This represents a dividend of 35.4% of net income attributable to shareholders before special items.

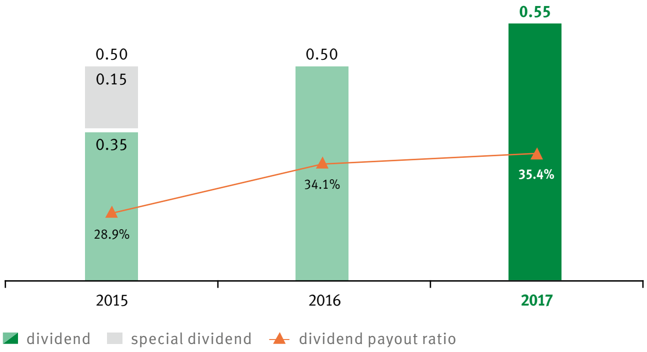
Performance of Schaeffler shares

Schaeffler shares gained 5.2% in 2017, a weaker performance than that of the benchmark indexes, the MDAX (+18.1%) and the STOXX Europe 600 Automobiles & Parts (+13.3%). This was primarily due to the reduced earnings guidance in the second quarter of 2017, which was only partially recovered in the third quarter. On December 31, 2017, the common non-voting shares of Schaeffler AG were quoted at EUR 14.79. The share price reached its high of EUR 16.52 on March 30, 2017, and its low of EUR 11.36 on August 21, 2017.

The daily trading volume averaged 882,843 shares in 2017 (prior year: 675,132). The significant increase in trading volume compared to the prior year period is largely due to the placement of a further 94.4 million common non-voting shares of Schaeffler AG in 2016.

Dividend trend

EUR per common non-voting share



Schaeffler share performance

	2017	2016
Share price at year-end 12/31/ (in €) [1]	14.79	14.06
Share price (high; in €) [1]	16.52	16.25
Share price (low; in €) [1]	11.36	11.62
Average trading volume (number of shares)	882,843	675,132
DAX 12/31/ [1]	12,918	11,481
MDAX 12/31/ [1]	26,201	22,189
STOXX Europe 600 Automobiles & Parts 12/31/ [1]	615	543
Average number of shares (in millions)		
• Common shares	500	500
• Common non-voting shares	166	166
Earnings per share (in €)		
• Common shares	1.47	1.29
• Common non-voting shares	1.48	1.30
Dividend per share (in €) [2]		
• Common shares	0.54	0.49
• Common non-voting shares	0.55	0.50

[1] Source: Bloomberg (closing prices).
[2] For the relevant year, proposed dividend for 2017.

On March 31, 2017, the common non-voting shares of Schaeffler AG were quoted at EUR 16.48, 17.3% higher than on December 31, 2016. This performance considerably exceeded that of the benchmark indexes DAX (+7.2% compared to December 31, 2016) and MDAX (+7.7%) as well as that of the STOXX Europe 600 Automobiles & Parts sector index (+4.5%).

Toward the end of the second quarter of 2017, the share price dropped considerably in response to the reduced earnings guidance for the full year 2017. The common non-voting shares of Schaeffler AG were quoted at EUR 12.54 on June 30, 2017, 23.9% less than on March 31, 2017.

This performance lagged behind that of the benchmark indexes DAX (+0.1% compared to March 31, 2017) and MDAX (+2.3%) as well as that of the STOXX Europe 600 Automobiles & Parts sector index (-5.3%) during the second quarter of 2017.

The share price initially continued to drop in the third quarter, reaching its annual low of EUR 11.36 on August 21, 2017. After that date, however, the shares rallied somewhat and recovered part of these losses, as did many similarly cyclical companies in the capital markets. On September 30, 2017, the common non-voting shares of Schaeffler AG were quoted at EUR 13.65, up 8.9% from the end of the second quarter. Thus, the shares outperformed the DAX (+4.1%) and the MDAX (+6.3%) in the third quarter of 2017, but rose slightly less than the STOXX Europe 600 Automobiles & Parts (+10.6%).

The shares continued their recovery in the final quarter. Gaining 8.3% compared to September 30, 2017, Schaeffler shares fared better than the benchmark indexes, the MDAX (+0.8%) and the STOXX Europe 600 Automobiles & Parts (+3.5%).

1.4 Schaeffler bonds and ratings

The Schaeffler Group had four series of bonds outstanding as at December 31, 2017, three of them denominated in EUR and one in USD. All of the bonds were issued by Schaeffler Finance B.V. in Barneveld, Netherlands.

A further bond series with a maturity of May 2021, a principal of USD 700 m, and a coupon of 4.25% was redeemed in full on May 24, 2017. The redemption was funded using available liquidity and a portion of the Revolving Credit Facility (RCF).

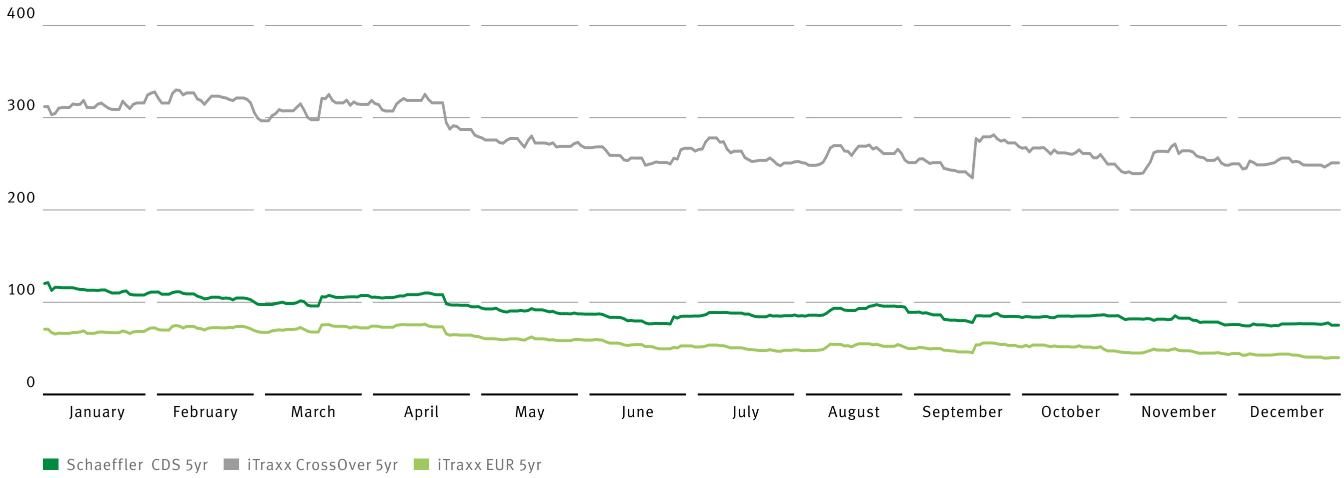
The Schaeffler Group had the following bonds outstanding at December 31, 2017:

Schaeffler Group bonds

ISIN	Currency	Principal in millions	Coupon	Maturity	Price in % [1] 12/31/2017	Price in % [1] 12/31/2016
XS1212469966	EUR	400	2.50%	05/15/2020	101.40	102.30
XS1067864022	EUR	500	3.50%	05/15/2022	102.00	102.96
US806261AM57	USD	600	4.75%	05/15/2023	102.99	101.75
XS1212470972	EUR	600	3.25%	05/15/2025	107.78	106.72

[1] Source: Bloomberg (closing prices).

Credit default swap (CDS) price trend 2017
in basis points



Source: Bloomberg (closing prices).

Performance of Schaeffler bonds

Bond prices remained stable in 2017. The two bond series maturing in 2023 and 2025 rose slightly, which lowered their effective yield. The other two bond series, which mature in 2020 and 2022, declined slightly, approaching the contractual redemption price at which these bond series have been callable since May 15, 2017.

The premiums for Schaeffler AG 5-year credit default swaps decreased from 117 basis points at December 31, 2016 to 76 basis points as at December 31, 2017. Thus, the CDS performed slightly weaker than the iTraxx CrossOver benchmark index, but considerably better than the iTraxx Europe.

Schaeffler ratings

On April 25, 2017, rating agency Fitch Ratings published its first rating of Schaeffler AG. Fitch assigned a rating of BBB- (investment grade) to Schaeffler AG with a stable outlook. The bonds were also rated BBB-.

Standard & Poor's raised the outlook for the company's rating from stable to positive on September 26, 2017. The following summary shows the ratings assigned to the Schaeffler Group by the three rating agencies Fitch, Moody's, and Standard & Poor's as at December 31:

Schaeffler Group ratings
as at December 31

	2017	2016	2017	2016
		Company		Bonds
Rating agency		Rating/Outlook		Rating
Fitch	BBB-/stable	-	BBB-	-
Moody's	Baa3/stable	Baa3/stable	Baa3	Baa3
Standard & Poor's	BB+/positive	BB+/stable	BB+	BB+

1.5 Investor relations

Schaeffler AG maintains open lines of communication on a continuous basis with share- and bond holders as well as with all other capital market participants. In addition to its ongoing road show activities in the major European financial centers as well as in the U.S., the company regularly presents and discusses quarterly and annual results via conference calls.

In 2017, the Board of Managing Directors and the Investor Relations team participated in a total of 10 investor conferences and seven road shows in New York, London, Paris, Amsterdam, Frankfurt, and other places.

The activities of Schaeffler's Investor Relations department also include maintaining regular contact with analysts covering the company and with investors.

Moreover, Schaeffler offers guided plant tours and management discussions at the various Schaeffler locations to interested investors and analysts. In 2017, five such tours and discussions were requested.

The company was covered by analysts representing a total of 19 banks (prior year: 13) as at February 19, 2018. Seven of these banks issued a recommendation of either buy or outperform on Schaeffler AG's common non-voting shares. Their average upside target was EUR 15.30.

Analyst opinions for Schaeffler AG shares [1)]

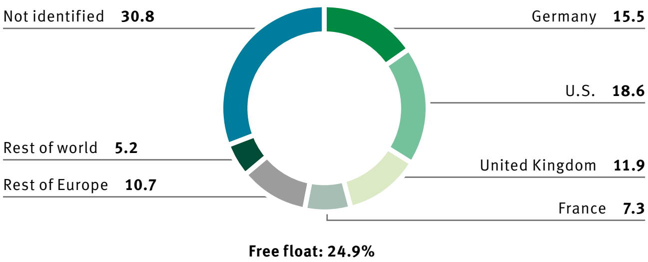
Banks	Recommendation	Price target in €
Bankhaus Lampe	Buy	18.00
Bankhaus Metzler	Buy	17.00
Berenberg Bank	Hold	12.00
BoA Merrill Lynch	Neutral	15.00
Citigroup	Neutral	14.70
Deutsche Bank	Hold	16.00
DZ Bank	Hold	15.00
Exane BNP Paribas	Outperform	16.50
Goldmann Sachs	Neutral	16.50
HSBC	Buy	16.00
J.P. Morgan Cazenove	Underweight	13.00
Jefferies	Hold	15.50
Kepler Cheuvreux	Buy	16.50
MainFirst Bank	Neutral	14.50
Morgan Stanley	Equal-weight	15.00
NordLB	Hold	13.50
Oddo BHF	Buy	15.50
UBS	Sell	12.00
Warburg Research	Buy	18.50

[1)] Recommendations up to February 19, 2018.

1.6 Geographic distribution of free float

The distribution of the institutional free float of Schaeffler's common non-voting shares as at December 31, 2017 was determined using a shareholder identification survey (Share ID). The identification rate was 69.2%, i.e. out of the 166 million common non-voting shares that are widely held, the survey was able to attribute 114.9 million shares to 334 institutional investors in 27 countries. 30.8 million shares were included in trading portfolios, mainly of U.S. banks, as at the reporting date. At year-end, 15.5% or 25.7 million shares were held by institutional shareholders in Germany. The unidentified free float of 30.8% included private investors and others.

Geographic distribution of free float
in percent, as at December 31, 2017



For further detail please contact:

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See back cover for financial calender.

Schaeffler Group

Financial report 2017

Group management report

Combined management report in accordance with section 315 (5) HGB (also referred to as “group management report” or “management report”). The company has chosen to integrate the management report of Schaeffler AG with the following group management report of the Schaeffler Group.

Special items
In order to facilitate a transparent evaluation of the company’s results of operations, the Schaeffler Group reports EBIT, EBITDA, net income, net debt to EBITDA ratio, ROCE, and Schaeffler Value Added before special items (= adjusted).

Impact of currency translation/constant currency
Revenue figures at constant currency, i.e. excluding the impact of currency translation, are calculated by translating revenue using the same exchange rate for both the current and the prior year or comparison reporting period.

Rounding differences may occur.

References
Content of websites referenced in the group management report merely provides further information and is not part of the group management report. This does not apply to the corporate governance report including the corporate governance declaration in accordance with section 289f HGB and 315d HGB, including the declaration of conformity pursuant to section 161 AktG. The reference to the combined separate non-financial report in accordance with section 289b (3), section 315b (3), and section 298 (2) HGB also forms part of the group management report.

Disclaimer in respect of forward-looking statements
This group management report contains forward-looking statements that are based on the Board of Managing Directors’ current estimation at the time of the creation of this report. Such statements refer to future periods or they are designated by terms such as “estimate”, “forecast”, “intend”, “predict”, “plan”, “assume”, or “expect”. Forward-looking statements bear risks and uncertainties. A variety of these risks and uncertainties are determined by factors not subject to the influence of the Schaeffler Group. Therefore, actual results can deviate substantially from those indicated.

1. Fundamental information about the group

1.1 Overview of the Schaeffler Group

The Schaeffler Group (also referred to as "Schaeffler" below) is a global automotive and industrial supplier. Top quality, outstanding technology, and exceptionally innovative spirit form the basis for the continued success of the company. With its approx. 90,000 employees, the Schaeffler Group is one of the leading global technology companies. The Schaeffler Group identifies key trends early on, invests in researching and developing new forward-looking products, and sets new standards in technology. In doing so, it focuses on its key opportunities for the future – E-Mobility, Industry 4.0, and Digitalization. Extensive systems know-how enables the Schaeffler Group to offer comprehensive solutions that are tailored to customer and market requirements. By delivering high-precision components and systems in engine, transmission, and chassis applications, as well as rolling and plain bearing solutions for a large number of industrial applications, the Schaeffler Group is shaping "Mobility for tomorrow" to a significant degree. This includes offering innovative products for hybrid and electric vehicles.

Under its strategy "Mobility for tomorrow", the Schaeffler Group concentrates on 4 focus areas: eco-friendly drives, urban mobility, interurban mobility, and energy chain. These 4 focus areas are based on four megatrends that will influence the business of the Schaeffler Group in the future: climate change, urbanization, globalization, and digitalization. The 8 strategic pillars developed based on these focus areas define the scope for action under the strategy "Mobility for tomorrow" and constitute the basis for the continuous further development of the Schaeffler Group. The excellence program "Agenda 4 plus One" was developed to ensure implementation of the strategy; it now consists of 20 strategic initiatives (prior year: 16) which have been grouped into five categories. In order to consistently implement its strategy, the Schaeffler Group has set itself Financial Ambitions 2020 that mark the financial corridor for implementing the strategy.

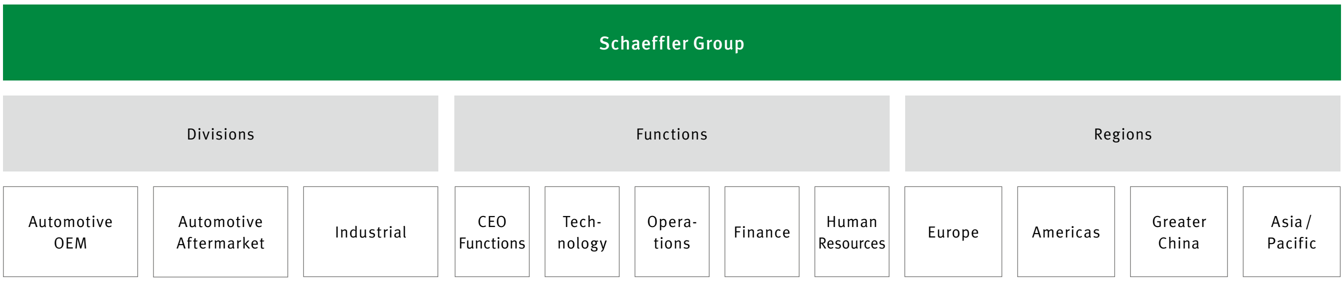
Schaeffler AG's common non-voting shares are listed on the Frankfurt Stock Exchange and are included in Deutsche Börse's MDAX index as well as in the STOXX Europe 600 index. The company's main shareholder is IHO Holding, a group of holding companies owned indirectly by the Schaeffler family that holds all of Schaeffler AG's common shares. The free float amounts to approx. 24.9% of Schaeffler AG's total common and common non-voting share capital. Schaeffler AG intends to continue to pay a dividend of 30 to 40% of consolidated net income before special items to its shareholders.

Organizational structure

The Schaeffler Group's corporate structure is characterized by a three-dimensional organizational and leadership structure which differentiates between **divisions, functions,** and **regions.** Thus, the Schaeffler Group's business is primarily managed based on the divisions, which also represent the reportable segments.

Until December 31, 2017, these divisions consisted of the Automotive and Industrial divisions. While the Automotive division organized its business in the Engine Systems, Transmission Systems, Chassis Systems, and Automotive Aftermarket business divisions, the Industrial division was primarily managed based on the regions Europe, Americas, Greater China, and Asia/Pacific.

Schaeffler Group organizational structure No. 001
since January 01, 2018



Simplified presentation for illustration purposes.

In order to shape the company's future in a fast-changing market and competitive environment and to become even more customer-oriented, the Board of Managing Directors, in cooperation with the Schaeffler AG Supervisory Board, decided, in 2017, to separate the Automotive Aftermarket from the Automotive division of Schaeffler AG and set it up as a third stand-alone division as of January 01, 2018. As a consequence, the Schaeffler Group has been dividing its business into three divisions – Automotive OEM, Automotive Aftermarket, and Industrial – since January 01, 2018. Like the Industrial division, the Automotive Aftermarket division is managed based on four regions. In addition, the company created an independent E-Mobility business division within the Automotive OEM division effective January 01, 2018.

In addition to the divisions, the Schaeffler Group's organizational model includes five functional areas: (1) CEO Functions, (2) Technology, (3) Operations, (4) Finance, and (5) Human Resources. Distribution is embedded directly in each of the divisions. The third dimension are the group's four regions Europe, Americas, Greater China, and Asia/Pacific.

Leadership structure

The Schaeffler Group is managed by the Board of Managing Directors of Schaeffler AG. Up until December 31, 2017, along with the Chairman of the Board of Managing Directors (Chief Executive Officer – CEO), the Board of Managing Directors comprised the CEOs of the Automotive (CEOs Automotive) and Industrial (CEO Industrial) divisions and the Managing Directors responsible for the Schaeffler Group's functions (Chief Technology Officer, Chief Operating Officer, Chief Financial Officer, and Chief Human Resources Officer). Since the Automotive Aftermarket was set up as a separate division effective January 01, 2018, the Board of Managing Directors also includes the CEO Automotive Aftermarket.

The Board of Managing Directors is directly responsible for managing the company, setting objectives and strategic direction, and managing the implementation of the growth strategy taking into account the interests of shareholders, employees and other stakeholders of the company in order to add long-term value. The CEO coordinates the management of the company and the Schaeffler Group.

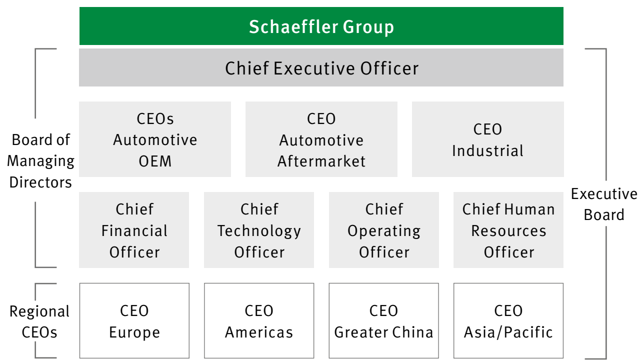
In addition to the divisions and the functions, the group's matrix organization comprises the regions Europe, Americas, Greater China, and Asia/Pacific, each managed by a Regional CEO. The Regional CEOs report directly to the CEO. Together, the Board of Managing Directors and the Regional CEOs represent the Schaeffler Group's Executive Board. In this manner, the Schaeffler Group's organizational structure is reflected in its leadership structure.

The Supervisory Board of Schaeffler AG appoints, advises, and oversees the Board of Managing Directors and is involved in fundamental decisions. The Chairman of the Supervisory Board coordinates the work of the Supervisory Board.

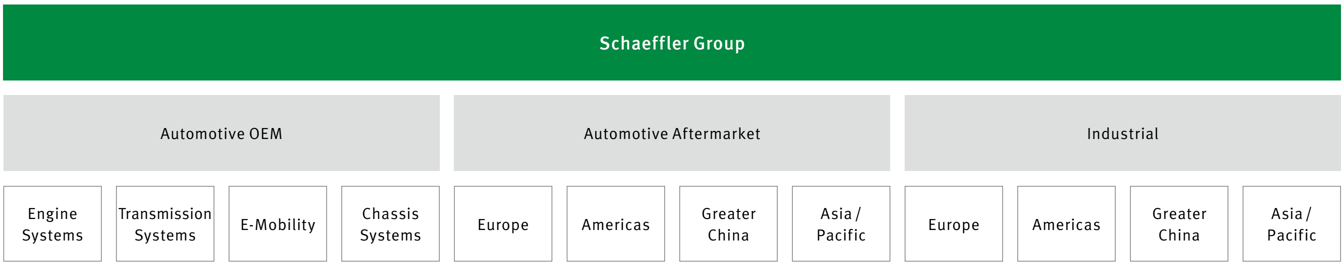
The Board of Managing Directors and the Supervisory Board comply with the recommendations of the German Corporate Governance Code in conducting their affairs and have issued the declaration of conformity pursuant to section 161 German Stock Corporations Act ("Aktiengesetz" – AktG) in December 2017. The corporate governance report including the corporate governance declaration in accordance with section 289f HGB and section 315d HGB including the declaration of conformity pursuant to section 161 AktG is publicly available from the company's website.

Corporate governance report including the corporate governance declaration in accordance with section 289f HGB and section 315d HGB including the declaration of conformity pursuant to section 161 AktG at: www.schaeffler.com/ir

Schaeffler Group leadership structure No. 002
since January 01, 2018



Schaeffler Group divisions and business divisions No. 003
since January 01, 2018



Simplified presentation for illustration purposes.

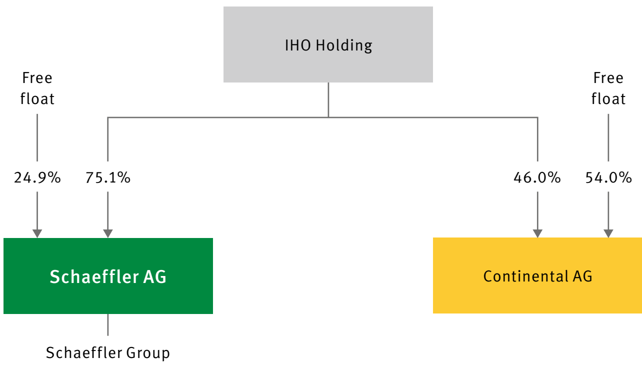
Locations and changes in the scope of consolidation

The corporate head office of the Schaeffler Group is located in Herzogenaurach. In addition, the Schaeffler Group's network of manufacturing locations, research and development facilities, and distribution companies consists of approx. 170 locations in over 50 countries. The production system with currently 74 manufacturing locations in 22 countries is the cornerstone of the Schaeffler Group's operations. The Schaeffler Group is actively helping to shape technological progress for “Mobility for tomorrow” at its 18 R&D centers and at additional R&D locations in a total of 24 countries. As a global development partner and supplier, Schaeffler maintains stable long-term relationships with its customers and suppliers. In addition to Schaeffler AG, which acts as the group's lead company, the Schaeffler Group included 151 (prior year: 152) domestic and foreign subsidiaries as at December 31, 2017. As at December 31, 2017, 103 (prior year: 104) of these subsidiaries are located in the Europe region, 25 (prior year: 26) in the Americas region, 10 (prior year: 9) in the Greater China region, and 13 (prior year: 13) in the Asia/Pacific region.

In 2017, the Schaeffler Group acquired the remaining 49% stake in Compact Dynamics GmbH. As a result, this company is now wholly-owned by the Schaeffler Group. The scope of consolidation underwent only minor changes overall during the year.

See the notes to the consolidated financial statements beginning on page 125 for further details

Legal group structure No. 004
as at December 31, 2017



Legal group structure

Schaeffler AG is a publicly listed corporation domiciled in Germany. Schaeffler AG's share capital consists of a total of 666 million shares. 500 million of these shares are unlisted common bearer shares and 166 million are common non-voting bearer shares. Each common share and each common non-voting share represents an interest in total share capital of EUR 1.00 each.

All 500 million of the common bearer shares are held by IHO Verwaltungs GmbH, which is part of IHO Holding. This represents an approx. 75.1% interest in Schaeffler AG. The 166 million common non-voting bearer shares in Schaeffler AG are widely held. The free float amounted to approx. 24.9% as at December 31, 2017. IHO Holding also holds approx. 46.0% of the shares in Continental AG.

1.2 Business activities

Divisions

The Schaeffler Group's business is primarily managed based on the operating divisions, which have global responsibility and also represent the reportable segments in accordance with IFRS 8.

Organizational structure up to December 31, 2017

Up to December 31, 2017, the Schaeffler Group divided its business activities into the two **divisions Automotive** and **Industrial,** with approx. 77% (prior year: approx. 77%) of the group's revenue generated by the Automotive division and approx. 23% (prior year: approx. 23%) by the Industrial division.

The Automotive division business was organized into the four **business divisions (BD) Engine Systems, Transmission Systems, Chassis Systems,** and **Automotive Aftermarket.** The Industrial division was primarily managed regionally, based on the **regions Europe, Americas, Greater China,** and **Asia/Pacific.**

Organizational structure since January 01, 2018

Effective January 01, 2018, the Automotive Aftermarket was separated from the Automotive division of Schaeffler AG and set up as a third stand-alone division.

As a consequence, the Schaeffler Group has been dividing its business into three divisions – **Automotive OEM, Automotive Aftermarket,** and **Industrial** – since January 01, 2018. The three divisions of the Schaeffler Group will in future be managed from decentralized divisional headquarters located in Buehl, Langen, and Schweinfurt. The Automotive OEM division will be headquartered in Buehl. The new Automotive Aftermarket division will be managed from Langen. The Industrial division continues to be located in Schweinfurt. The corporate head office of the Schaeffler Group is in Herzogenaurach.

The decisions taken further underscore the intention to render the company even more customer-oriented and decentralized in a fast-changing market and competitive environment. This realignment reflects the increased significance of the Automotive Aftermarket business to the Schaeffler Group. These decisions are designed to help emphasize the Schaeffler Group's various business models and to simplify the company's structures: increased focus on the business, increased responsibility for the divisions, closer to the customer, and faster and more flexible decisions.

At the same time, the separation provides the opportunity to streamline the Schaeffler Group's organizational and leadership structure and develop it with a view to the future. This also includes the new E-Mobility business division set up in the Automotive division and the independent organizational unit Industry 4.0 created in the Industrial division effective January 01, 2018.

As a consequence of these decisions, the Schaeffler Group has been reporting under the new structure discussed above since January 01, 2018.

Automotive OEM division

- Strong customer base: all major automotive manufacturers as well as approx. 1,200 automotive suppliers (Tier 1)
- Change to new powertrain technologies addressed proactively: The number of customer projects and volume production orders in the field of E-Mobility is increasing continually
- New E-Mobility business division set up

Customers and products

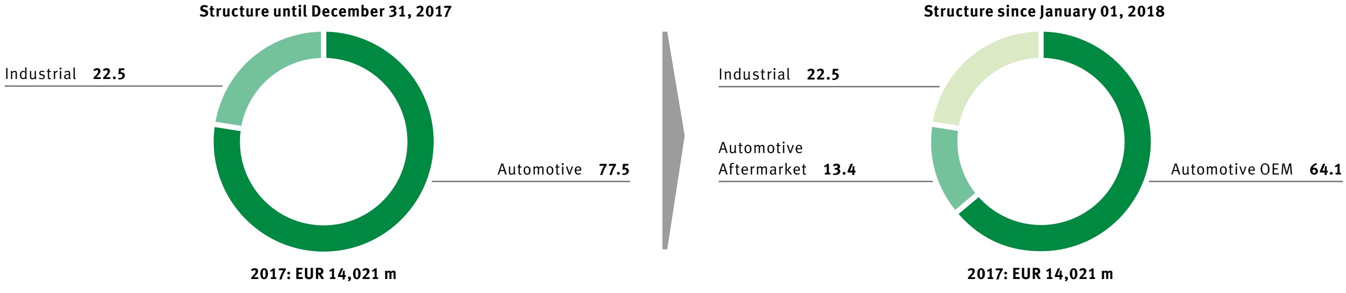
One of the preferred technology partners, the Automotive OEM division is working on technologies for the various drive concepts, markets, and regions and delivers appropriate solutions for the most varied requirements of the automotive industry.

The division's product range includes components and systems for vehicles with drive trains based on internal combustion engines as well as for hybrid and electric vehicle applications. Since January 01, 2018, all products and system solutions for electric mobility, i.e. for hybrid and purely battery-electric vehicles, are managed centrally through the new E-Mobility business division. On this basis, the Automotive division is subdivided into the following four business divisions, which in turn comprise several business units and product lines:

- The **Engine Systems BD** develops and provides components and systems for engines. Precision products are key to helping engines consume less fuel and comply with increasingly stringent emissions standards. The product portfolio includes valve-lash adjustment elements, variable camshaft phasing units, timing and front end auxiliary drives, and thermal management modules.
- The **Transmission Systems BD** develops and provides components and systems for transmissions. Recent years have seen the development of numerous products for the various types of transmissions that have already made it into volume production. Automated manual transmissions and double-clutch transmissions have joined the classic manual and automatic transmissions.

Schaeffler Group revenue by division
in percent

No. 005



- The **E-Mobility BD** combines all components and system solutions for hybrid and purely battery-electric vehicles – from mild hybrids (48 volt) and plug-in hybrids through to purely electric vehicles. The product portfolio includes hybrid modules, primary components for continuously variable transmissions (CVTs), electric axle drives, hydrostatic clutch actuators and electric wheel hub motors.
- The **Chassis Systems BD** develops and provides components and systems for chassis. Its wide range of products includes wheel bearings and mechatronic systems through to electromechanical actuators for active chassis control with integrated sensors that capture data.

The Automotive OEM division's global key account management function is responsible for serving key customers. In this manner, the Automotive OEM division is consistently aligned along customer and market needs and the course for its sustainable profitable growth has been set.

Sales markets

The key indicator for trends in the Automotive OEM division's relevant market is global automobile production. Research institute IHS expects steady market growth in the next few years, with electric drives characterizing the mobility of the future. By 2030, as much as 30% of all newly produced cars will be using all-electric drive systems according to a scenario recently proposed by Schaeffler. 30% will be equipped exclusively with an internal combustion engine and 40% will have a hybrid powertrain consisting of an internal combustion engine plus an electric drive. The Automotive OEM division responds to these challenges with a comprehensive approach. Whether components and systems for vehicles with drive trains based on the internal combustion engine or hybrid and electric vehicle applications – the division provides innovative solutions for all types of drives in order to make low-emission driving fit for the future.

Key growth drivers

Under the strategy "Mobility for tomorrow", the Automotive OEM division addresses the current megatrends of the automotive sector – drives reducing fuel consumption and emissions, electrification, shared mobility, interconnectedness, and autonomous driving. These megatrends offer growth perspectives in all market segments. These perspectives are driven, in particular, by growing sales of modules and systems in the field of new electrification technologies, which is intended to considerably increase content per vehicle, and, as a result, generate growth approx. four percentage points higher than the annual growth rate of the global automotive market.

From drive trains based solely on an internal combustion engine through to a hybrid or electric design: The Schaeffler Group's broad development expertise creates tailored drive solutions for the mobility needs of the various target markets, making an important contribution to ensuring that tomorrow's mobility is efficient and clean.

Drives reducing fuel consumption and emissions: The Automotive OEM division's comprehensive know-how enables it to make the classic drive train as eco-friendly as possible and has a broad and growing product portfolio. The integrated torque converter, the electronic clutch, the electric camshaft phasing unit, the fully variable valve control system UniAir, and the second-generation thermal management module offer innovative solutions for meeting legal limits and emission targets.

Electrification: Considerable potential improvements are offered by the electrification of conventional drive trains. In light of this, the field of E-Mobility represents one of the key opportunities for the future under the strategy "Mobility for tomorrow". Consequently, the E-Mobility initiative was defined as part of the excellence program "Agenda 4 plus One". The Automotive OEM division already offers innovative solutions for hybrid and electric vehicles today. 48-volt systems with components by the Automotive OEM division being a particularly cost-efficient solution for driving with zero local emissions. These systems enable electric clutch systems, as well as hybrid modules and electric axles to be integrated in existing vehicle architectures, making new efficient and convenient features possible. Plug-in hybrids can also be operated in all-electric mode and thus with zero local emissions. Another development was the electric axle, a modular kit solution for hybrid and all-electric vehicles. The fully electric drive system features a modular design for flexible use. The electric wheel hub motor "eWheelDrive" offers innovative technology for the mobility of tomorrow, as well. This highly integrated drive facilitates completely new vehicle designs.

The number of customer projects and volume production orders in the field of electric mobility is continually increasing. The division plans on as at least 15% of total Automotive OEM revenue being generated by components, subsystems and systems for hybrid and fully battery-electric vehicles as early as 2020. The Schaeffler Group has received a total of currently eight volume production orders for electric axles and hybrid modules from various automobile manufacturers around the world, the main driver being the Greater China region, which is increasingly setting global market trends in electric mobility. Three of these volume production orders for electric axles and hybrid modules came from China.

Shared mobility, interconnectedness, and autonomous driving: Interconnectedness between people, processes, data, and things is advancing at an unstoppable speed and is one of the strongest growth segments of the future. The digital revolution also influences all facets of the automotive sector. For Automotive OEM, a key component here is the development of intelligent components and systems for autonomous driving, electrification, and interconnectedness. The wheel hub motor offers the perfect platform for driverless and shared vehicles and mobility solutions. Integral electromechanical sensors assess parameters such as location and road surface condition and transmit them to the cloud. Topics such as autonomous and interconnected driving as well as shared mobility are also giving rise to new development partnerships and business models.

Automotive Aftermarket division

- Automotive Aftermarket business strengthened: Automotive Aftermarket set up as third stand-alone division
- Close to the customer due to approx. 2,200 customers and over 55 sales offices and branches worldwide
- Construction of an integrated European assembly and packaging center

Customers and products

Being one of the leading development partners to the global automotive sector, the Schaeffler Group can tap into decades of experience in the Aftermarket business and stands for groundbreaking innovations. Whether for passenger cars, light and heavy commercial vehicles, or tractors – the new Automotive Aftermarket division offers tailored solutions for transmission, engine, and chassis systems for all vehicle classes and models in original-equipment quality.

Setting up the Automotive Aftermarket as a separate division of the Schaeffler Group reflects the increased significance of the automotive aftermarket business to the company. The management model of the new division follows a regional approach based on the **regions Europe, Americas, Greater China,** and **Asia/Pacific.**

Within each region, the division uses two distribution channels to sell its products and services: the Original Equipment Service (OES) and the open (independent) market, known as the Independent Aftermarket (IAM). The OES comprises the automobile manufacturers' spare parts business, that is, supplying original spare parts and services to branded repair shops, i.e. those that are authorized by automobile manufacturers. IAM, on the other hand, supplies independent repair shops that are not tied to any one vehicle brand with spare parts and services via the various distribution levels. IAM differentiates between two types of business. In addition to the traditional component business consisting of replacing parts, the service business provides repair sets and kits custom assembled to help make vehicle repairs simple, efficient, and professional.

Schaeffler Automotive Aftermarket customers mainly include almost all major international and national trading companies, which in turn supply Schaeffler products to other distribution levels all the way down to the repair shop. In addition, the division cooperates with all international and national trade cooperatives in which a large number of its customers are organized.

Like the Automotive OEM and Industrial divisions, the Automotive Aftermarket division operates under the Schaeffler corporate brand. The comprehensive Aftermarket product range includes products and repair solutions for engine, transmission, and chassis applications, such as timing drives, clutch and clutch release systems, or wheel bearings, that are distributed using the four product brands LuK, INA, FAG, and Ruville. All components are optimally tuned to work together and allow for fast and professional replacement.

The division assists repair shops in professional clutch repairs with its LuK RepSet family. The product range also includes the complete hydraulic clutch release system, the dual-mass flywheel, as well as professional repair solutions for commercial vehicles and tractors.

Under its INA brand, Schaeffler offers know-how across the four key systems in an engine: The product portfolio of the full-range supplier comprises components for the timing drive (for both belt- and chain-driven vehicles), the front end auxiliary drive, the valve train, and the cooling system. The replacement parts program consists of individual products as well as solutions provided in the form of innovative kits and sets.

Schaeffler's FAG brand supplies what it takes to make replacing wheel bearings seamless. Its reliable wheel bearings and innovative repair solutions range from the classic wheel bearing set, the FAG WheelSet, and the FAG WheelPro (for replacing the wheel bearings of both wheels of an axle) through to wheel bearing repair solutions for light commercial vehicles and preassembled wheel bearing units for heavy commercial vehicles, such as the FAG RIU (Repair Insert Unit) and the FAG SmartSET.

Being a specialist for chassis and steering parts, the Automotive Aftermarket division develops intelligent repair solutions and kits for all common European and Asian vehicle models, tailored to suit market needs and requirements. All of them include all replacement and accessory parts required for professional installation.

Increasingly complex vehicle applications and the large number of new vehicle models are constantly confronting vehicle professionals with challenging repair situations. The Automotive Aftermarket division's REPXPERT offers comprehensive services covering every aspect of its products and repair solutions. Whether they utilize the web portal, service hotline, installation guides and videos, training seminars and events, or tools tailor-made for professional repairs – repair shops benefit from the Schaeffler Group's over 40 years of experience in the Automotive Aftermarket. In addition to its own services, the Automotive Aftermarket division has also co-founded important service initiatives with industry partners, a significant contribution to keeping repair shops and distributors well informed. These initiatives include TecAlliance, a company providing solutions for electronic catalog data, inventory management, and digitalization, as well as the telematics platform CARUSO.

Sales markets

The ever growing vehicle population, rising average vehicle age, and increasing vehicle complexity provide tremendous opportunities for growth in the division's replacement parts business. According to research institution IHS (February 2018), the worldwide vehicle population will grow from approx. 1.3 bn in 2017 to approx. 1.6 bn in 2022, and the average vehicle age will increase from approx. 9.5 years to approx. 9.8 years. As the most significant increase for both parameters is expected in the Greater China region, the division considers this region to hold a high potential for future growth. Although the move toward new drive technologies will only have a very minor impact on the Aftermarket business over the next 10 years, the Automotive Aftermarket division is already preparing for future demands. Networking with the Automotive OEM division within the Schaeffler Group is key to this preparation.

Key growth drivers

The division aims to generate annual revenue growth averaging approx. 3% in the coming years – based on technical excellence, intelligent solutions, and outstanding services, as well as a consistently global operation. The Greater China and Asia/Pacific regions are driving the division's growth. Another focus is on maintaining the high degree of coverage provided by the division's product and service portfolio as well as on further improvements regarding availability and customer loyalty. Digitalization is also becoming a focus of the Automotive Aftermarket's attention. Working with other disciplines from across the group, the division will develop repair solutions and services that make repair shops ready for the future.

In order to secure opportunities for growth and to considerably expand customer and delivery service, the division plans to realize a highly automated logistics location in Saxony-Anhalt near Halle/Saale, whose capacity can be adjusted flexibly; the facility is slated for commissioning in the first quarter of 2020. The project will establish a state-of-the-art integrated European assembly and packaging center known as ⊙ Aftermarket Kitting Operation (AKO). The AKO is part of the "Agenda 4 plus One". This logistical structure will be implemented in additional regions beyond Europe as well. The company is planning AKOs in North America, Asia/Pacific, and China, and there is already an AKO in operation in South America. Implementing the AKOs is an important step toward further improving the delivery performance of the Automotive Aftermarket division in order to generate maximum customer satisfaction in the long-term.

Industrial division

- Products and solutions for approx. 7,800 customers from a variety of industrial sectors
- Program "CORE" aimed at increasing earnings quality progressing on schedule
- Mechatronic systems and digital services business combined into organizational unit Industry 4.0

Customers and products

The Industrial division understands and meets the needs of customers in numerous different sectors. It offers goods and services ranging from high-volume standard products to individual specialized solutions and from mechanical components through to mechatronic systems and digital services. The common denominator is the technological expertise and the know-how covering the customer's entire system.

The management model of the Industrial division follows a regional approach based on the **regions Europe, Americas, Greater China,** and **Asia/Pacific.** Within the regions, the direct business with the OEMs is grouped into eight sector clusters: (1) wind, (2) raw materials, (3) aerospace, (4) railway, (5) offroad, (6) two-wheelers, (7) power transmission, and (8) industrial automation. In addition to these sector clusters, the division sells via distributors through the indirect distribution channel known as Industrial Distribution.

This structure has proven invaluable with respect to the Industrial division's customers, since many customers have a regional focus. It allows the division to target its response to local customer needs even more closely and to strengthen customer loyalty. Transregional issues, such as the global technology and product strategy, are driven forward by the close network linking the regions within the division. A global key account management function for key customers with operations in more than one region ensures that their needs are met equally all over the world. Thus, the Industrial business is consistently aligned along customer and market needs and the course for its sustainable profitable growth has been set.

With a view to mobility, the Industrial division develops rolling bearings and power transmission solutions for bicycles and motorcycles, rail vehicles, aircraft and spacecraft, as well as agricultural and construction machinery. A great deal of importance is placed on energy efficiency, for instance in eco-friendly engine designs in the aviation sector. Schaeffler offers bearing solutions for all types of drives, whether mechanical, electric, or hydraulic. The Industrial division's technological expertise in the field of renewable energy is already on display in products and solutions for hydropower, solar energy, and wind power applications. Customers in the paper industry and in the raw material extraction, preparation, and processing sectors with their generally "heavy duty" rolling bearing applications play an important role for the Industrial division. For decades, this division has also been an innovative systems partner in the industrial automation sector cluster, particularly for machine tools and machinery for the textile, printing, food, and packaging industries, as well as for medical technology and the semiconductor industry. Industrial Distribution is responsible for the business with distribution partners serving end customers and OEMs in the above sectors.

Customers require intelligent solutions and optimized lifecycle costs, which opens up new growth areas for the Industrial division. The newly established organizational unit Industry 4.0 is aimed at developing these growth areas. This unit combines the entire industry-specific business with mechatronic systems and digital services as well as the required related components. Industry 4.0 is to the Industrial division what electric mobility is to the Automotive OEM division. The field of Industry 4.0 is one of the key opportunities for the future under the strategy "Mobility for tomorrow". Consequently, the Industry 4.0 initiative was defined as part of the excellence program "Agenda 4 plus One". The division plans on approx. 10% of revenue being generated by Industry 4.0 products and solutions by 2022.

Sales markets

The key indicator for trends in the Industrial division's relevant market is the global market volume for rolling and plain bearings, linear technology, and service products. The Industrial division expects market volume to increase by approx. 3% at constant prices in the next five years. The growing number of competitors, especially from Asia, will intensify competition. Assuming this will cause prices to gradually decline, the relevant market will experience only a slight expansion.

Key growth drivers

In the future, the Industrial division's success will also be based on its strong product portfolio for rotary and linear applications. Gained in years of collaboration with customers, the know-how regarding the use of products in systems will enable the division to grow beyond rolling bearings with complex mechanical and mechatronic systems and Industry 4.0 applications.

Components: The cornerstone of the successful growth of the Industrial division is its core business with components, which are constantly being developed further and improved. Successful examples of newly developed products are bearings of X-life quality or the innovative material known as Mancrodur. The wide variety of goods and services, which comprises standard products offering good value for money, technical advice, as well as solutions developed specifically for the customer, offers the ideal balance between cost and benefit for every customer.

Mechanical systems, mechatronics, and Industry 4.0 services: Being successful in the systems business requires competitive components and an understanding of how they interact within the system. The Industrial division meets both of these requirements thanks to its many years of cooperating with its customers and providing advice to them. In the future, mechanical components, sensors, actuators, and control electronics will increasingly be combined into integrated mechatronic systems. Examples of components equipped with sensors include the "Spindlesense" (spindle bearing equipped with sensors) and the "Durasense" (linear guidance system equipped with sensors) presented at the EMO trade fair in Hanover.

The Industrial division itself provides a significant proportion of development and value added, with the remainder sourced in cooperation with suppliers. Direct drives for rotary tables in the food industry and linear drives used in medical technology, for instance, are developed and manufactured in-house by the Industrial division.

Mechatronic systems supply the data that forms the basis for digital services reducing the customer's lifecycle costs. Among other things, the Industrial division has been active in the field of "condition monitoring" (i.e. monitoring operating condition) for many years. Additional services are being developed and are aimed to help the Industrial division grow faster than the market.

Program "CORE"

The program "CORE" started by Schaeffler AG's Board of Managing Directors in 2015 is progressing on schedule. The agreed upon staff reduction targets having been reached, the first wave was completed successfully. In order to achieve future earnings targets, the company worked hard to further develop the second wave in 2017 that was initiated by Schaeffler AG's Board of Managing Directors in 2016. In addition to the measures addressing the production network and distribution that have already been communicated and executed, further efficiency measures are planned regarding overheads and production cost. Along with cost reductions, the company is also planning to increase its profitability using targeted price and portfolio measures. On this basis, the division aims to improve its EBIT margin before special items to 11 to 13% by 2020.

Schaeffler Group functions No. 006
since January 01, 2018

Schaeffler Group

CEO Functions	Technology	Operations	Finance	Human Resources
– Quality – Schaeffler Consulting – Communications & Branding – Investor Relations – Legal – Internal Audit – Business Development & Strategy – Compliance & Corporate Security – Corporate Real Estate	– Corporate R&D Management – Technology Strategy & Innovation – R&D Processes, Methods & Tools – R&D Competence & Services – Intellectual Property Rights – Surface Technology – Information Technology – Strategic IT – Coordination Office Digitalization	– Operations Strategy & Processes – Production Technology – Special Machinery – Tool Management & Prototyping – Industrial Engineering – Bearing & Components Technologies – Logistics – Purchasing – MOVE	– Finance Strategy, Processes & Infrastructure – Corporate Accounting – Corporate Controlling – Corporate Treasury – Corporate Taxes – Corporate Insurance – Divisional Controlling Automotive OEM – Divisional Controlling Automotive Aftermarket – Divisional Controlling Industrial	– HR Strategy – HR Policies & Standards – Leadership, Recruiting & Talent Management – Schaeffler Academy – HR Systems, Processes & Reporting – Environment, Health & Safety – HR Functions – HR Automotive OEM – HR Automotive Aftermarket – HR Industrial

Simplified presentation for illustration purposes.

Functions

The multi-dimensional structure of the Schaeffler Group includes the functional management level with five functional areas: (1) CEO Functions, (2) Technology, (3) Operations, (4) Finance, and (5) Human Resources.

The functions are essential to securing the Schaeffler Group's long-term competitiveness and innovative ability. In accordance with the company's commitment to top quality, outstanding technology, and exceptionally innovative spirit, the two functions Technology (particularly Research and Development, R&D) and Operations are discussed in more detail below.

Quality

The Schaeffler Group's benchmark is consistently ensuring top quality and product safety across all applications. Based on the strategy "Mobility for tomorrow" and the "Agenda 4 plus One", the company's quality strategy is oriented toward ensuring products and processes are free of defects and errors. Thus, it focuses primarily on three issues in order to facilitate "Mobility for tomorrow":

- Continuous improvement of the core business, one of the Schaeffler Group's key success factors.
- Constant improvement of the management system and of the processes on which the company's entire business is founded.
- The preventative quality assurance measures in product development that ensure sustainability and set trends.

Quality strategy programs and projects are defined and promoted in a wide variety of events. Thus, in 2017, quality was covered in the Technology Dialog, including presentations on quality technology topics with a development horizon of 5 to 10 years. For instance, an end-of-line test for mechatronic applications was presented that is still under development; it uses Digitalization to perform correlation analyses in order to determine the cause of errors detected. Applied in volume production, this test rig will enable non-conformity costs and waste to be reduced for the long-term.

This innovative testing technology was also included as a pilot in the Quality for Tomorrow initiative that is part of the "Agenda 4 plus One". The objective of this initiative is to increase the quality of both the product and the processes once again, regardless of complexity. The initiative addresses structuring the quality management function to accommodate increasingly complex products, new technologies for quality assurance, and improving existing quality processes. However, the overall aim of the initiative is not only to come up with a response to new trends in the market, but also to increase the quality and efficiency of the existing business. One example of this is the "Fit for low noise bearing quality" project, which coordinates activities related to ball bearings in order to meet the highest demands regarding noise. Thus, the "Quality for Tomorrow" initiative is not only of a safeguarding, preventative nature, but actively and measurably contributes to the Schaeffler Group's profitability.

The “Fit for Quality” initiative was one of the key topics at the quality day held in 2017. Well-established within the company for several years, “Fit for Quality” is a program aimed at achieving “zero defects” and delivering top quality to internal and external customers. A revision in 2015 resulted in a renewal: The change from a quality improvement program to a comprehensive quality culture. The amended guiding principles (Fit for Quality Axioms) follow the standards regarding quality-oriented leadership, systematic planning and training, tools and processes, error detection, and review of processes and measures, as well as the transfer of good solutions to other areas. Outstanding results were presented during the Fit for Quality Zero Defect Days in January 2017.

Outstanding quality is a key feature differentiating the Schaeffler Group from its competition and represents the basis of the group’s future long-term growth. The Schaeffler Group’s high quality standards are demonstrated by, among other things, numerous awards received from customers. The Schaeffler Group received a total of 58 quality awards in 2017, including Ford Motor Company’s “World Excellence Award” in the “Quality Pillar” category. The “World Excellence Awards” are designed to recognize Ford’s outstanding suppliers around the world; these suppliers distinguish themselves by excellence in all areas.

In addition, all of the Schaeffler Group’s manufacturing locations are certified under globally recognized quality norms and standards. Following its activities in 2016, the Schaeffler Group has successfully rolled out, or initiated the rollout of, the requirements of the new certification standards IATF 16949:2016 (Quality management system – standard of the automotive sector), the ISO/TS 22163 (Quality management system – particular requirements for application of ISO 9001:2015 in the rail sector), as well as the SAE AS 9100D:2016-09-20 (Quality Management Systems – Requirements for Aviation, Space, and Defense Organizations) in all relevant Schaeffler plants worldwide in 2017. Compliance with these standards is reviewed and confirmed using regular internal and external audits at the relevant locations.

Technology

Globalization, urbanization, digitalization, scarcity of resources, renewable energy, and the growing need for mobility worldwide are resulting in changing market requirements. This also leads to changing EcoSystems requiring the development of comprehensive expertise ranging from energy generation through to energy supply and energy consumption. In light of this, the Schaeffler Group’s Technology function relies on the continuous improvement of existing technologies as well as on the development of completely new technologies.

More on the group strategy on pp. 23 et seq.

The Schaeffler Group benefits from its many years of experience and expertise with product and systems development. Being a supplier of complex modules and complete system solutions, the Schaeffler Group will continue to expand this expertise while maintaining its established components business. The goal here is to safeguard the Schaeffler Group’s technological leadership and to thoroughly delight customers worldwide by delivering innovative application- and customer-oriented system solutions from a single source.

From an organizational perspective, the Technology function includes Corporate R&D Management, Technology Strategy & Innovation, R&D Processes, Methods & Tools, R&D Competence & Services, Intellectual Property Rights, Surface Technology, as well as Information Technology and the Coordination Office Digitalization. Strategic IT was added in 2017.

Schaeffler Group R&D

The Schaeffler Group is actively helping to shape technological progress for “Mobility for tomorrow” with an average of 7,634 R&D staff (prior year: 7,121) at 18 R&D centers (prior year: 17) and additional R&D locations in a total of 24 countries. Its 2,316 patent registrations filed with the German Patent and Trademark Office made the Schaeffler Group the second most innovative company for the fourth consecutive year in 2016. The more than 3,294 inventions reported internally in 2017 (prior year: 2,950) also demonstrate the company’s innovative ability. On this basis, the Schaeffler Group expects to once again rank among the most innovative companies in Germany in 2017.

The Schaeffler Group’s research and development activities comprise corporate research and development as well as the application-oriented development activities of the Automotive OEM, Automotive Aftermarket, and Industrial divisions.

Research and development expenses No. 007

	2013	2014	2015	2016	2017
Research and development expenses (in € millions)	611	622	673	751	846
Research and development expenses (in % of revenue)	5.5%	5.1%	5.1%	5.6%	6.0%
Number of research and development staff [1]	6,039	6,387	6,651	7,121	7,634

[1] Averages.

Corporate research and development: The company's corporate research and development, which is incremental to the divisions, facilitates long-term customer- and market-specific technical solutions and helps promote interdisciplinary knowledge transfer. The corporate R&D activities follow a systematic process that is aligned along the product lifecycle and speeds up development. The technical knowledge gathered is collected and combined in the Schaeffler Group's competence centers, ensuring increased technical depth of product development as well as quick and valid decisions.

One focus of the corporate research and development activities is on covering the entire energy chain – from energy generation, mainly from renewable energy sources, through to the storage and consumption of energy. In the field of energy generation, for instance, low-friction bearings are currently being developed for the wind power sector; they will reduce wear and tear, extending their operating life. In addition, Schaeffler is preparing to enter the field of industrialized fuel cell technology. Existing expertise in technologies such as forming, coating, and assembly is used to develop and manufacture high-performance metal bipolar plates, which are at the core of any fuel cell.

Collaborations: The corporate R&D activities are founded on a global innovation network that contributes significantly to the Schaeffler Group's global technological leadership. Collaborations with universities in the form of a "Schaeffler Hub for Advanced Research" (SHARE) under the "Company on Campus" concept ensure the consistent development of future-oriented technologies. For instance, SHARE at FAU (Friedrich-Alexander University of Erlangen-Nuremberg) focuses on Digitalization along the entire value chain, SHARE at KIT (Karlsruhe Institute for Technology) on electric mobility, lightweight design, and energy storage (battery and fuel cell), and SHARE at NTU (Nanyang Technological University, Singapore) on personal urban mobility. In 2017, the Schaeffler Group once again expanded its global footprint at universities by officially inaugurating a SHARE at Southwest Jiaotong University (SWJTU) in Chengdu, China. This collaboration with one of the most acclaimed universities in the world in the field of new-generation rail vehicles focuses on research and development regarding mobility concepts for railway transport. Schaeffler has also been successfully collaborating with various Fraunhofer Institutes for many years. In 2017, the Schaeffler Group has entered into a comprehensive strategic partnership with Fraunhofer-Gesellschaft designed to bring technologies into practical applications even faster and in a more targeted manner.

Interconnection with start-up companies adds to this innovation network. Many product and process innovations as well as new work and business models are initially created by start-up companies. Combined with Schaeffler's strengths and experience, ideas are efficiently developed into marketable products and services. Schaeffler operates an office in Silicon Valley to help extensively exchange ideas with start-up companies and also cooperates with the start-up campus Factory Berlin and the tech incubator ZOLLHOF in Nuremberg. In 2017, the company's innovative ability and resulting products received, among others, the PACE Award and the AutomotiveINNOVATIONS Award.

One example of the company's corporate innovation activities is the Bio-Hybrid. Intermodal traffic in areas where space is at a premium and the ability to change smoothly from one means of transport to another is becoming more and more important for dealing with the growing volume of traffic in urban centers. Schaeffler is offering an innovative solution, the Bio-Hybrid concept, which sits somewhere between a pedelec and an electric car in terms of size and range. The growing passenger traffic leads to another issue of the future: autonomous driving. Schaeffler is doing research in this field under publicly subsidized projects at the SHARE at KIT research location. The results have applications that go beyond those directed toward autonomous driving. For instance, the energy efficiency of power steering systems was improved, reducing the vehicle's consumption.

R&D in the Automotive OEM division

The megatrends globalization and urbanization require new forms of mobility. Climate change and the growing scarcity of resources make reducing energy consumption essential. These challenges offer significant opportunities for the Schaeffler Group and characterize the development environment in the automotive sector. In the future, in addition to fully battery-electric vehicles, a large share of the vehicle population will be hybrid-driven. Especially in the next few years, there will still be a demand for large numbers of conventional drives. As a result, the company's research and development activities are aimed at increasing the efficiency of internal combustion engines in order to reduce harmful emissions.

The Schaeffler Group predicts a steady increase in electrified vehicles over the coming years. In light of this, the field of E-Mobility, along with Industry 4.0 and Digitalization, represents one of the key opportunities for the future under the strategy "Mobility for tomorrow". Consequently, the company has defined the E-Mobility initiative as part of its "Agenda 4 plus One" excellence program. The Schaeffler Group already offers innovative solutions for hybrid and electric vehicles today. To facilitate a consistent approach, the company created the E-Mobility Systems Division several years ago, which consolidates its wide range of activities relating to alternative types of drives across departments and national borders. This development was continued by establishing the E-Mobility business division effective

January 01, 2018. These internal activities are supplemented by work at research institutions such as the SHARE at KIT, where engineers are developing solutions in the field of energy storage, electric drives, and automated mobility. The know-how gained from the FIA Formula E Championship is also incorporated in the development of electric mobility technologies.

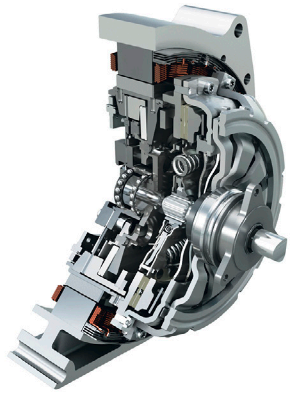
Starting with individual components, Schaeffler develops total technological system solutions for electric drives. Drives integrated in axles or wheels are particularly suitable for battery-electric vehicles. While the electric wheel hub motor is still at the predevelopment stage, volume production of the electric axle is imminent. The newly developed electric axle was presented at the International Motor Show (IAA) in 2017. Schaeffler's electric axle offers a modular solution for hybrid vehicles and battery-electric cars. The single-speed electric axle is designed with an extremely compact transmission, offering plenty of space for the electric motor. The basic configuration can be expanded by adding functional elements such as a parking lock. A second gear is particularly necessary for plug-in hybrid vehicles requiring dynamic, all-electric operation up to 120 km/h and high top speed. The two-speed axle developed by Schaeffler offers a solution to this need.

With a view to electric mobility, electrification of conventional drive trains offers significant potential improvements. A 48-volt system represents a comparatively cost-efficient solution to this issue. In current volume production vehicles, this system, instead of a starter-generator, is connected to the crankshaft of the internal combustion engine via a belt. For future vehicle generations, Schaeffler also offers the integration of the 48-volt electric motor into the engine-transmission unit and into the axle. This solution allows vehicles to move off from a standstill using electric power only, to maintain the speeds required in city traffic purely electrically, and to recuperate braking energy, all valuable contributions to protecting the environment.

A plug-in hybrid drive powertrain enables even greater fuel consumption savings to be achieved as well as driving with zero local emissions across longer distances. As far back as in 2010, Schaeffler delivered major components for such a drive system. Now, Schaeffler has developed its own high-voltage hybrid module enabling the transfer of very high torques that is about to enter volume production. A patented branching of the power flow within the module makes it possible to transfer such high torques, so that vehicles with very large mass can comfortably move off from a standstill.

In addition to the mechanical architecture, electric vehicles also require power electronics to supply electric power as and when needed. In a collaborative partnership with SEMIKRON, Schaeffler is expanding its electronics expertise and, using space-optimized power electronics, has the capability to efficiently convert, control and integrate electric energy into the entire system. Alternative drive systems also require individual software solutions. Schaeffler leverages its expertise in engineering, for instance to achieve perfect interaction between the drive units throughout the entire system.

Schaeffler hybrid module 48-Volt No. 008



Along with electricity-based drive technologies, the Schaeffler Group's research and development activities focus on improving the efficiency and performance of conventional internal combustion engines. The second-generation thermal management module, which went into volume production in 2017, is one example of this. The thermal management module uses rotary slide valves controlled by sensors to precisely manage the temperature within the vehicle's drive train and enables the ideal temperature window for the engine and transmission to be reached quickly. This has a positive effect on fuel consumption and consequently on CO_2 emissions. Due to these optimized temperatures, the thermal management module also positively affects component life within the drive train. The dynamic timing of the engine's valves is another important source of leverage for reducing fuel consumption and, consequently, emissions. To this end, the Schaeffler Group has developed an electric camshaft phasing unit that facilitates fast intake valve adjustment even in dynamic driving modes and has successfully introduced it into volume production.

R&D in the Automotive Aftermarket division

The R&D activities of the Automotive Aftermarket division focus on the specific requirements of customers in the service and replacement parts business. They consist of analyzing the markets' repair needs and behavior. Its broad and deep understanding of Schaeffler products and solutions enables the Automotive Aftermarket to offer solutions along entire systems. Building on this, product specialists consisting of engineers and master mechanics create intelligent repair solutions, allowing the repair shop to perform professional repairs with high product quality.

One example of the outcome of these research and development activities is the repair sets and kits that include all replacement parts required for a complete repair. The introduction of the LuK GearBOX has simplified transmission repairs to the extent that repair shops can now repair transmissions on their own. Another example is the introduction of mixed reality applications for the repair shop. These applications enable the customer to use virtual reality to take a look at the digitized future of the Automotive Aftermarket.

R&D in the Industrial division

The megatrend digitalization is among the key drivers of development in the Industrial division. Consequently, the company has developed the Industry 4.0 initiative as part of its “Agenda 4 plus One” excellence program. Under Industry 4.0, the Schaeffler Group relies on intelligent networks connecting product development, production, logistics, customers, and suppliers. Its technological basis are intelligent, digitally linked systems that will maximize the possibilities for autonomous production and optimum plant operation in the future: People, machines, and products communicate and collaborate directly with one another. In the future, the company will utilize this expertise for internal processes and offer it to customers while maintaining its “classic” components business. The technological expertise and the know-how covering the customer’s entire system are key to achieving success with the entire range from mechanical components through to cloud-based services.

At the Hannover Messe, the Schaeffler Group presented, as part of its “Industry 4.0” initiative, the Smart EcoSystem, a digital infrastructure for new business models based on digital services that increases availability, reliability, and process quality of machines and plants. From a technical perspective, the Smart EcoSystem is structured in three levels. The lowest level, “Mechatronics”, contains what are known as smart components, including, among others, mechatronic products with additional sensor- or actuator-based functionalities. One example of this is the VarioSense, a standard ball bearing equipped with a sensor cluster for recording machine and process data such as temperature or speed. At the next level, these systems can be linked via an interface, creating what are known as “Virtual Twins”. The accompanying digital services offer a wide range of potential uses such as optimizing machine utilization. At its top level, “Applications”, the Smart EcoSystem offers the possibility to perform analyses that can be used, among other things, to make improvements and to develop new products and services. Potential uses for both internal and external customers lie in increased machine availability and productivity, reduced operating and maintenance costs, improved process stability and quality, and improved product quality.

Spindle bearings with integrated sensor technology represent another successful example from 2017. Machine tool downtime is frequently the result of defective spindles. From this initial situation, Schaeffler has developed a system of sensors with the objective of preventing spindle failure. The completely new sensor system, which has been developed specifically for applications in machine tools, measures the displacement of the spindle shaft under load in high resolution and in five spatial directions. All of the software and the required algorithms are integrated into the sensor technology. In the event of a collision, the spindle is deactivated very quickly, preventing further damage to the spindle. In addition, the system allows the machine operator to detect unfavorable operating conditions in order to make targeted adjustments to the machining process.

Sensor system in a spindle bearing No. 009

In addition to the activities around the development focus Industry 4.0, the Industrial division pressed forward with several other initiatives, such as the improvement and new development of bearings for wind turbines. The bearing supports of the rotor in a wind turbine are exposed to enormous operational stresses. The rolling bearings are subjected to highly dynamic loads and operating conditions. Schaeffler has developed a new, compact bearing unit for locating bearing concepts for rotor bearing supports. The tapered roller bearing unit is pre-drilled for flange mounting and enables loads to be supported safely thanks to the large contact angle and narrow axial guidance of the rotor. Schaeffler offers the option of expanding the functionality of the unit by integrating the digital GreaseCheck. The sensor analyzes the grease used and optically measures the water content, turbidity, mechanical wear, and grease temperature directly in the bearing arrangement.

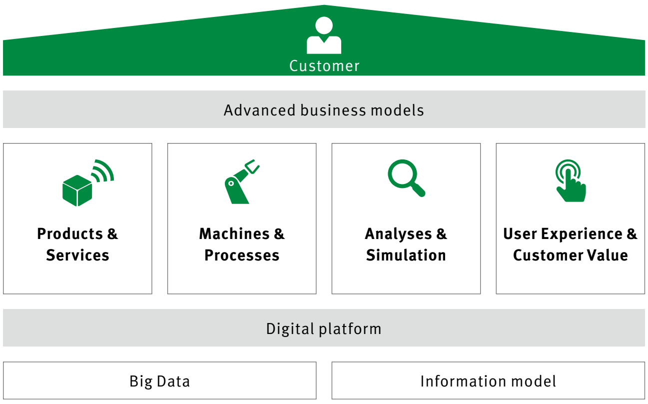
Digitalization and IT

As it increasingly merges the real world and the digital world, the digitalization megatrend poses new challenges, but also offers great opportunities in an enormous growth area. Digitalization is transforming traditional processes. Digital technologies are gradually becoming a core component of value added in purchasing, manufacturing, logistics, distribution, as well as in the human resources and finance functions. Therefore, the Schaeffler Group has developed and implemented the Digital Agenda initiative as part of its "Agenda 4 plus One" excellence program, a component of the group's strategy "Mobility for tomorrow". Its key objective is connecting the physical and the digital world. The company intends to raise the proportion of value added by digitally enhanced products and services to approx. 10% by 2020. The customer benefits from the combination of big data analyses with Schaeffler's thorough application know-how. To improve internal processes and generate added value for external customers, existing business models are expanded and new, digital business models are developed and implemented. To this end, the Schaeffler Group is adding sensors, actuators, and controllers, including the relevant software, to its components. They will facilitate collecting and processing data on machine or plant condition and behavior in the future.

Qualified employees are fundamental to the successful implementation of the Digital Agenda. In addition to existing specialists, the Schaeffler Group was able to win numerous "digital and IT talents" in 2017 and is aiming to establish a significant talent pool. To appropriately concentrate these activities, the Nuremberg location will be transformed into an IT campus which will act as the basis for consolidating the company's IT expertise. The Schaeffler Group has established a centralized project management in order to support the groupwide and cross-functional coordination and implementation of its Digitalization projects. This "Coordination Office Digitalization" manages the set-up and expansion of the group's digital activities under the "Digital Agenda" and has just moved into the corporate "Digital Home" in Herzogenaurach.

The "Digital Agenda" starts with the customer. The new digital business models are oriented toward the customer's benefit. The Schaeffler Group focuses on four components representing the key digital business scenarios. In 2017, projects were initiated for each of these components.

Digital Agenda of the Schaeffler Group No. 010



Products & Services: Functions of existing products are expanded using data generated by sensor systems. By linking products to the Cloud, the Schaeffler Group is aiming to add additional value. For instance, together with the experts from the Industrial division, a platform for digital services is being developed to enable wind park providers to efficiently monitor wind turbines.

Machines & Processes: In production, processes are continually being improved by providing digital assistance to humans and connecting, for instance, machines or transport vehicles. The Schaeffler Group is aiming to utilize data comprehensively. Among other things, the company is creating new service products to be offered to the customer. A "Digital Shadow" represents the digital image of a process, including historical and real-time information, in order to understand, quantitatively visualize, and improve the process. One example of this is an initial pilot project at the Berndorf, Austria, location implementing a comprehensive energy management system in production that resulted in significant energy savings.

Analyses & Simulation: Analyses based on the interaction of primary data and the sector- and application-related expertise of Schaeffler's specialists provide information that adds value. Analyses developed in 2017 include an automated acoustics analysis which detects product quality fluctuations. Given the complexity and limited reproducibility of manual tests, this automation has resulted in notable efficiency gains. Efficient data analytics algorithms are used to analyze big data collected. Production accuracy of ball screw drives was significantly increased in this manner, for instance. This approach also helped improve the accuracy of warehouse inventory planning within sales forecasting. The increased accuracy was achieved by training the model based on time series of past orders and connecting the forecasting models to expert knowledge and artificial intelligence.

User Experience & Customer Value: The interaction between humans and machines is a significant factor for productivity in the digital world. The primary objectives are quick recognition and learning as well as goal-oriented interactions between the user and the machine. For instance, a "digital twin" facilitates the digital representation of a physical entity or a system along its lifecycle. It represents an image used to comprehensively exchange or integrate data and functionalities across business processes. An actual application of this is the Engineering Cockpit, which accelerates and improves the development process. Among other benefits, it reduces the amount of effort required to manage configurations and changes. In distribution, the Supply Chain Cockpit creates a personalized digital working environment that facilitates comprehensive process improvements based on modularly adapted data from several source systems. In the field of augmented and virtual reality, initial prototypes for maintenance, special machinery, and tool assembly were realized in cooperation with FAU.

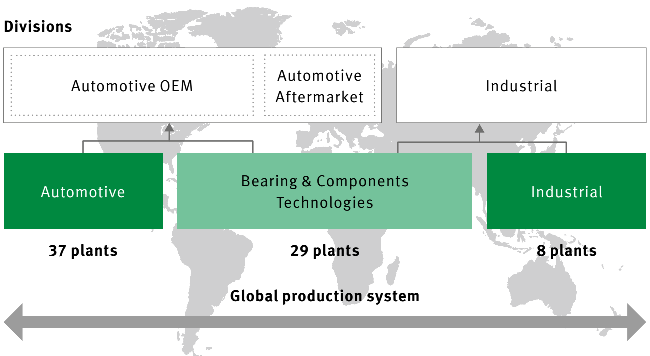
Implementing the four components requires the appropriate IT landscape. To put Schaeffler's IT in a position to successfully meet the challenges of the future, the company has developed the IT 2020 initiative as part of its "Agenda 4 plus One" excellence program. The initiative aims to rapidly put in place the information technology required for Digitalization, for renewing and further developing the application and infrastructure landscape, and for changing the role of IT within the company from that of an internal service provider to that of a strategic business partner shaping and integrating the digital business models. The Process Excellence initiative, part of the "Agenda 4 plus One", creates an organization comprising the clear responsibilities that this requires. To help implement "IT 2020", the company has centralized responsibility for the initiative in the new "Strategic IT" department that was set up in 2017 and will ensure efficient implementation of the initiative. The "IT 2020" initiative involves setting up the digital platform for the Schaeffler Group's own integrated cloud solution, which, based on leading IBM technology, is available worldwide and forms the basis for the future digital ecosystem. This puts in place the foundation for realizing new digital standards and solutions. In addition, the initiative harmonizes the IT architecture model in order to link to and integrate other standard IT solutions such as SAP S/4 HANA, Microsoft Office solutions, or IT security solutions. IT processes are expanded with a specific focus on smart products, processes, and services, as well as on operating more extensive embedded systems solutions.

Operations

Production

As a global automotive and industrial supplier, the Schaeffler Group currently has a global production system consisting of 74 plants in 23 countries. The plants, which employ approx. 65,000 staff, form the core of the Schaeffler production system. They represent the Schaeffler Group's "backbone" and are managed based on uniform principles. The global network of plants, the manufacturing technologies they utilize, and the high degree of vertical integration represent key factors underlying the Schaeffler Group's worldwide success.

Integrated production model No. 011



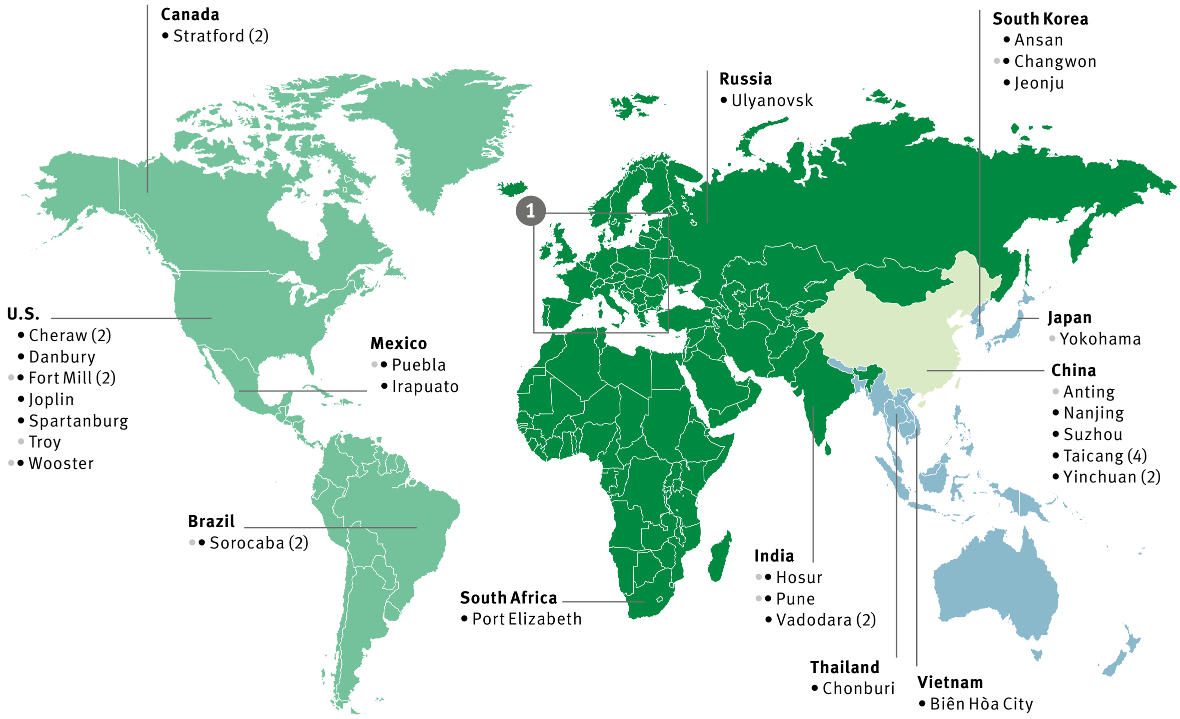
The global production system follows an integrated model. Along with currently 37 plants producing for the Automotive division and currently 8 plants producing for the Industrial division, the internal supplier "Bearing & Components Technologies" (BCT) brackets all of the Schaeffler Group's rolling bearing activities. BCT combines the Schaeffler Group's specialized expertise regarding development and production of rolling bearings and provides it to its internal customers. BCT defines the global standards for rolling bearings within the Schaeffler Group's production system. This streamlines organizational structures, increases transparency and standardization, and generates synergies.

In total, the global production system makes it possible to maintain consistent high levels of quality and efficiency at all Schaeffler plants. The Schaeffler production system is part of the group strategy and, as such, represents the basis for the continuous improvement of quality, cost efficiency, and reliability of supply. Among other things, it facilitates very rapid transfer of innovative methods and processes within the entire network of plants.

Schaeffler Group plants and R&D centers

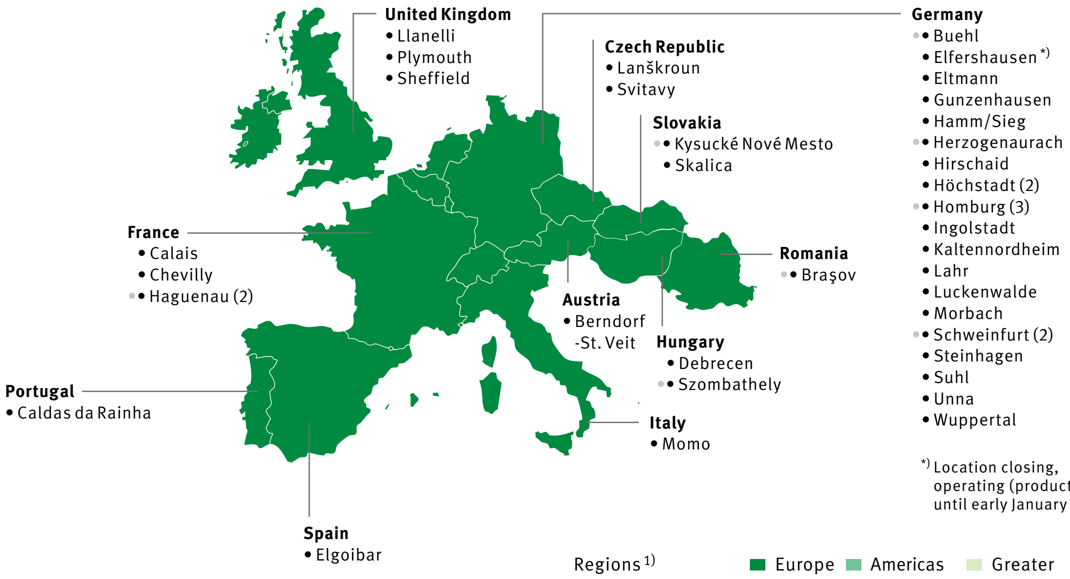
No. 012

World



1 Europe

(enlarged section)



*) Location closing, operating (production) until early January 2018

Regions [1]		Europe	Americas	Greater China	Asia/ Pacific
R&D centers	● (grey)	10	5	1	2
Plants	●	47	14	8	5

[1] Regions reflect the regional structure of the Schaeffler Group.

This standardization accelerates production start-ups and provides flexibility in reacting to regional market fluctuations. As a result, nearly any product can be manufactured at several locations across the globe. The global production system is subject to continuous improvement, with all locations consistently applying the “zero defects principle”. Modern quality management techniques and integrated planning across the entire supply chain ensure that quality requirements are being met. Additionally, continuous value streams between the Schaeffler Group’s customers, plants, and suppliers can be created based on close integration of the network of plants with purchasing and distribution.

2017 was characterized by strong growth, mainly in the Greater China region. The company continued to realize improvements in quality and efficiency, resulting in, among other things, a reduction in the number of customer complaints. In addition, the global production system was consistently advanced with respect to efficiency and proximity to the customer. Examples include shifting capacity to lower-cost locations, closing the Elfershausen location, and restructuring production in Brazil. A further priority was the further expansion of the research and development network, which resulted in considerable improvements in proximity to the customer and response times.

In the future, Digitalization will offer significant opportunities for the global production system. The basis for this is interconnecting plant and machines and equipping them with sensors, which increases autonomy in manufacturing processes. For instance, unplanned downtime was minimized by analyzing machine and production data during ongoing production and using the results to predict machine failures. Combined with elements of “Lean Management”, this generates significant efficiency gains and, therefore, improvements in the Schaeffler Group’s competitive position.

Innovative products require an innovative production environment. Therefore, the company aims to create a production environment promoting this while at the same time handling resources in a sustainable manner. The Factory for Tomorrow concept, an initiative under the “Agenda 4 plus One”, demonstrates solutions in response to this. The Schaeffler Group’s “Factory for Tomorrow” breaks new ground when it comes to designing factories. Under this concept, the Schaeffler Group’s objective is to make the plants attractive for employees while increasing the level of integration of all relevant areas in the value chain. Numerous factory planning projects until 2020 offer the opportunity to put this into practice. For instance, the concept is being implemented at the new plant under construction in Xiangtan, China, for the first time. Insight gained from this pilot project will be used in future projects.

Plants in the regions: A total of 47 plants represent the Schaeffler Group in its **Europe region.** In addition to manufacturing locations in Germany, France, the United Kingdom, Italy, Portugal, and Spain, the group also maintains significant production plants in Central and Eastern Europe. The main plant in Herzogenaurach with its approx. 3,500 production employees ranks among the largest Schaeffler plants and its eight production segments put it among the largest lead production plants worldwide. Along with transmission and steering components, components for the overrunning alternator pulley, and axial bearings, Herzogenaurach also produces complete systems for shifting units, mainly for the automotive sector. A total of just under one billion parts are produced at the Herzogenaurach plant each year. In the future, industrializing electrical axle transmissions under the group’s strategy “Mobility for tomorrow” will be one of its main priorities.

In addition, the “Additive Manufacturing FabShop” was set up at the Herzogenaurach plant. “Additive manufacturing”, colloquially known as 3D printing, covers a number of digital manufacturing methods, in which objects are manufactured by gradually adding material in layers. The FabShop is responsible for developing additive manufacturing into Schaeffler’s manufacturing technology of the future. Along with additive manufacturing of prototypes, tools, and devices from metals and plastics, the Fab Shop team also addresses issues related to process and materials development, design adapted to additive manufacturing, and the additive process chain. In order to ensure that insights are gained very quickly, the FabShop is used to manage a network of expertise in additive manufacturing that includes not only internal experts but also acclaimed external partners in industry and academia.

Production capacity at the Central and Eastern European production plants is continually being expanded due to increasing demand for Schaeffler products. For instance, a new plant was opened in Svitavy, Czech Republic, in 2017. The new plant further strengthens the Schaeffler Group’s network of plants in Eastern Europe, which is already quite strong. The thermal management modules Schaeffler produces in Svitavy are a product that is required in both internal combustion engines and future mobility concepts, and thus supports the Schaeffler Group’s strategy “Mobility for tomorrow”.

The Schaeffler Group operates a total of 14 plants in the **Americas region,** including eight plants in the U.S. (South Carolina (5), Ohio, Connecticut, and Missouri) and two each in Canada, Mexico, and Brazil. In Fort Mill in the U.S., the Schaeffler Group operates two plants with a total of approx. 700 employees. In 2017, the plants at the Fort Mill location were expanded to increase capacity for stamping, heat treating, and the assembly of axial bearings.

In its **Greater China region,** the group operates 8 plants. The persistently high level of demand for Schaeffler products in China requires a continual expansion of local production capacity. As expansion in Taicang and Nanjing has reached its limits, the Schaeffler Group is establishing a new production location in Xiangtan, China, following the "Factory for Tomorrow" concept. It is constructing a plant for automotive parts and precision bearings approx. 200,000 square meters in size. The company intends to expand the new location gradually. Hence, the Tool and Prototyping departments at the new location started operating in 2017. The plant is scheduled to commence full operations in early 2019, which will expand the company's production capacity in the Greater China region, improving its delivery performance to customers in both the home market and in international markets.

The Schaeffler Group has 5 plants in its **Asia/Pacific region.** The plant in Changwon, South Korea, is the largest plant in this region. It is spread over three locations and employs a total of approx. 900 staff. In terms of the value chain, location 1 produces deep groove ball bearings and tapered roller bearings and is vertically integrated from heat treating through to assembly and packaging. A newly installed surface treatment machine will expand vertical integration for Automotive applications. Location 2 is the component supplier – vertical integration ranges from forging soft rings through to turning. Location 3 is a mix of precision bearing manufacturing, tapered roller bearing manufacturing, and special machines, as well as an R&D center. This setup facilitates very efficient and customer-specific process design, from development through to tooling and the full vertical range of manufacturing.

Logistics

The logistics function is responsible for designing, operating, and continually improving the Schaeffler Group's entire supply chain. The primary goal of this function is to maximize customer satisfaction at minimum cost by way of timely, accurate, and efficient supply to all Schaeffler customers and plants worldwide.

In 2017, the logistics function was responsible for managing approx. 210 distribution locations with more than 375,000 square meters in storage space and for moving approx. 300,000 tonnes in freight between the most significant destinations within the Schaeffler Group. More than 120 shipping points ensure deliveries to customers. Logistics activities were expanded compared to the prior year.

A significant element of the strategic alignment of Schaeffler Group logistics is the "European Distribution Center" (EDC) project. This project will create a high-performance logistics network for the Industrial division aimed at improving market supply and delivery performance, thus making an important contribution to strengthening the Schaeffler Group's competitive position. The two warehousing locations "EDC North" (Arlandastad, Sweden) and "EDC South" (Carisio, Italy) have met their performance specifications with a good logistical performance in their first two years of operation. At the central distribution center "EDC Central" (Kitzingen), the next important milestone toward completing the new distribution network, construction is just about complete. The technical equipment is undergoing initial bulk testing, and the first Kitzingen employees are starting their jobs.

European Distribution Center (EDC) Central — No. 013

For the Automotive Aftermarket, the company is currently planning the construction of a new assembly and packaging center to be known as Aftermarket Kitting Operation (AKO). The AKO is part of the "Agenda 4 plus One". The objective of this project is to expand the company's future competitive position and to mitigate any potential capacity bottlenecks at the seven European warehouses currently in operation. The new logistics center, which will be built in Saxony-Anhalt near Halle/Saale with a floor space of about 40,000 square meters, will be the main supply hub for all of the Automotive Aftermarket division's other regional warehouses in Europe. At the same time, it will serve as the regional warehouse for Central Europe. Construction of a new, highly automated logistics location whose capacity can be adjusted flexibly is designed to further optimize Schaeffler's Automotive Aftermarket processes, considerably improve delivery performance, increase customer satisfaction, and secure the forecasted revenue growth. The new logistics center will be commissioned in the first quarter of 2020.

Purchasing

The Schaeffler Group's purchasing function ensures optimal supply of goods and services to the plants taking into account quality, cost, and reliability of supply. By means including involving suppliers in the process of establishing production, it guarantees external supply even before production starts. By consolidating purchasing volumes, the purchasing function contributes to the continual improvement of the Schaeffler Group's supplier network. The key objectives of purchasing remain (1) improving the quality provided by suppliers by cooperating extensively with suppliers, (2) securing competitive procurement costs, and (3) optimizing the supply chain to increase the security of supply by utilizing better logistical connections. In addition, the Working Capital initiative, which is part of the "Agenda 4 plus One", is aimed at adding value by harmonizing purchasing terms.

Purchasing consists of the corporate purchasing function for production and non-production materials, and project-related purchasing for the divisions. In addition, purchasing is divided into the Europe, Americas, Greater China, and Asia/Pacific regions, which incorporate the purchasing function for the respective plants.

In 2017, the Schaeffler Group reported an operational increase in the total volume of purchases compared to the prior year. The volume of production material (raw materials and components) included here rose in proportion to the increase in production output. The purchasing volume in general purchasing (non-production materials, i.e. primarily intangible assets, property, plant and equipment, tools, supplies, and services) was higher than in the prior year. The Schaeffler Group was able to ensure supply to its plants around the world at all times in 2017. Purchases related primarily to the Europe (63.8%) and Americas (16.2%) regions. 13.6% and 6.4% related to the Greater China and Asia/Pacific regions, respectively.

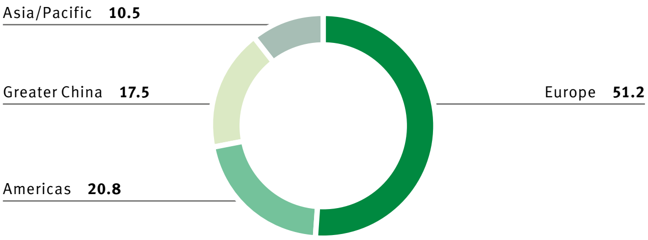
The Schaeffler Group uses various raw materials such as steel (flat steel or steel bar), iron and aluminum casting, as well as non-ferrous metals in manufacturing its products. The production materials Schaeffler uses primarily depend, directly or indirectly, on the trend in the price of scrap steel, coking coal, and iron ore, as well as non-ferrous metals. Price changes are normally either passed on indirectly with a time-lag via changes in costs charged by suppliers or via new prices during contract negotiations.

Continental Group and the Schaeffler Group have been cooperating on purchasing for eight years. Both companies benefit from improvements in cost structures from combining purchasing volumes. By utilizing synergies resulting from numerous cross-regional projects and programs, the Schaeffler Group was able to further improve its cost of materials in 2017.

Regions

The Schaeffler Group's three-dimensional matrix organization divides the company's business not only into divisions and functions, but also groups the company's activities into the four regions Europe, Americas, Greater China, and Asia/Pacific. Each of the Schaeffler Group's four regions is managed by a Regional CEO, who is a member of the Schaeffler Group's Executive Board. This organizational arrangement allows for flexible management of the regions and facilitates cooperation with regional customers.

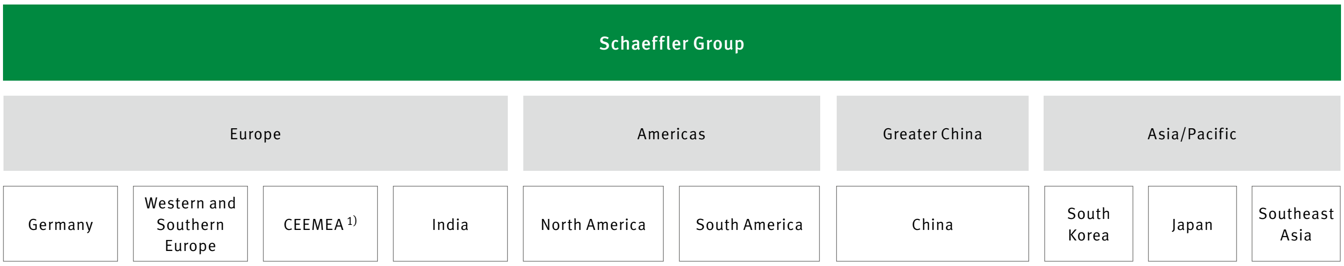
Schaeffler Group revenue by region No. 014
in percent by market view



The basis for the Schaeffler Group's economic success is its proximity to the customer. With approx. 170 locations worldwide, 74 production facilities, 18 research and development centers, and a tight-knit sales and service network, the Schaeffler Group ensures that its customers always find it close at hand – true to its guiding principle: "We are a global player with a local presence". Cooperation across divisions and countries thus leads to a high degree of flexibility in solving new customer requirements and the opportunity of anticipating emerging trends early on.

In its Global Footprint initiative, which is part of the "Agenda 4 plus One", the Schaeffler Group is continually working to further develop its global stature. Among other things, the initiative includes creating and expanding regional research and development expertise, enhancing the structure of the global plant network and logistics activities, as well as realigning the distribution locations. In light of this, proactively localizing activities in the markets of the future constitutes one of the key challenges in implementing the strategy "Mobility for tomorrow". It also demands thinking even more deeply in terms of global connections and delegating responsibility away from head office in the future. In addition to better acceptance due to cooperation with local customers and suppliers, the Schaeffler Group's increasing localization results in efficiencies in purchasing and logistics as well as several benefits regarding sustainability and the environment. The resulting growing regional presence is also reflected in a high degree of localization. The degree of localization describes the relation of a region's total sales to sales volume manufactured in that region.

Schaeffler Group regions and subregions No. 015



[1] CEEMEA = Central and Eastern Europe & Middle East and Africa.

The **Europe region** combines the subregions Germany, Western and Southern Europe, Central and Eastern Europe & Middle East and Africa (CEEMEA), as well as India. The Western Europe and Southern Europe subregions were combined into one subregion in 2017 in order to further simplify the organizational structure. The Germany subregion represents the Schaeffler Group's most important sales market. The Europe region contributed 51.2% (prior year: 53.1%) of consolidated revenue in 2017. The degree of localization amounted to approx. 96% (prior year: 96%) in 2017. The Europe region employed a total of 61,554 employees in 2017, representing 68.3% of the company's entire workforce. This figure includes the employees of the group's global head office in Herzogenaurach. The region has 47 plants and 10 R&D centers. Its regional head office is located in Schweinfurt.

In 2017, the Schaeffler Group further strengthened its network of plants in Eastern Europe, which is already quite strong, by opening the new plant in Svitavy, Czech Republic. As part of the measures taken to intensify the company's research and development activities in the growth region India, the Hosur location was developed into an R&D center focusing on clutch systems. Another focus was on streamlining the legal structure and on the synergies to be realized from better collaboration across companies in India. The result is a plan to merge the three Indian subsidiaries into one company. The merger is subject to the required local regulatory approvals and the consent of the minority shareholders. The transaction is expected to close in the third quarter of 2018. The company will be known as "Schaeffler India Limited".

In addition, a new shared service center will be set up for the Europe region as part of the strategic Shared Services initiative. The objective of the initiative is to develop a global, forward-looking, and cross-functional shared services concept, standardize and harmonize transaction processing, and further improve processes. The first processes to be combined, optimized, and digitized with a view to these objectives are those in Finance, Human Resources, Purchasing, Logistics, and IT. The improvements in the indirect areas resulting from the new shared service center for the Europe region affect several German and European locations.

The **Americas region** consists of the two subregions North America and South America. This region contributed 20.8% (prior year: 21.0%) of revenue in 2017. The degree of localization amounted to approx. 71% (prior year: 71%) in the Americas region. A total of 13,056 staff were employed at 14 plants and 5 R&D centers as well as at distribution locations in North and South America. The Americas region has its regional head office in Fort Mill in the U.S. The Schaeffler Group has been manufacturing in this region since 1953. In 2017, the plants in Fort Mill were expanded and a new multifunctional administrative building, adapted to the new work environments of the New Work initiative, was opened. The company also invested in an expansion of the production area at the Wooster location in the U.S. Starting in 2018, the plant will manufacture products including hybrid modules on the additional production area of 8,900 square meters. This makes Wooster one of the Schaeffler Group's centers for further developing electric mobility in the U.S.

As China is a strategically important sales market for the Schaeffler Group, China, Taiwan, and Hong Kong are managed as a separate **Greater China region.** The regional head office is located in Anting in metropolitan Shanghai, China. Schaeffler's first subsidiary in this region was founded in Taicang, China, in 1995. The region generated 17.5% (prior year: 15.4%) of group revenue in 2017. The degree of localization amounted to approx. 73% (prior year: 74%). A total of 12,537 staff were employed in Greater China. 8 plants and 1 R&D center are located in this region. As a consequence of the especially dynamic trend in recent years, it is important to the company to further expand not only E-Mobility, but also its local presence and to consistently raise the degree of localization in the future. At its Xiangtan location in China, the Schaeffler Group is building its first "Factory for Tomorrow". While the first production plant is scheduled for commissioning in early 2019, a training center was already opened officially in mid-June 2017. Employees are qualified based on the German dual system of vocational training.

The **Asia/Pacific region** comprises South Korea, Japan, and the countries in Southeast Asia. The Schaeffler Group has been represented in this region since 1953. 10.5% (prior year: 10.5%) of group revenue was generated by this region in 2017. The degree of localization amounted to approx. 38% (prior year: 38%) in 2017. The Asia/Pacific region had 3,004 employees. The regional head office is located in Singapore. The Schaeffler Group operates a total of 5 plants and 2 R&D centers in this region. By opening a new plant in Bien Hoa City, Vietnam, the group is considerably expanding its production capacity in the Asia/Pacific region. Furthermore, due to the strong presence of robotics manufacturers in this region, it was agreed that Schaeffler Asia/Pacific would take the lead in creating a robotics competence center in consultation with the Industrial division. Along with the current component business, the competence center will also coordinate development and testing of mechatronic systems and Digitalization services for robotics applications.

1.3 Group strategy and management

Strategy "Mobility for tomorrow"

The Schaeffler Group is a global automotive and industrial supplier. Top quality, outstanding technology, and exceptionally innovative spirit form the basis for the continued success of the company. By delivering high-precision components and systems in engine, transmission, and chassis applications, as well as rolling and plain bearing solutions for a large number of industrial applications, the Schaeffler Group is already shaping "Mobility for tomorrow" to a significant degree.

In late 2016, the Schaeffler Group developed its strategy "Mobility for tomorrow" to guide its way into the future and presented it to the public. The company continued to press forward with the implementation of this strategy in 2017: For instance, creating the new E-Mobility business division and the organizational unit Industry 4.0 set the course for future development in two key future-oriented fields. All initiatives under the "Agenda 4 plus One" excellence program are in the implementation phase. Implementation of the program is currently 35% complete. Following extensive communication measures, the strategy is fully known and understood throughout the company. All strategic activities, ranging from design right through to implementation and communication, focus on the same fundamental elements: one common vision and mission, 4 focus areas, 8 strategic pillars, and the 20 strategic initiatives of the "Agenda 4 plus One".

Vision and mission

In its mission, the Schaeffler Group describes the task it is committed to. Underlying this mission are three key concepts: working in partnership with all customers and business partners, top-level expertise in manufacturing technology, and advanced systems know-how. The Schaeffler Group's vision and mission mutually complement and amplify each other, with the vision describing the aspirations that will guide the group's activities in the future.

Schaeffler Group mission and vision No. 016

Mission

"Guided by the values of a global family business, we work closely together with our customers as true partners to deliver a compelling value proposition through our best-in-class expertise in manufacturing technology and systems know-how. In doing so, we contribute to the success of our customers, the advancement of our employees, and the prosperity of our society."

Vision

"As a leader in technology, we combine a passion for innovation with the highest standards of quality to shape the future of mobility – for a world that will be cleaner, safer, and smarter."

Mobility for tomorrow – 4 focus areas No. 017

4 Focus areas

As its fundamental assumption about the future of its markets, the Schaeffler Group has identified four megatrends that will significantly influence its future business: climate change, urbanization, globalization, and digitalization. From these megatrends, the Schaeffler Group derived 4 focus areas that form the basis for the company's strategic direction.

(1) Eco-friendly drives

One of the primary goals of the Schaeffler Group is to develop energy-efficient drive systems with low or zero emissions. In the automotive field, this means on the one hand further optimizing conventional combustion engines, and on the other hand developing drive solutions in the area of E-Mobility, whether for vehicles with hybrid drive trains or for battery-electric vehicles. Key components such as variable valve-control systems, the thermal management module, wet and dry double-clutches, and electronic control modules help reduce CO_2 emissions of conventional drives based on internal combustion engines. In addition, for the Schaeffler Group's automotive customers, innovative products for the field of electric mobility, such as hybrid modules, the electric axle drive, or the wheel hub motor "E-Wheel Drive", play an increasing role in achieving lower CO_2 emission targets. The same logic can be applied to modern industrial drive systems, where the Schaeffler Group's wealth of knowledge in the automotive field is essential.

(2) Urban mobility

The shift in mobility is nowhere as noticeable as it is in megacities across the globe. At the same time, it is nowhere as necessary. Cities like Moscow, Tokyo, or Shanghai experience a daily traffic volume in which fast and flexible movement is almost impossible. At the same time, more and more cities are banning cars from their downtown areas. This trend calls for new mobility solutions, whether in micro-mobility or by designing more efficient public transit. Responding to this trend, the Schaeffler Group is further expanding its product portfolio for hybrid and electric mobility. Its torque sensor bottom brackets, for instance, have positioned the Schaeffler Group as an innovative supplier in the growing e-bike market, and the "Bio-Hybrid" micro mobile and the "Torque Stick Board" nano mobile demonstrate its strong innovative ability in this area.

(3) Interurban mobility

The term interurban mobility means interconnecting global centers. As globalization progresses, traffic will increase significantly worldwide over the years to come, particularly rail and air traffic, and require a large degree of flexibility. Providing modern and efficient mobility solutions presents a key challenge to both industries. The same is true for the off-highway sector, including agricultural technology, outside the cities. In this area, the Schaeffler Group and its innovative rolling bearing solutions and exceptional systems know-how are set to lead the market.

(4) Energy chain

Common to all of the focus areas mentioned above is the continuing need for the cleanest energy possible. In light of dwindling resources and significant climate challenges, worldwide demand for clean energy is growing. Schaeffler partners with the energy sector, assisting in the development of renewable energy production and focusing on wind power, hydropower, and solar power. In conventional energy generation as well, the Schaeffler Group sees opportunities for expanding its range of products and services. After all, ultimately all segments of the energy chain – from its production to its transport and conversion to energy consumption, must be optimized further. Hence, in addition to conventional energy generation, Schaeffler also offers a comprehensive portfolio of products in the field of renewable energy – from bearing solutions for wind turbines through to solutions for solar and water power.

8 Strategic pillars No. 018

1. We want to be the preferred technology partner for our customers.
2. We are an Automotive and Industrial supplier.
3. We are a global company with a local presence throughout the world.
4. We produce components and systems.
5. We view E-Mobility, Industry 4.0, and Digitalization as key opportunities for the future.
6. We strive for the highest possible quality, efficiency, and delivery performance.
7. We want to be an attractive employer.
8. We live by the values of a global family business.

8 Strategic pillars

The strategy "Mobility for tomorrow" defines the company's scope for future action and constitutes the basis for the continuous further development of the Schaeffler Group. In order to describe this scope for action in a manner that is specific and easily understood, the company has devised 8 strategic pillars that describe what Schaeffler wishes to achieve or further improve in the future.

1 We want to be the preferred technology partner for our customers.

For many years now Schaeffler's comprehensive systems know-how, cutting-edge technological expertise, and unwavering commitment to customer service have made the company a highly sought-after development partner for its customers in the automotive and industrial sectors. On this basis, the Schaeffler Group will continue to shape the mobility of the future together with its customers.

2 We are an Automotive and Industrial supplier.

The Schaeffler Group is an automotive and an industrial supplier. The two divisions are united by the Schaeffler Group's worldwide manufacturing excellence and global platform of production facilities combined with economies of scale in purchasing materials and commodities. In addition, Schaeffler's global research network facilitates cross-divisional technological innovations. Diversification across divisions will continue to generate synergies and promote the transfer of know-how in the future.

3 We are a global company with a local presence throughout the world.

With its approx. 170 locations worldwide, 74 production facilities, 18 research and development centers and a tight-knit sales and service network, Schaeffler ensures that the customer always finds it close at hand. For only those who recognize and understand the challenges confronting their customers can develop tailored solutions. And only those who maintain a local presence are able to respond quickly.

4 We produce components and systems.

Schaeffler supplies components for products that facilitate and promote mobility. At the same time, the company understands and is able to deliver complex modules and complete system solutions. Schaeffler values both business segments equally. And for good reason: Those without expertise in components will not be able to handle the system.

5 We view E-Mobility, Industry 4.0, and Digitalization as key opportunities for the future.

As a leading technology partner, the Schaeffler Group began engaging in the topics of E-Mobility, Industry 4.0, and Digitalization years ago and has made these areas a clear priority. As a supplier, Schaeffler wants to take an active role in shaping this development for its customers and considers this a key future opportunity.

6 We strive for the highest possible quality, efficiency, and delivery performance.

Quality is of paramount importance for Schaeffler. It has always had the goal to consistently ensure high quality and product safety in all applications. Another Schaeffler goal is to serve its customers with the highest-possible efficiency and delivery performance.

7 We want to be an attractive employer.

The Schaeffler Group's employees are vital for guaranteeing its success. Identifying, promoting, and retaining the best team for the Schaeffler Group in the long term is crucial for the successful realization of the company's strategy. The Schaeffler Group is not only concerned about new employees here. Rather, it wants to be an attractive employer for all of its employees.

8 We live by the values of a global family business.
The Schaeffler Group is a listed family business. A company with a strong foundation of values, established by its founders. Schaeffler particularly identifies with the corporate values "Sustainable", "Innovative", "Excellent", and "Passionate". These values form the basis for the continued success of the Schaeffler Group for the benefit and in the interest of its customers and business partners, employees and managers as well as its shareholders and family shareholders.

Four corporate values No. 019

Sustainable
A long-term view and continuity will foster the growth of the Schaeffler Group, thereby enabling a future worth living.

Innovative
For (nearly) every problem there is a solution. If not, we will create one!

Excellent
We develop solutions that are of the highest quality based on our extensive expertise.

Passionate
Our biggest driver is our passion for innovative technologies and joint success with our customers.

20 Strategic initiatives

In execution of the strategy "Mobility for tomorrow", the company launched its "Agenda 4 plus One" excellence program with the Schaeffler Group's 16 most significant strategic initiatives in 2016. The strategic initiatives are grouped in 4+1 categories: Customer focus, Operational excellence, Financial flexibility, Leadership and talent management, and – as "plus One" – securing long-term competitiveness and value creation.
All initiatives have the same objective: positioning the Schaeffler Group for the future and making it even better. The stated aim is to successfully implement all initiatives by the end of 2020, i.e. in 4+1 years. Each initiative is the responsibility of a member of the Executive Board as a sponsor, managed by a project manager, and supported by a project organization.
A program office was established to coordinate the management of the strategic initiatives and thus ensure the success of the "Agenda 4 plus One".

Once the program organization was successfully set up and had proven its worth, the Executive Board decided to expand the program by four additional initiatives, increasing the number of initiatives to 20 effective January 01, 2018: "Global Supply Chain", "Aftermarket Kitting Operation" (AKO), "Global Reporting", and "Focus". This will ensure the initiatives are successfully implemented in a consistent format.

The ⊙ Global Supply Chain initiative focuses on optimizing global supply chains taking into account integrated planning and the interfaces between production and distribution. The initiative is designed to improve working capital, speed up delivery, and improve delivery performance.

The ⊙ Aftermarket Kitting Operation initiative involves the construction of a state-of-the-art assembly and packaging center – AKO for short – for the Automotive Aftermarket designed to further optimize Automotive Aftermarket processes and generate sustained improvements in quality of delivery.

The ⊙ Global Reporting initiative is aimed at improving the Schaeffler Group's consolidation and reporting systems as well as management information.

The fourth new initiative, the ⊙ Focus initiative, will deal with improving the building situation at the company's main locations in Germany and is designed to increase efficiency and improve space requirements as well as appearance.

Like these four initiatives, all 16 initiatives originally planned are in the implementation phase. They have reached varying maturity levels depending on their scope. The following discusses selected key successes achieved over and above those already addressed elsewhere in the annual financial report. A transfer to or establishment of business units or line functions will ensure that the initiatives are implemented for the long term.

First and foremost, there are the ⊙ E-Mobility and ⊙ Industry 4.0 initiatives. As a result of the growing number of customer projects and in order to accommodate the increasing significance of these activities, dedicated business units were set up for both effective January 01, 2018. The E-Mobility business division brings together all products and system solutions for hybrid and pure battery-electric vehicles. Due to the significance of the Chinese market, a second competence center will be set up in China in 2018 as well. In the Industrial division, the entire industry-specific business with mechatronic systems and digital services as well as the required related components are being combined in an independent organizational unit Industry 4.0. As a supplier, Schaeffler wants to take an active role in shaping the digital transformation for its customers with Industry-4.0-enabled products.

Agenda 4 plus One No. 020

Schaeffler has been at its customers' side as an expert solution partner for many years, a connection that has always been key to innovation. The ⦿ Customer Excellence initiative moves this customer-focused culture further into the spotlight. It especially aims to continually improve and optimize the company's dialog with the customer, customer interaction, and customer relationship management.

An appropriate, customer-oriented structure is essential for the indirect functions as well. The objective of the ⦿ Shared Services initiative is to set up a powerful, cross-functional shared services organization. Starting with the first shared services units that are already well-established, this initiative will create a global network of coordinated multifunctional shared services locations embedded in the regions. Prerequisites include a new group process model with clear responsibilities that was developed in the ⦿ Process Excellence initiative and can now be used in a next step to optimize processes.

The company's brand identity and corporate image are harmonized under the ⦿ Global Branding initiative. In future, the Schaeffler Group, as a company with operations worldwide, will focus on the "Schaeffler" corporate brand. This will illustrate its commitment to growing together even more as a listed family business. This will only work with one common strategy, one corporate brand, one remuneration model, and one strong foundation of common values. Harmonizing the Schaeffler Group's corporate image around the world will reduce the complexity of the group's current brand architecture while at the same time strengthening its corporate brand. The individual product brands, such as INA, LuK, and FAG will remain, but will be used only in connection with the related product and in conjunction with the Schaeffler corporate brand. In Schweinfurt, this initiative has already started. The Schaeffler Group plans to move all Schaeffler locations worldwide to the new branding concept by the end of 2019.

Financial Ambitions 2020

The company intends to grow its revenue – excluding the impact of currency translation – by an average of 4 to 6% per year over the coming years and to achieve an EBIT margin before special items of 12 to 13% by 2020. On this basis, the Schaeffler Group wants to achieve free cash flow before cash in- and outflows for M&A activities of approx. EUR 900 m by 2020. Furthermore, the group intends to increase its earnings per share to approx. EUR 2.00 in 2020. In addition to these operational indicators, it is critically important for the success of the Schaeffler Group to further improve its financial flexibility and the quality of its balance sheet. For this purpose the company has set itself the task of managing the ratio of net financial debt to equity – known as the gearing ratio, the quotient of the two variables – to be less than 75% by 2020. Moreover, the Schaeffler Group is planning to pay out dividends amounting to 30 to 40% of annual net income before special items to its shareholders. Summarizing the Financial Ambitions 2020, the Schaeffler Group wants to maintain and secure in the long term the investment grade rating gained in 2016, as it represents the basis for further growth strategies.

All these ambitions can ultimately be merged into one key objective: The Schaeffler Group wants to continue to grow profitably and create sustainable value.

Financial Ambitions 2020 No. 021

Revenue growth	**Ø 4 – 6% p. a.** at constant currency
EBIT margin	**12 – 13%** before special items in 2020
Free cash flow [1]	**~ EUR 900 m** in 2020
Earnings per share	**~ EUR 2.00** per share in 2020
Gearing ratio [2]	**‹ 75%** in 2020
Dividend [3]	**30 – 40%** of net income

[1] Before cash in- and outflows for M&A activities.
[2] Net debt to equity ratio (excluding pensions).
[3] Dividend payout ratio based on net income.

Market assumptions
Automotive sector: Global growth in passenger vehicle production of 2%
Industrial sector: Low single-digit growth in global industrial production.

M&A strategy

The Schaeffler Group pursues a strategy of mainly organic growth based on its existing technological expertise and innovative edge. Under this strategy, acquisitions will primarily be made if they add technological value or strengthen the Schaeffler Group's current market position. The company will generally focus on acquisitions related to the future-oriented fields of E-Mobility, Industry 4.0, and Digitalization.

For this purpose, the company has defined the details of key elements of its M&A strategy and further developed its M&A process in 2017. At the core of this approach is an M&A radar that is applicable groupwide and defines seven focus areas where the company is aiming to acquire expertise and generate inorganic growth both within the various divisions and across divisions. The company's search for opportunities to expand the profile of its expertise and its portfolio specifically targets these clearly defined areas. It focuses on smaller, additive targets with a transaction volume in the nine figure range intended to complement and strengthen the technology spectrum, thus adding long-term value.

Having already successfully acquired Compact Dynamics GmbH in late 2016, Schaeffler acquired autinity systems GmbH, an IT company based in Chemnitz, Germany, in the context of Industry 4.0 and Digitalization in a variety of industrial applications in 2017. The acquisition builds on the existing collaboration between the two companies and allows the Schaeffler Group to benefit especially by accelerating further developments in the fields of machine data recording and condition monitoring.

Strategy communication

Following the announcement of the strategy "Mobility for tomorrow" in late 2016, the Board of Managing Directors explained the strategy in person to selected management and employees at international townhall meetings. This was supported by extensive further communication, especially in the form of a strategy brochure and various focal points in the company's online and print communication. On this basis, the company's strategy and future direction were also communicated to individual customers and business partners.

Also in 2017, the strategy was rolled out to all employees at the various Schaeffler Group locations based on a comprehensive roll-out plan using a variety of media in the Schaeffler Group's four regions. The key elements of this communication were presentations and workshops with manufacturing plant employees and administrative staff as well as communication mainly via print media and digital platforms. On this basis, the core elements of the strategy – mission and vision, 4 focus areas, 8 strategic pillars, 20 strategic initiatives and the corporate values – are embedded within the company in a uniform manner for the long term. The company is planning additional activities for the coming years to ensure a long-term understanding of the strategy and to refresh knowledge of its contents.

Strategy and planning process

The Schaeffler Group goes through an annual strategy and planning process comprising three key components, (1) the Technology Dialog, (2) the Strategy Dialog, and (3) the Planning Dialog, that sequentially build on one another.

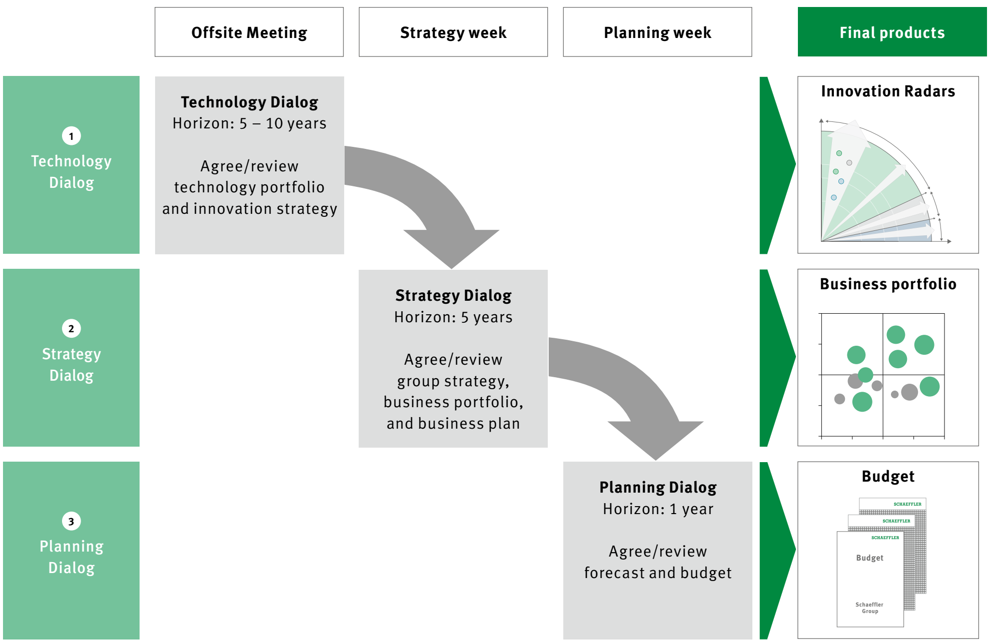
The starting point is the **Technology Dialog** that primarily deals with the megatrends and the resulting impact on technology and innovation. The time frame considered is 5 to 10 years into the future. Based on the information developed, an "Innovation Radar" is approved containing and prioritizing the initiatives aimed at securing the Schaeffler Group's profitable growth over a period of 5 to 10 years. However, this requires investing in intangible assets and property, plant and equipment and starting research and development activities early on. The initiatives approved in the Technology Dialog are further refined during preparation for the Strategy Dialog.

The **Strategy Dialog** takes place mid-year. It focuses on the Schaeffler Group's business strategy (including indicative business plan) for the coming 5 years, the substrategies for the divisions with their strategic business units, the regions, and the functions. A detailed market analysis and an analysis of the initial internal position represent the starting point. Building on these, strategic initiatives are developed from which an indicative business plan can be derived. As part of the process, the various substrategies are coordinated with one another, prioritized, and added to where necessary.

In the Strategy Dialog 2017, specific business cases were developed for selected topics; these business cases systematically compare the quantitative and qualitative outcome of an initiative to the resources and investments required, enabling the Board of Managing Directors to make immediate strategic decisions. The company also defined overarching focus issues for the development of the substrategies, ensuring the various organizational units are aligned consistently. Additionally, as in prior years, numerous initiatives of the divisions, regions, and functions were identified and are being implemented and followed up on within the relevant units.

The results of the Strategy Dialog form the starting point for deriving the top-down objectives for the coming budget year. In the subsequent bottom-up process, the objectives are defined in detail, validated on a bottom-up basis, and the overall plan adjusted if necessary. During the **Planning Dialog** in October, the Executive Board approves the detailed budget for the first planning year. The results of the strategy and planning process are presented and approved at the following meeting of Schaeffler AG's Supervisory Board. The results of the planning process represent the starting point for the key financial performance indicators discussed in the report on expected developments and become part of the agreed objectives of the Managing Directors and management.

Strategy and planning process No. 022



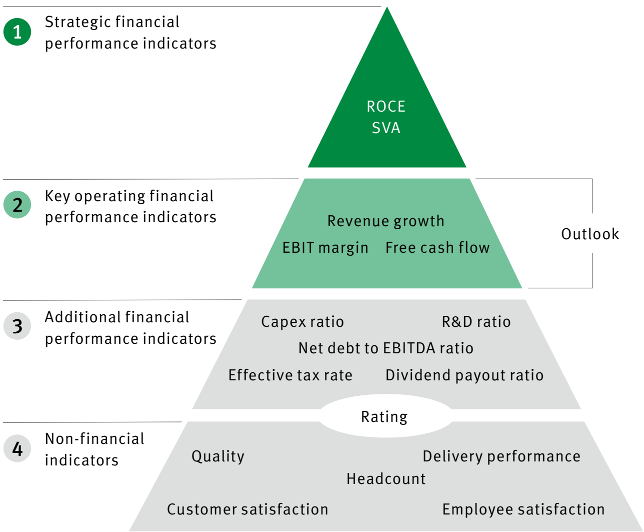
Group management

Schaeffler AG's Board of Managing Directors is directly responsible for managing the Schaeffler Group, setting objectives and the strategic direction, and managing the implementation of the growth strategy. The Supervisory Board of Schaeffler AG appoints, supervises, and advises the Board of Managing Directors.

In 2017, the Schaeffler Group's management utilized a three-dimensional matrix organization consisting of two divisions, five functions, and four regions to manage the group's business activities. In the context of this matrix organization, the Schaeffler Group's business was primarily managed based on the Automotive and Industrial divisions. Effective January 01, 2018, the Automotive Aftermarket was set up as a third stand-alone division. As a consequence, the Schaeffler Group has primarily been managing its business based on three divisions – Automotive OEM, Automotive Aftermarket, and Industrial – since January 01, 2018.

The Schaeffler Group's internal management system consists of the annual budget developed based on the strategic framework specified by the Board of Managing Directors, ongoing monitoring and management of financial performance indicators, regular meetings of the Board of Managing Directors and management, as well as reports provided to the Supervisory Board of Schaeffler AG. Ongoing monitoring and management is based on a comprehensive system of standardized reports on net assets, financial position, and earnings. Discussions at the meetings of the Board of Managing Directors and of management address the results of operations, including the achievement of targets and objectives, as well as the outlook for the year as a whole and any action that may be required.

Management system No. 023



Value-based management

The Schaeffler Group's internal management system is designed to support implementation of the group strategy. Ensuring that the Schaeffler Group continues to meet its core business objective of growing profitably and creating long-term value necessitates a value-based approach to managing its business portfolio. One important principle underlying value-based management of companies is the necessity to reflect the interests and needs of investors.

Value-based management is an integral component of all planning, management, and control processes. Schaeffler's success-based management remuneration is directly linked to the economic development of the company as well.

1 Strategic financial performance indicators

In order to grow profitably and create long-term value, the company has to employ its available capital profitably. Having earnings sustainably exceed the cost of available debt and equity capital creates the fundamental basis for this.

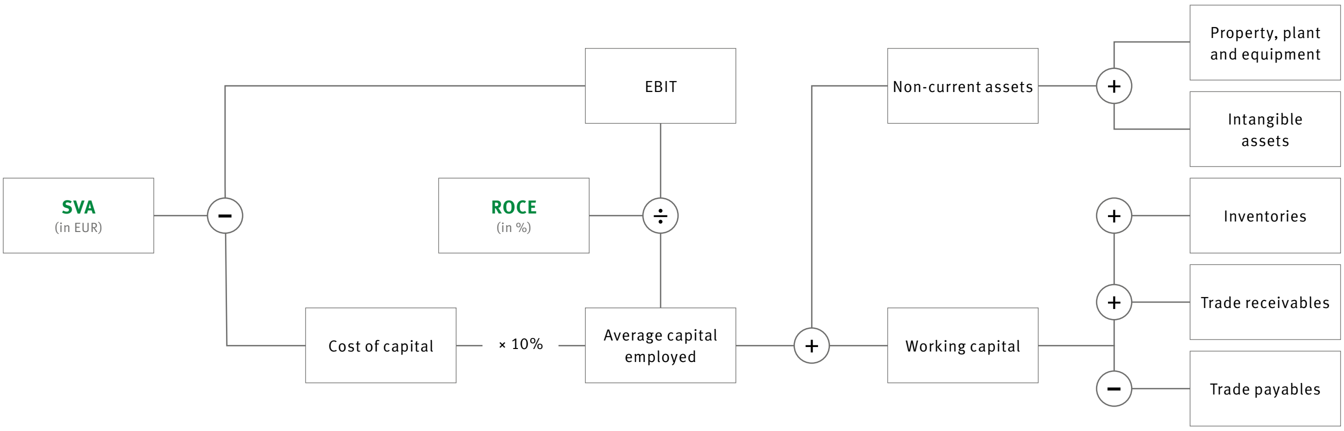
The Schaeffler Group's internal management system consists of several levels. The Schaeffler Group's key value-based performance indicator is **return on capital employed (ROCE)** as well as **Schaeffler Value Added (SVA),** which is closely linked to ROCE. Schaeffler Value Added represents a key performance criterion within the framework governing the variable short-term remuneration of the Board of Managing Directors and the remuneration at the next-lower levels of management. Both indicators are determined before special items.

More on special items on pp. 60 et seq.

Schaeffler Value Added (SVA): The Schaeffler Group's value added is measured using the amount of value added by the company, referred to as Schaeffler Value Added (SVA). Calculation of the SVA starts with the company's EBIT (earnings before financial result and income taxes). EBIT has to be sufficient to cover the cost of capital. Positive SVA means that EBIT has exceeded the cost of capital for the period and, therefore, that the Schaeffler Group has added value in this amount. Cost of capital is calculated by applying the minimum return of 10% p.a. (before tax) set by the Board of Managing Directors and the Supervisory Board to the average capital employed during the year.

Average capital employed is calculated by adding up the following operating balance sheet items: property, plant and equipment, intangible assets, and working capital, which in turn comprises trade receivables and inventories net of trade payables. The annual average is determined as the mathematical average of the balance at the end of each of the four quarters.

Strategic financial performance indicators No. 024



Return on Capital Employed (ROCE): While Schaeffler Value Added is an absolute measure of the value added by the company, ROCE measures the relative return on capital employed in percent. The ROCE indicator measures the rate of return on capital and is defined as EBIT divided by average capital employed. The indicator shows how efficiently a company manages the use of its resources. Comparing ROCE to the cost of capital answers the question of how much value was added. If ROCE exceeds the cost of capital, the company is adding value. Thus, ROCE serves as a tool for value-based management.

2 Key operating financial performance indicators

The two indicators ROCE and SVA serve as indicators of the amount of shareholder value added during the year. However, their high level of aggregation makes using them as a basis for targeted operational management difficult. Therefore, these indicators are mainly used for reporting purposes.

Consequently, at group level, the objectives of profitable growth and adding long-term value are operationalized using key financial performance indicators. Thus, the Schaeffler Group focuses on continually monitoring and optimizing the following three key operating financial performance indicators:

- **Revenue growth (at constant currency)**
- **EBIT margin (before special items)**
- **Free cash flow**

These three key operating financial performance indicators represent the basis for operating decisions and also form the basis for the outlook. Overall optimization of these indicators adds shareholder value for the long-term by sustainably generating a premium over and above the cost of capital.

Revenue growth (at constant currency): Since the Schaeffler Group's economic success is based on a long-term growth strategy, significant importance is attached to the performance indicator revenue growth. Revenue growth is a relative indicator and measures the change in revenue compared to the prior year. In order to increase the comparability over time, the Schaeffler Group reports revenue growth at constant currency.

EBIT margin (before special items): The EBIT margin is used as an indicator of the Schaeffler Group's operating performance. The EBIT margin is a relative indicator calculated as the ratio of EBIT to revenue. This ratio measures the company's profitability and indicates how successfully the company's operating business is being managed. Thus, group management ensures that the Schaeffler Group is growing profitably while utilizing capital efficiently. The EBIT margin is calculated before special items in order to make the operating performance more comparable over time.

Free cash flow: Traditionally, the Schaeffler Group's growth has been financed from internal sources. The primary performance indicator of the group's ability to generate internal financing is free cash flow, which is defined as the sum of cash flows from operating activities and cash flows from investing activities. Free cash flow measures the company's ability to convert its operating performance to cash inflows in order to finance ongoing operations and any required capital expenditures from the company's own operating activities. Along with profitability, the key factors affecting free cash flow are effective management of working capital as well as the level of capital expenditures.

In order to improve comparability over time, the Schaeffler Group will report free cash flow, one of its key operating financial performance indicators, before cash in- and outflows for M&A activities beginning in 2018.

More on trends in the indicators discussed above under "course of business" on pp. 50 et seq.

3 Additional financial performance indicators

In addition to the three key operating financial performance indicators, the Board of Managing Directors also continually tracks additional financial performance indicators including, among others, the capex ratio, R&D ratio, net debt to EBITDA ratio, effective tax rate, and the dividend payout ratio.

The company further monitors a number of leading **operating indicators** in order to be able to identify trends in a multitude of factors affecting the Schaeffler Group's business early on and take them into account in managing the company. For instance, the company analyzes forecasts of relevant market, economic, and sector data, such as gross domestic product, currency trends, as well as automobile and industrial production in order to gain important insight into the future of the business. Raw materials prices are monitored as well in order to estimate trends in significant costs.

In order to obtain a reliable indication of the likely level of capacity utilization and the probable revenue trend, Schaeffler also monitors certain leading operating indicators specific to each division.

- **Automotive OEM:** Multi-year master agreements won within one period are measured using the indicator "lifetime sales" on an ongoing basis and compared to current period revenue by calculating the "book-to-bill ratio", which provides an indication of the medium- to long-term utilization of the Automotive OEM division's capacity. Orders received for short-term delivery under master agreements with customers validly cover a period of approx. two months. Changes in this measure of capacity utilization are monitored on a weekly basis.
- **Automotive Aftermarket:** For the Automotive Aftermarket, no comparable leading indicators can be derived from the volume of order intake or orders on hand. This division holds regular discussions with major customers and observes its markets to obtain leading indications of the short-term demand situation.
- **Industrial:** The Industrial division uses the change in orders on hand due within the following three months as a leading indicator. This figure is monitored on a monthly basis.

All financial indicators are calculated on a monthly basis using standardized reports on earnings, financial position, and net assets. These reports contain a comparison of budget vs. actual as well as a prior year comparison. The comparison of budget vs. actual is based on the annual budget flowing from the integrated operating budget embedded in a longer-range strategic corporate plan established by the Board of Managing Directors.

4 Non-financial indicators

In addition to the financial performance indicators, management monitors additional key non-financial indicators. Such indicators are calculated using standardized reports during the year and include: quality, headcount, delivery performance, customer satisfaction, employee satisfaction, and rating.

Further non-financial indicators were defined for sustainability management purposes. Thus, the company has defined a set of key figures for each field of action addressed in the sustainability strategy, used to manage the operation of the group's sustainability measures. The company has a medium-term objective to define non-financial performance indicators and to incorporate these indicators in the value-based management of the company.

In managing the company, senior management considers it imperative that each individual Schaeffler Group employee act strictly within the relevant legal limits and comply with corporate governance standards.

More on corporate governance on pp. 84 et seq.

Presentation of strategic financial and key operating financial performance indicators in the group management report No. 025

	2017	2016	Course of business	Earnings	Performance indicators	Financial position and finance management	Overall assessment	Report on expected developments
ROCE (before special items, in %)	19.9	22.3	x		x		x	
SVA (before special items, in € millions)	787	939	x		x		x	
Revenue growth (at constant currency, in %)	5.9	3.4	x	x	x		x	x
EBIT margin (before special items, in %)	11.3	12.7	x	x	x		x	x
Free cash flow (in € millions)	488	735	x			x	x	x

Remuneration model

A company's success depends to a considerable extent on the performance of its employees. In order to appropriately acknowledge this performanceand to offer a motivating incentive, and to offer a motivating incentive, the company has developed a comprehensive remuneration system.

The Schaeffler Group aims to consistently align its brand identity, management model, and the four corporate values with one another and to focus the entire organization on common goals. A consistent performance-based remuneration system is key to achieving this aim. Harmonizing the indicators used to determine variable remuneration is one of the key objectives designed to standardize the Schaeffler Group remuneration models.

As a first step, the remuneration system for the Board of Managing Directors was adjusted and consistently oriented toward the Schaeffler Value Added/increasing shareholder value and free cash flow targets when Schaeffler AG's common non-voting shares were listed in October 2015. In a subsequent step, the company adjusted the remuneration system for its top executives in 2016, applying the same considerations underlying the remuneration system for the Board of Managing Directors. A significant change introduced in this amendment was the harmonization of the variable short-term component, the short-term bonus, and the introduction of a long-term variable component, the long-term bonus. The short-term bonus references a one-year period while the long-term bonus, with the share price trend acting as one of its key performance criteria, covers a four-year period.

More in the remuneration report on pp. 101 et seq.

The targets largely represent the strategic and key operating financial performance indicators, with the latter in turn representing the key performance indicators reflected in the annual outlook. As a result, operating targets are designed to be congruent with the measures comprising the outlook. Shareholders' interests are reflected in the remuneration system by taking into account Schaeffler Value Added (performance criterion for variable short-term remuneration) and the increase in the share price (key component of variable long-term remuneration).

In 2017, the company then aligned the performance indicators relevant to variable remuneration across all remuneration models, both at the management level and for all levels of staff below management, e.g. for the profit sharing arrangement in Germany.

The realignment is designed to create a modern, attractive and motivating remuneration system that is consistent with the values of a global family business and whose key performance measures reflect both the current year's performance and the long-term and sustainable value added.

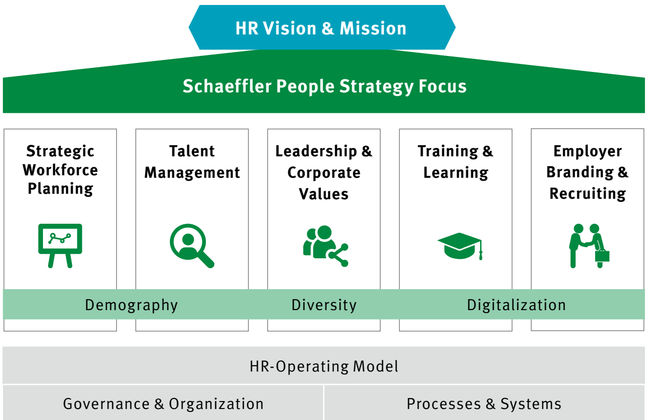
1.4 Employees

Its employees represent one of the key pillars of the Schaeffler Group's success. Their technical knowledge, skills, commitment, and passion for innovation secure the continuous progress of the company and are essential to the Schaeffler Group's current and future success. The objective of the company's human resources activities is to identify, support, and retain the best employees for the long term as an attractive employer in order to safeguard Schaeffler's competitive position.

HR strategy

The Schaeffler Group's strategic human resources activities are based on the HR strategy, which was redefined in 2016, and the related Roadmap 2020 with a set of initiatives for Human Resources (HR) that are designed to work in concert.

HR strategy house No. 026



The strategic direction of HR is summarized in the HR strategy house. Its starting point are the HR vision and mission creating a uniform global identity for the HR function. The HR strategy house is built on five pillars illustrating the fields of action prioritized by HR vis-à-vis employees.

- Strategic workforce planning
- Talent management
- Leadership & corporate values
- Training & learning
- Employer branding & recruiting

The company has created initiatives and projects for each of these pillars and is consistently working on them and driving them forward. They reflect the demands of demographics, diversity, and digitalization by assessing and appropriately taking into account their current and future impact. Underlying Schaeffler's human resources activities is an HR operating model including strong HR governance and a strong HR organizational structure, as well as a solid and efficient process and systems landscape.

Strategic workforce planning

Strategic workforce planning integrates the Schaeffler Group's strategic human resources activities into its Strategy and Technology Dialog.

It provides a basis for determining quantitative and qualitative staffing requirements for the medium to long-term planning period. Being able to quickly and efficiently determine long-term global staffing requirements is essential for responding to significant changes, for instance in the future growth areas of E-Mobility, Digitalization, and increasing globalization.

The results of strategic human resource planning serve as a basis for deciding what actions are required, such as internal and external recruiting, qualification programs, or in- or outsourcing strategies. These actions enable the Schaeffler Group to identify and actively mitigate the risk of excess personnel or a shortage of staff. In late 2017, the company initiated a project to investigate the need for future technical and commercial vocational training and engineering degree programs at universities offering cooperative education in Germany. The results will be available in early 2018 and will be used as input to the Strategy Dialog.

Talent management

Talent management supports management in identifying talents and promotes the development of all employees based on a uniform standardized approach worldwide.

One of the key responsibilities of talent management is the personal development of each and every employee within the company. To the Schaeffler Group, talent management is an integrated approach to providing employees with opportunities for development, identifying high-potential staff, and protecting key positions using focused succession management.

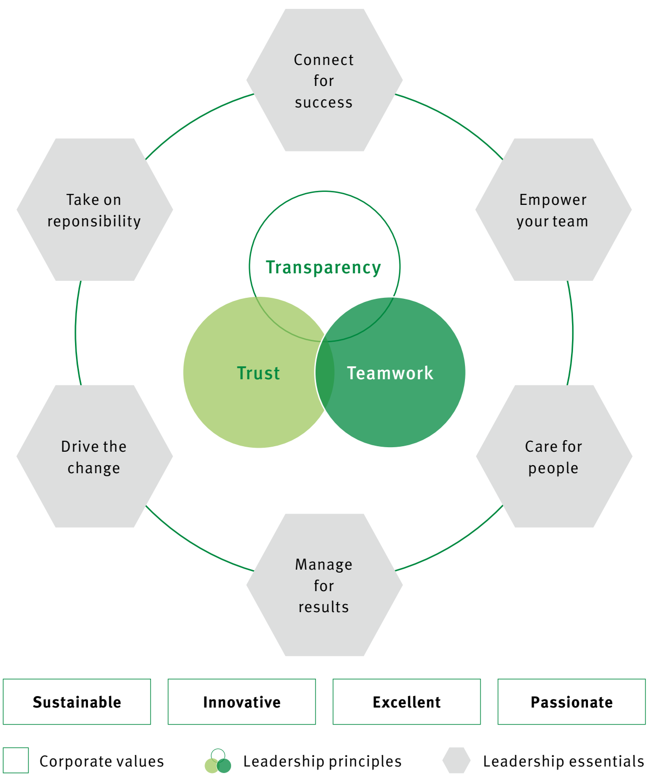
The worldwide standardization of the talent management process as part of the Global Talent Management HR initiative divided the process into two integrated phases: the Employee Development Dialog (EDD) and the Global Talent Review (GTR). Actions decided upon in EDDs and GTRs are realized throughout the year. The software developed specifically for this purpose and the related processes have been rolled out successfully in most countries, covering approx. 86% of relevant employees worldwide. Starting in 2018, the "Global Talent Management 2.0" project will work on an even more effective and efficient process and IT system in order to considerably increase its utility to everyone involved – employees, management, and Schaeffler as a company.

Leadership & corporate values

The Leadership & Corporate Values initiative that is part of the "Agenda 4 plus One" addresses the question of what leadership should look like within the Schaeffler Group in the future and defines leadership essentials applicable around the world that reflect the four corporate values.

The first phase of this initiative, which started in 2017, was an extensive analysis surveying a total of approx. 400 employees. All Executive Board members were interviewed, and workshops with participants representing various hierarchical levels and responsibilities were held in each of the four regions. An online survey was part of the process as well. The analysis was centered around the issues of how leadership is currently perceived within the company and what Schaeffler requires in terms of leadership in the future. Following the data collection phase, the results of the analysis were further consolidated using a variety of focus

Leadership essentials No. 027



groups. Participants of the Schaeffler Top Management Meeting dealt extensively with an initial draft of the new leadership essentials in workshops of various formats. After further reviews, the six leadership essentials, along with descriptions of five leadership behaviors for each, were issued in their final form in early October 2017. Starting now, these leadership essentials represent the framework – applicable around the world – preparing the Schaeffler Group's management for future developments.

- Connect for success
- Empower your team
- Care for people
- Manage for results
- Drive the change
- Take on responsibility

Together with the four corporate values and the leadership principles, the leadership essentials create a uniform understanding. The corporate values describe the Schaeffler Group's identity and provide orientation to all employees. The leadership principles and leadership essentials illustrate the benchmark in terms of leadership and how managers are expected to lead their staff.

Training & learning

All training and continuing education courses worldwide are consolidated under the umbrella of the Schaeffler Academy.

The Qualification for Tomorrow initiative, part of the "Agenda 4 plus One", addresses the challenges of the future, such as an increasingly complex workplace, shorter and shorter development cycles, and a steady rise in information. As global networks and a digital work environment are becoming more and more essential for meeting today's needs, lifelong learning anywhere anytime is a success factor for being able to compete worldwide. As a result, this initiative focuses on the most important core issues and the company's future strategy related to the issue of learning.

The introduction of a new learning management system in 2017 is an important initial milestone in a modern world of learning. The cloud-based system is easy to use and is gradually being rolled out worldwide. Staff in Germany, France, and China are already enjoying its benefits.

The Schaeffler Academy supports the company's strategy by providing tailored qualification programs. Trends like digitalization and Industry 4.0 are transforming products and organizational processes as well as employee qualification requirements. In response, the Schaeffler Academy is adding issues such as design thinking, data analytics, and scrum to its training program, supplementing them with modular programs geared toward the relevant target groups.

Redesigning training content and methods creates a modern training program preparing trainees well for changing job profiles. A new comprehensive qualification program was created and launched in 2017. It prepares instructors for future challenges and provides them with input on issues like digitalization, generation Y and Z, new media, through to migration and diversity.

Employer branding & recruiting

HR's employer branding & recruiting activities strengthen Schaeffler's perception as an attractive employer and the position of the employer brand "Schaeffler" with the aim of contacting the best talents worldwide and recruiting them for the company.

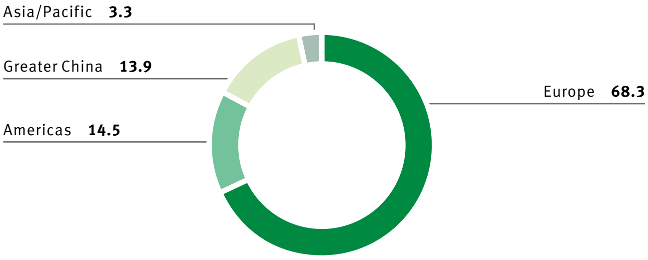
The human resources strategy is driven by the key commitment to making employment with the Schaeffler Group fit for the future – for external candidates as much as for employees who have been with the company for many years. Effectively positioning the company as an attractive employer worldwide is fundamental to continuing to successfully compete for the brightest talents in the future. The Schaeffler Group ranked highly in recognized employer rankings in 2017. Research institution "trendence" listed the company as one of the ten most popular employers among young professionals in the automotive sector and among the 30 employers most attractive to engineering students in Germany in 2017. The group was also successful internationally. In China, the Schaeffler Group was named "Top Employer China 2017" by the Top Employers Institute and received the "Best Employer of the Year" award for the Suzhou district from career platform Zhaopin.com.

In order to attract qualified students and graduates, the company focused on cooperative and sustainable partnerships with universities, student unions, student associations, and organizations such as Formula Student Germany in 2017 as well. As part of its university marketing activities, Schaeffler held more than 30 events in Germany alone during the year. Additionally, Schaeffler's technical departments helped run realistic case studies at universities and assisted students in various practical projects.

More on cooperation with universities on page 13

Schaeffler Group employees by region No. 028

in percent, as at December 31, 2017



In 2017, Schaeffler took the important step of establishing global employer branding and recruiting functions aimed at creating global standards and utilizing synergies more effectively. This year, recruiting activities were especially affected by an increasing need for staff and changing job specifications, since the implementation of the strategy "Mobility for tomorrow" requires new job descriptions and new qualifications on the part of candidates.

In addition, the market for internal candidates remains a key source for filling open positions. In Germany, more than 40% of vacancies were successfully filled with internal talents in 2017.

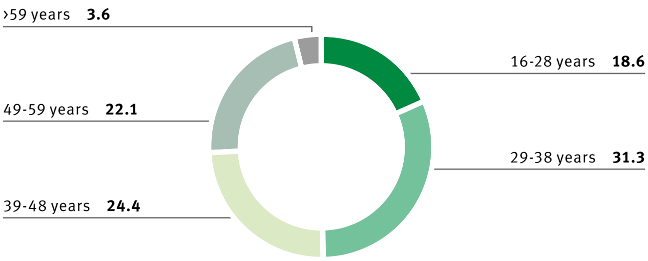
Employee structure and development

The Schaeffler Group employed an average of 88,697 employees (prior year: 85,733) in 2017. The number of employees at December 31, 2017, was 90,151 (prior year: 86,662), 4.0% above the prior year level.

The company recruited new personnel compared to December 31, 2016, primarily in production and production-related areas – mainly in the Greater China and Europe regions, especially in Eastern Europe.

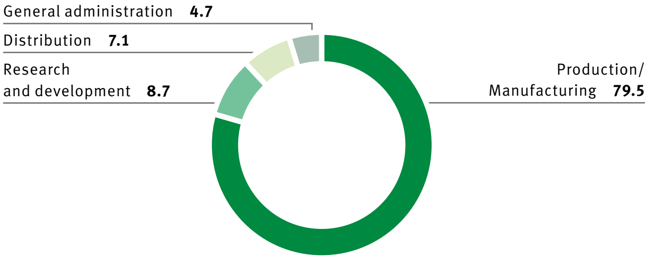
Schaeffler Group employees by age group No. 029

in percent, as at December 31, 2017



Schaeffler Group employees by function No. 030

in percent, as at December 31, 2017



Workforce structure

The average period employees have been with the Schaeffler Group (tenure) amounted to 11.0 years in 2017 (prior year: 11.2). The average age of the Schaeffler Group's workforce was 39.7 years (prior year: 39.8).

For the Schaeffler Group, diversity is closely related to the company's success, since international teams heterogeneous in terms of age and gender are particularly successful. The proportion of female staff among the Schaeffler Group's employees increased to 21.7% (prior year: 21.4%) in 2017, and the proportion of female managers was 12.4% (prior year: 11.8%).

The company signed the "Charta der Vielfalt" (diversity charter) as early as in 2008, committing to implementing the Charta's guidelines internally by taking measures to promote diversity within the company. Diversity will contribute significantly to the company's success by further increasing the company's innovative ability. In order to seize the latest trends and developments quickly and effectively, the Schaeffler Group regularly exchanges information with various external catalysts of innovation.

More on diversity on page 43

Workforce – structural data No. 031

	12/31/2017	12/31/2016	Change	in %
Average age (years)	39.7	39.8	-0.3	%
Average tenure (years)	11.0	11.2	-1.8	%
Labor turnover rate (%) 1)	3.9	3.6	0.3	%-pts.
Proportion of female employees (%)	21.7	21.4	0.3	%-pts.
Proportion of female managers (%) 2)	12.4	11.8	0.6	%-pts.

1) Initiated by employee.
2) Managers are defined as employees in a supervisory function.

Number of employees No. 032

	2013	%	2014	%	2015	%	2016	%	2017	%
Europe [1)]	55,392	70.8	57,607	70.0	58,600	69.6	60,127	69.4	61,554	68.3
Americas	12,146	15.5	12,229	14.9	12,625	15.0	12,480	14.4	13,056	14.5
Greater China	8,068	10.3	9,741	11.8	10,216	12.1	11,255	13.0	12,537	13.9
Asia/Pacific	2,652	3.4	2,717	3.3	2,757	3.3	2,800	3.2	3,004	3.3
Schaeffler Group	**78,258**	**100**	**82,294**	**100**	**84,198**	**100**	**86,662**	**100**	**90,151**	100

Figures as at December 31.
[1)] Incl. employees of the corporate head office.

Personnel development

As strategic human resource planning has to take into account new requirements and skills early on, supporting employees and helping them gain additional qualifications is key to the Schaeffler Group.

3,514 classroom training sessions (prior year: 4,054) with an enrollment of 30,646 (prior year: 37,345) were held in Germany in 2017.

Employee qualification and continuing education No. 033

Number in Germany	2017	2016	Change in %
Classroom training sessions	3,514	4,054	-13.3
• Enrollments – classroom training sessions	30,646	37,345	-17.9
E-learning courses	97	90	7.8
• Enrollments – e-learning courses	15,593	25,074	-37.8

In addition, 97 different e-learning courses were offered to staff and were taken by 15,593 employees. The prior year included mandatory courses for employees on new, specific issues (prior year: 90 e-learning courses offered; 25,074 enrolled). With the expansion of its online training program, the Schaeffler Group follows the trend toward making continuing education courses available to employees anytime, anywhere.

Of particular note are the national and international management and leadership programs. The programs provide training in specific intercultural management skills as well as company-specific information on strategy development, making them pivotal in achieving medium- and long-term business objectives.

In 2017, the company designed the “In The Lead@Europe” series of training events which ensures uniform leadership training events are held in each country in the Europe region. The leadership essentials defined as part of the “Leadership & corporate values” initiative form the basis for the content of the training, which is taught using modern and interactive learning methods. Three new regional development programs are geared to high-potential managers. The Accelerators Program (ACE) and the Management Talent Program (MTP) were implemented in the Asia/Pacific region. The Leadership Operations Program for candidates with potential in Operations, originally only available in Germany, has now been rolled out to the Europe region.

Specialist and project career path

As a company with operations worldwide, the Schaeffler Group not only requires line managers, but it also needs especially highly motivated and qualified specialists as well as project managers who combine extensive technical expertise and key know-how with outstanding project management skills.

The specialist and project career path with its global standards, career stages, and requirements offers specialists and project managers within the Schaeffler Group a framework for following their strengths and interests in developing and establishing themselves in a career path.

Supporting new talents

Attracting and training new talents in all areas is essential to ensuring the company's long-term success. 3,185 trainees (or 3.5% of the Schaeffler Group's workforce) were pursuing an apprenticeship at the Schaeffler Group (prior year: 2,982 or 3.4% of the workforce) as at the end of 2017. These future specialists are trained in a total of 20 specific jobs requiring formal training at various Schaeffler Group locations. In addition to technical qualifications and Schaeffler-specific know-how, the Schaeffler Group's training particularly values methodological, social, and personal skills. Training at Schaeffler is aimed at teaching young employees to think and act independently, promoting their creativity, and strengthening their environmental awareness and sense of responsibility.

Cooperative education programs ("Duales Studium") play another important role in attracting new talents in Germany. The Schaeffler Group offers various types of these programs of academic studies, such as a "Duales Studium" in cooperation with colleges offering this type of cooperative education program (Duale Hochschulen) or a "Two-in-One" program in cooperation with universities of applied sciences in Germany. A total of 173 students were enrolled in the "Duales Studium" and 163 in "Two-in-One" bachelor programs in 2017. The company also offers a graduate degree in the form of a master's degree program with currently 22 students.

In addition, the Schaeffler Group offers special trainee programs to university graduates that have demonstrated above-average performance and commitment, enabling them to gain a comprehensive overview of the group and its functional areas over a period of 12 to 24 months. The accompanying qualification measures aimed at personal development ideally prepare these trainees to take on positions carrying responsibility within the Schaeffler Group. In Germany, for instance, 49 young talents (prior year: 40) were enrolled in this trainee program as at December 31, 2017. Similar programs operate in other countries around the world, including in the U.S.

Health management and occupational safety

The demographic trend is profoundly changing the structure of the group's workforce. The future success of the company depends on the employees' qualification and motivation and on the long-term maintenance of their health. The Schaeffler Group's workplace health management program is based on the principles of the Luxembourg Declaration and represents a key element of the HR initiatives.

The design of the workplace health management program focuses on measures to maintain the mental and physical health of the company's employees as well as their capacity to work and their performance capabilities. Priorities are measures regarding the musculoskeletal system and providing individual skills for coping with stress. Ergonomic measures and reducing the negative impact of shift work also contribute to prevention.

The company consolidates measures promoting the health of individual employees in the "pit stop" ("Boxenstopp") program by specific target groups. In addition to this program, the company offers a multitude of measures for target groups with comparable tasks and similar health risks. Measures offered are based on an analysis of the requirements at each location, guaranteeing that they are tailored.

The workplace health management program is part of Schaeffler's EnEHS management system (Energy Environment Health and Safety), which ensures that working conditions are continually reviewed and occupational safety requirements complied with. Certification takes place worldwide in accordance with the European EMAS ("Eco-Management and Audit Scheme") Directive. The company regularly holds information days, training sessions and continuing education seminars on occupational safety. These types of preventative and awareness measures helped reduce the accident rate from 8.4 to 7.1 AccR (AccR = lost time incidents per 1 million labor hours) during the reporting period.

1.5 Sustainability

To the Schaeffler Group, sustainability means enabling a future worth living by fostering the growth of the Schaeffler Group with a long-term view and continuity for the benefit of all stakeholders. "Sustainable" is one of the Schaeffler Group's four key corporate values. The company accepts its corporate responsibility to operate its business as ecologically and socially responsibly as possible – even above and beyond legal requirements. As such, the Schaeffler Group has defined a framework in the form of its sustainability strategy "Responsibility for tomorrow 2030+".

Sustainability strategy and management

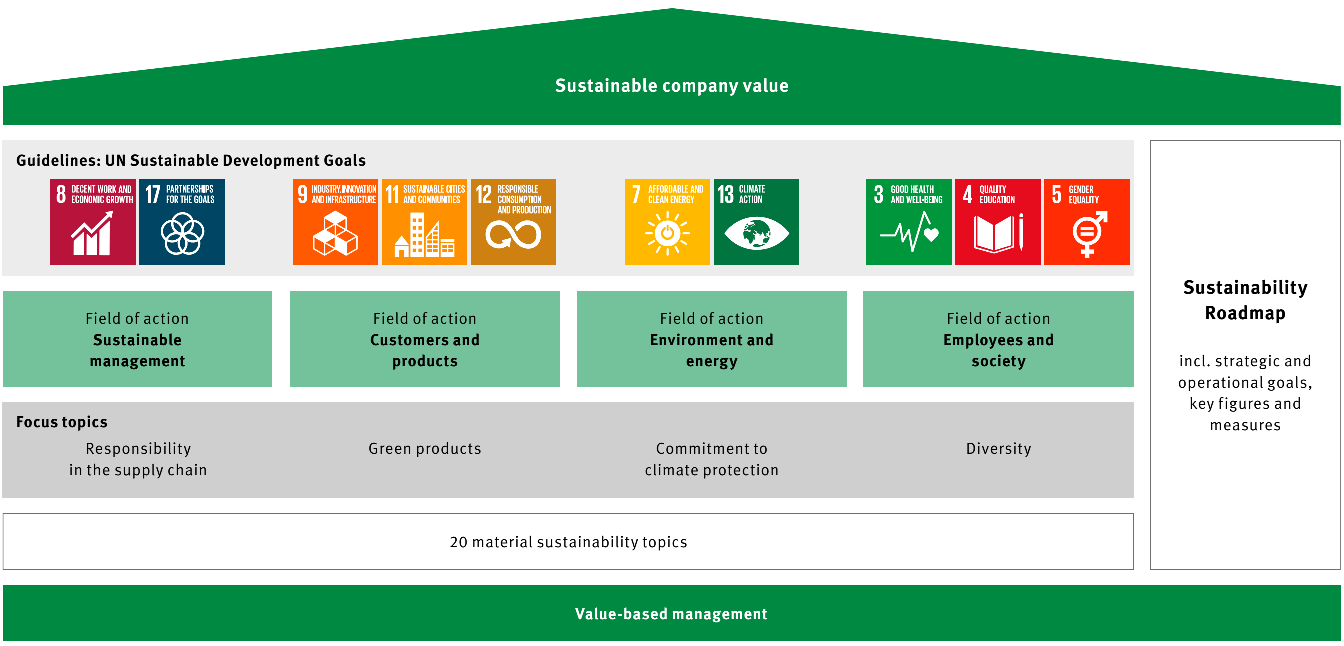
The sustainability strategy "Responsibility for tomorrow 2030+" is based on the Schaeffler Group's vision and mission and supports the objective of adding long-term shareholder value. The company used the United Nations' 17 "Sustainable Development Goals" (SDGs) to guide its sustainability focus.

The member states of the United Nations (UN) issued the Agenda 2030 for sustainable development in order to successfully address the global challenges. The Agenda 2030 is aimed at facilitating worldwide economic progress and prosperity while achieving social justice and respecting the ecological limits of global growth. The Agenda applies equally to all countries in the world: All developing countries, emerging countries, and industrialized nations have to contribute.

At the core of the Agenda are the 17 Sustainable Development Goals that officially came into effect in January 2016. For the first time, they reflect all three dimensions of sustainability: social issues, the environment, and the economy. The goals include reducing poverty and hunger, promoting good health and education, facilitating gender equality, protecting the environment and the climate, and making consumption more responsible. Meeting the ambitious SDGs requires everyone to cooperate: politicians, civil society, and the private sector. This puts the onus on companies, as well, to make concrete contributions with a view to their business activities. The Schaeffler Group lives up to this obligation and its responsible corporate behavior contributes to ten of the 17 United Nations SDGs:

- 3 Good health and well-being (SDG 3)
- 4 Quality education (SDG 4)
- 5 Gender equality (SDG 5)
- 7 Affordable and clean energy (SDG 7)
- 8 Decent work and economic growth (SDG 8)
- 9 Industry, innovation, and infrastructure (SDG 9)
- 11 Sustainable cities and communities (SDG 11)
- 12 Responsible consumption and production (SDG 12)
- 13 Climate action (SDG 13)
- 17 Partnerships for the goals (SDG 17)

Sustainability strategy "Responsibility for tomorrow 2030+" No. 034



The activities aimed at meeting the SDGs are grouped in the four fields of action set out in the “Responsibility for tomorrow 2030+” sustainability strategy:

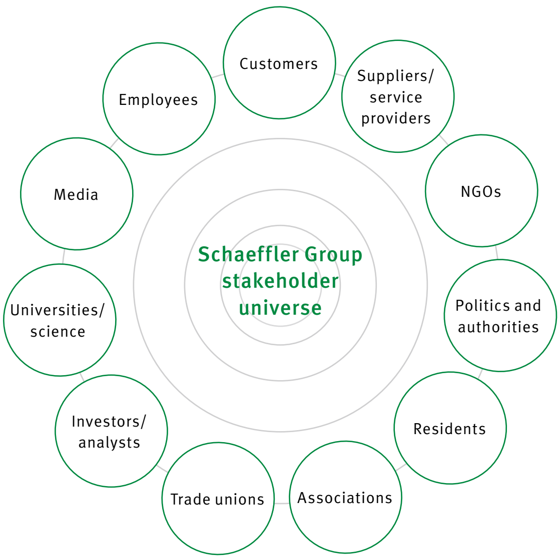
1. Field of action: “Sustainable management” (SDGs 8/17)
2. Field of action: “Customers and products” (SDGs 9/11/12)
3. Field of action: “Environment and energy” (SDGs 7/13)
4. Field of action: “Employees and society” (SDGs 3/4/5)

The focus here is on the topics of “responsibility in the supply chain”, “green products”, “commitment to climate protection”, and “diversity”.

A “Sustainability Roadmap” sets out specific objectives and measures that are relevant to the four fields of action and that are used in the operating and strategic measurement and management of Schaeffler’s sustainability performance. The Sustainability Roadmap represents the medium-term, dynamic element of the sustainability strategy.

As understanding the internal and external interests and expectations vis-à-vis the company and taking them into account in order to add long-term value is essential to the success of the sustainability strategy “Responsibility for tomorrow 2030+”, the Schaeffler Group regularly and openly exchanges information with its key stakeholders. Additionally, the Schaeffler Group regularly completes a significance process in order to detect key sustainability issues early on.

Schaeffler Group stakeholders No. 035



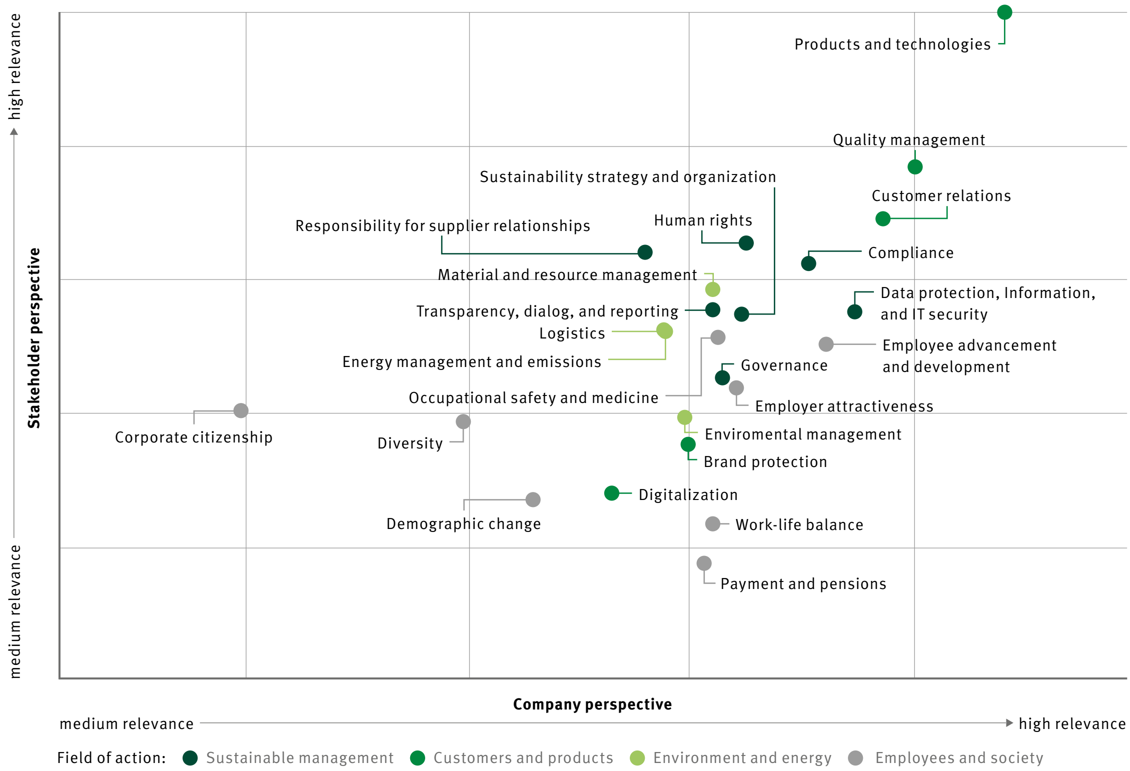
The significance analysis performed in 2016 by the Schaeffler Group was developed in cooperation with selected stakeholders: The company invited all employees as well as selected customers and suppliers from around the world to participate in an online survey assessing the relevance of certain issues to Schaeffler as a responsible company and to formulate sustainability-related expectations of the company. A total of 1,250 employees and 431 customers and suppliers participated in the survey. The relevant issues were initially identified by means of a comprehensive document analysis, and participants were given the opportunity to add to them.

The result of the significance analysis consisted of 24 topics that were assigned to the four fields of action “Sustainable management”, “Customers and products”, “Environment and energy” and “Employees and society”. The topics identified in the significance analysis were verified by the Schaeffler Group’s sustainability organization in the context of the company’s operations and used to create a materiality matrix. The group’s Sustainability Roadmap lists concrete objectives and measures for each issue set out in the matrix. The materiality matrix illustrates the relevance of the various issues to the company and its stakeholders and serves as the basis for reporting on sustainability.

The sustainability organization then held an internal workshop to discuss the opportunities, risks, and relevance to the Schaeffler Group of the 24 topics defined, starting with the results of the significance analysis, and to consider the internal perspective regarding their relevance to and the impact of the company’s operations. The results of this workshop were then used to select the 12 non-financial topics to be included in the non-financial statement for 2017. In accordance with section 315b (3) HGB, Schaeffler AG has prepared a separate group combined non-financial report that is not part of the group management report and that combines the non-financial report of the parent company with that of the group in accordance with section 289b (3), section 315b (3), and section 298 (2) HGB. The combined separate non-financial report is publicly available from the company’s website.

Combined separate non-financial report in accordance with section 289b (3), section 315b (3), and section 298 (2) HGB at: www.schaeffler.com/sustainability/nfr2017

Materiality matrix – 24 topics No. 036



The Schaeffler Group also reports on significant sustainability topics in a voluntary annual sustainability report covering additional non-financial concepts, goals, and measures. The company issued an initial separate sustainability report, entitled "Responsibility for tomorrow", in 2017, laying the foundation for future sustainability reports. The sustainability report was prepared in accordance with the fourth generation (G4) of the Guidelines of the Global Reporting Initiative (GRI), the guidelines most frequently used to prepare sustainability reports worldwide. The next sustainability report will be issued in April 2018.

When evaluating its sustainability performance, the company refers to external sustainability ratings and rankings. In 2016, the sustainability rating platform EcoVadis awarded the "Silver Recognition Level" to the Schaeffler Group in recognition of the company's sustainability performance. The assessment covered the four categories "environment", "working conditions", "responsible management", and "sustainable procurement".

The Schaeffler Group's corporate responsibility is managed and exercised by a sustainability organization that is integrated throughout the group's divisions, functions, and regions. The sustainability steering committee, the Schaeffler Group's panel of experts representing the technical departments, develops strategic sustainability targets and designs non-financial reports. It receives support from the sustainability working group, which is responsible for operational implementation. In addition, a sustainability center of expertise generates ideas for the divisions, functions, and regions and as a communicator and dialog partner for stakeholders. The sustainability organization reports directly to Schaeffler AG's Chief Executive Officer.

1. Field of action: "Sustainable management"

8 17

The Schaeffler Group's strategy is based on the group's commitment to drawing on its strength as an automotive and industrial supplier and partnering with its customers to shape the mobility of the future. To put this commitment into concrete terms, it has developed the following vision: "As a leader in technology, we combine a passion for innovation with the highest standards of quality to shape the future of mobility – for a world that will be cleaner, safer, and smarter."

In following this vision, the Schaeffler Group's actions are guided by the core values of a global family business: Schaeffler's actions are sustainable, innovative, excellent, and passionate. This applies to its own operations as well as to its global supply chain. Fairness, mutual respect, and integrity are the cornerstones upon which the Schaeffler Group's actions are based. The Schaeffler Code of Conduct sets out the principles and practices that all Schaeffler employees, managers, and the Executive Board must follow, and the Schaeffler Group expects the same of its business partners.

To the Schaeffler Group, responsibly managing its own supply chain also means raising service providers' and suppliers' awareness of the group's requirements and expectations. This applies to high-quality and efficient cooperation as well as to compliance with obligations and norms regarding environmental and social issues. National legislators' requirements regarding responsible procurement are high. For instance, the British Modern Slavery Act requires companies to disclose steps they have taken to prevent modern slave labor in their supply chain. In response, responsibility in the supply chain was identified as a focus topic within the sustainability strategy "Responsibility for tomorrow 2030+". It represents the Schaeffler Group's objective of cooperating with its suppliers to make its own supply chain more and more sustainable.

Establishing sustainability in procurement requires the Schaeffler Group's partners to adhere to the group's commitments. The Schaeffler Group's Supplier Code of Conduct plays a key role in this. It sets out minimum requirements for suppliers regarding, for instance, respect for human rights, handling information subject to data protection legislation, and conduct regarding the environment, health, and safety. The Schaeffler Group's Supplier Code of Conduct (SCoC) is based on the principles of the United Nations Global Compact (UNGC) and the core conventions of the International Labour Organization (ILO). Any violation of principles, guidelines, or requirements set out in the SCoC is considered a fundamental breach of contract by the supplier causing such violation and results in an escalation process that may result in the termination of the supplier relationship. Acknowledging the SCoC is an integral part of contracts governing new supplier relationships.

The Schaeffler Group reviews potential suppliers with respect to their compliance with environmental and social standards before integrating them into its supplier portfolio. If the initial assessment (formerly known as assessment of potential) of possible new business partners with respect to energy, environment, health, and safety (EnEHS) issues indicates that they do not meet the required minimum standards, they are eliminated from the selection process during supplier development. If violations are serious, existing business relationships are terminated as well.

The company's comprehensive material compliance management system is designed to ensure that any components and raw materials used comply with the applicable legislation, regulations, and standards. The Schaeffler Group's compliance management system helps the company and its employees comply with all relevant local, national, and international laws and regulations.

More on the governance structure on pp. 97 et seq.

2. Field of action: "Customers and products"

The Schaeffler Group aims to help customers meet the challenges resulting from global trends such as urbanization, digitalization, shortage of resources, and climate change, such as reducing CO_2 emissions with innovative products and system solutions. In 2017, the company defined the focus topic "Green products" for the "Customers and products" field of action. This includes developing and manufacturing products contributing significantly and measurably to making urban and interurban mobility, eco-friendly drives, and the energy chain environmentally sound.

One example in the field of eco-friendly drives is the "Gasoline Technology Car II" (GTC II) concept car, which demonstrates the potential of intelligent state-of-the-art 48-volt hybridization. The GTC II facilitates additional fuel savings of 13% in the NEDC (New European Driving Cycle) compared to the GTC I presented at the Vienna Motor Symposium in 2014.

Sustainable "Mobility for tomorrow" requires considering the entire energy chain. In the energy chain field, the Schaeffler Group develops solutions for generating, storing as needed, converting, and utilizing energy. The Schaeffler Group develops high-performance components for wind and hydro-power plants and supports operators with services such as sensor-based remote diagnostics. In addition, the company is researching coatings to increase the efficiency of hydrogen and fuel cells. In the field of energy utilization, the Schaeffler Group is working on improving existing technologies and further electrifying the drive train.

As a result of increasingly complex products and supply chains, ensuring product safety is proving challenging for many manufacturing companies. In the interest of product safety, the Schaeffler Group's customers place high demands on brand protection. In 2017, the Schaeffler Group gave end customers, distributors, and authorities the OriginCheck app, a tool to quickly and easily carry out an initial check on products purchased. If this check leads the user to suspect that a product may be counterfeit, he or she can use the app to take direct further steps to obtain proper clarification. These checks are based on GS1-standard data matrix codes (DMC) that are placed on Schaeffler packaging. These two-dimensional codes contain various types of information in an encrypted form and identify the product worldwide with no conflicts.

3. Field of action: “Environment and energy”

The Schaeffler Group's sustainability strategy documents the company's high standard when it comes to environmental protection and reducing greenhouse gas emissions. In 2017, the company defined the focus topic “Commitment to climate protection” for the “Environment and energy” field of action. The targets are clearly defined: Increasing energy efficiency by 40% by 2020 (base year 2011) and carbon neutrality for one location in each region in the medium-term. The Schaeffler Group is implementing a stringent energy policy and related measures in order to meet these targets.

The Schaeffler Group's energy policy commits both the Board of Managing Directors and the company's employees to energy efficiency and to saving resources, acting sustainably, and continually improving energy management. The Schaeffler Group measures and monitors its progress with respect to energy management using its energy data management system (EDMS).

In 2017, a pilot project aimed at further digitalizing energy management and maintenance was initiated at Schaeffler's Berndorf location in Austria. In the first step of the project's development, data-based energy efficiency and maintenance as well as the appropriate supply of media to all machines and the production environment were combined in what is known as the Schaeffler Group's digital platform. The pilot project is designed to help develop new approaches to increasing the “Industry 4.0 capability” of machines, plants, and buildings and to solve new innovation-related issues early on.

To help the company effectively protect the environment, the Schaeffler Group has implemented environmental management systems in accordance with the European EMAS (“Eco-Management and Audit Scheme”) Directive and the ISO 14001 standard at all of its relevant locations. The Schaeffler Group's locations utilize an energy management system based on the ISO 50001 standard to make their operating processes more energy-efficient. The number of manufacturing locations certified under ISO 50001 worldwide increased from 57 to 61 in 2017. Nearly all manufacturing locations worldwide have been validated under EMAS and certified under ISO 14001 by independent assessors. The Schaeffler Group has demonstrated its first-rate environmental management by having nearly all of its manufacturing locations worldwide entered into the EMAS site register by the end of 2017.

In February 2017, Schaeffler officially commissioned a new water supply commences operation on the banks of the Main river in Schweinfurt that had been constructed over a period of several months. It is aimed at helping to make production at the Schaeffler Group's Schweinfurt location more economical while reducing the strain on the valuable groundwater supply and meeting environmental requirements imposed by the city of Schweinfurt and the Water and Shipping Authority.

The Schaeffler Group also strives to support its employees in making their mobility more sustainable. To this end, it is in the process of implementing a comprehensive conceptual mobility plan. As part of the plan, the infrastructure for charging electric vehicles at the company's German locations was doubled compared to the prior year. In addition, the Schaeffler Group has opened up its company car policy in Germany to plug-in hybrids and electric vehicles, allowing employees to order and use these vehicles as company vehicles.

4. Field of action: “Employees and society”

The responsibility for its employees and good corporate citizenship are deeply embedded in the Schaeffler Group's core. Based on the significance process, the “Employees and society” field of action focuses on the issues of diversity, being an attractive employer, work-life balance, health management, compensation and retirement benefits, supporting and developing employees, as well as good corporate citizenship.

Diversity is anchored in the HR strategy and, to Schaeffler, it means acknowledging, appreciating, and including diverse views, experiences, and technical expertise across all hierarchical and organizational units. The company signed the “Charta der Vielfalt” (diversity charter) as early as in 2008 and is committed to proactively promoting diversity within the company. In order to gradually embed this issue throughout the company, it has issued a conceptual diversity plan in 2017 that it plans to implement in the coming years. Demographics, promoting women, internationality, and people with disabilities are important issues to be dealt with here. During the year, a reverse mentoring program was launched in order to promote the sharing of experiences between young and old and an international network was founded. The objective of the latter is connecting employees around the world using the opportunities for interaction and teamwork provided by Schaeffler CONNECT, the company's new social intranet.

Globalization and digitalization make new demands on organizational and work processes. The Schaeffler Group responds to these trends with its New Work working methods initiative that forms part of its “Agenda 4 plus One”. Working method and space planning concepts that promote interaction are used to promote knowledge transfer and communication between employees and to support innovation processes. The comprehensive approach to finding the ideal combination of space planning, structuring work processes, and technology increases interdisciplinary collaboration. Advancing the existing company culture and providing flexible workspace layouts ensures that the “Mobility for tomorrow” strategy can be experienced in the working environment as well. The Schaeffler Group has initiated or completed four pilot projects at its Schweinfurt , Erlangen, and Nuremberg locations. These projects include providing multifunctional rooms, quiet areas, and „gravity points“, where employees can have flexible meetings and conversations in an appropriate and attractive atmosphere. A win–win situation for the company and its employees: The innovative use of existing resources in a manner that meets existing needs significantly increases employee satisfaction and Schaeffler's attractiveness as an employer.

The company has continued to systemize its workplace health management program during the year. Location-specific health management programs were established that have been adapted to the situation in the specific working environment. To help with this project, a standard analysis instrument for surveying employees was developed and used. In Schweinfurt, Wuppertal, and Herzogenaurach, the company initiated the "pit stop active back" ("Boxenstopp Rücken Aktiv") program involving exercises to counteract the specific strains and stresses of the production workplace. The training program "Fit4Shift" for shift workers was developed in Herzogenaurach, Eltmann, and Buehl in order to prevent health issues like insomnia and stress. The "Fit4Innovation" program was launched in Buehl and Herzogenaurach. It provides future project managers with information on avoiding stress and on resilience, and helps them form stabilizing networks among themselves. In order to be able to offer measures under the workplace health management program at the same level of quality all over Germany, the company began cooperating with a health insurer with operations throughout the country. This provides the company with access to an existing network of certified service providers, allowing it to flexibly plan and execute its health management program measures.

In its Factory for Tomorrow initiative, which is part of the "Agenda 4 plus One", the newly developed job register was rolled out at two locations as part of the company's efforts to design workspaces more ergonomically. The register uses a database solution to determine and visualize the ergonomic strain involved in the job. The Schaeffler Group uses the instrument in its inclusion efforts to compare the employee's skills to the requirements of the job, allowing the company to identify jobs for employees with impaired physical abilities that are appropriate for their performance capabilities and medical condition. At the same time, it also promotes the focused reduction of high-strain jobs.

Attractive remuneration and benefit programs are key elements of the HR strategy aimed at promoting employee satisfaction. In addition, fair, transparent, and performance-based remuneration and retirement benefit schemes that meet employees' needs are important characteristics of an attractive employer.

The Schaeffler Group's remuneration models were changed to reflect uniform, consistent performance indicators and adjusted for all levels of staff. As a result of these changes, the profit sharing arrangement in Germany is now based in equal parts on three indicators. Along with the existing quality indicator, in 2017, the company component, comprising Schaeffler Value Added and free cash flow, was adjusted and delivery performance of the German production locations was added as a new indicator.

By making this adjustment, the company is not only pursuing its objective of consistent and performance-based remuneration models, but also highlights the importance of the proven "Quality-Cost-Delivery performance" approach, which emphasizes a strong quality and cost mindset as well as delivery performance.

A further significant step toward becoming a more attractive employer was coming to an agreement that LuK GmbH und Co. KG will join the collective labor agreement of the metal and electric industry in Baden Wuerttemberg effective January 01, 2018. Collectively bargained working conditions and transparent remuneration rules now apply to blue- and white-collar workers alike.

To cover potential pension shortfalls, the company offers its employees attractive retirement benefit schemes financed by the employer and/or the employee. A dedicated retirement benefit portal provides employees in Germany with extensive information about various retirement benefit schemes and with the opportunity to obtain a calculation of the income they can expect to receive from the various retirement schemes.

The Schaeffler Group's ideas management system enables its employees to be actively involved in the company. By contributing their creativity and knowledge, employees are taking on responsibility and are continually improving processes and products. The Schaeffler Group's employees submitted a total of 33,988 ideas via the ideas management software in 2017, generating cost savings of approx. EUR 20.8 m. The group is currently using this system at 45 locations in 13 countries and is continually adding further locations. The ideas management system, an important management instrument, assists senior management with achieving objectives and helps secure the company's success for the long-term.

More on the HR strategy on pp. 33 et seq.

The Schaeffler Group focuses its corporate citizenship activities on three main areas: education and science, health and social affairs, and sports and cultural events. Its priority is on supporting organizations and projects near Schaeffler locations.

Schaeffler's strategic partnerships and collaborations in education and science demonstrate its commitment in this field. For instance, the company is the main partner of the "Young Car Mechanic" competition held for the first time in Poland in May 2017. Students from Poland, Lithuania, and Latvia competed against each other in a variety of virtual vehicle repair tasks using a specifically designed simulator. The competition is designed to get young people interested in being a professional mechanic.

Through its HOPE initiative (Health, Occupational skills, Preservation of culture & heritage, and Empowerment of society), the Schaeffler Group continually provides support in India via Schaeffler India Limited. Under the heading "May everyone be happy", the initiative helped expand a school in Vadodara, India, which will shortly provide 800 students with the opportunity to obtain an education, compared to less than 200 students previously.

In addition, the Schaeffler Group supports sports and cultural activities to help convey values and provide impetus for the positive development of society. In November 2017, female employees of Schaeffler's Barcelona location participated in the "Carrera de la Mujer", the largest women's sports event in Europe, in order to raise funds for initiatives against breast cancer and violence against women. Schaeffler also once more supported the "Lauf für Kaya!" ("Run for Kaya!"), which was held in conjunction with the 7^{th} Earth Day in Herzogenaurach to promote cultural exchange between Germany and Burkina Faso.

2. Report on the economic position

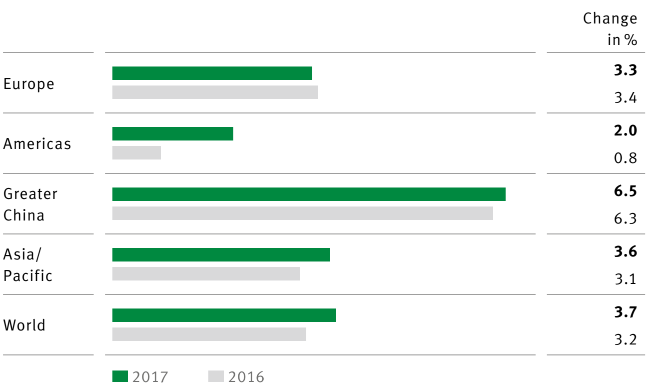
2.1 Economic environment

Macroeconomic environment

The **global economic** upturn that had emerged in the second half of 2016 continued in 2017. Global gross domestic product rose by 3.7% in 2017; this represents the strongest growth rate in six years (Oxford Economics, January 2018). The increasing momentum took hold of large parts of the industrialized economies as well as of the emerging and developing countries.

In the euro region, the continuing economic upturn was felt across countries and sectors. Growth in gross domestic product reached its highest level in a decade, driven by private consumption and investment as well as by strong foreign demand brought on by the worldwide economic recovery. The German economy expanded significantly, generating its highest growth rate since 2011. In the United Kingdom, however, the economy was much less dynamic. Continuing uncertainty regarding the upcoming withdrawal from the EU and the impact of the considerably weaker pound contributed to economic growth there falling behind that of the euro region. Following a weak first quarter of 2017, economic activity in the U.S. increased considerably during the remainder of the year. The Fed continued to gradually tighten its monetary policy and raised its benchmark interest rate three more times. The situation of the Japanese economy improved, with especially stronger foreign demand bolstering the higher-than-expected rise in gross domestic product.

Growth in gross domestic product No. 037



Source: Oxford Economics (January 2018).
Regions reflect the regional structure of the Schaeffler Group.

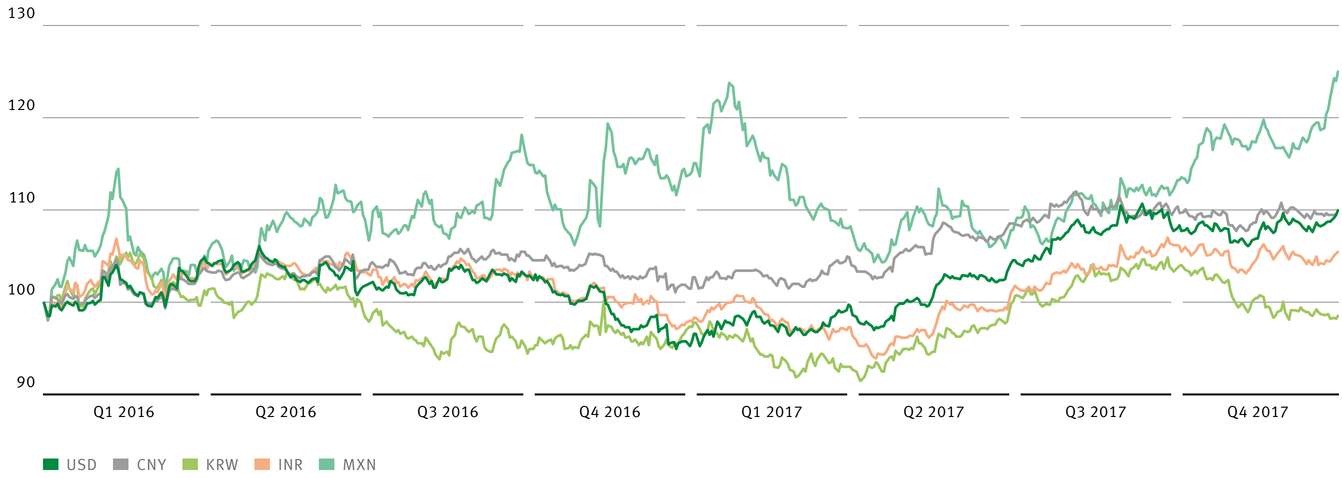
In China, growth temporarily increased slightly for the first time since 2010, primarily due to stronger demand for exports. In addition, private consumption continued to gain in significance compared to investment, as intended by the ongoing restructuring of the economy. Momentum in the Indian economy slowed temporarily due to non-recurring impacts. The economies in Brazil and in Russia, on the other hand, began to recover from their earlier deep recession.

In this context, the situation of the Schaeffler Group's regions during the year was as follows: Gross domestic product in the Europe region rose by 3.3%, and the economic output of the Americas region grew by 2.0%. The Greater China region reported a growth rate of 6.5%, while gross domestic product in the Asia/Pacific region increased by 3.6%.

The global **capital markets** reported some significant increases in the reporting year, with both the Dow Jones Industrial Average (DJIA) and the Deutsche Aktienindex (DAX) rising to new all-time highs in the fourth quarter of 2017.

Currency market trends No. 038

EUR against selected currencies in percent (12/31/2015 = 100)



Source: Bloomberg.

In the **currency markets,** the euro rose against all foreign currencies significant to the Schaeffler Group over the course of the year. However, comparing annual averages to prior year provides a mixed view. In terms of annual average exchange rates, the euro gained ground against the U.S. dollar, the Chinese renminbi, and the Mexican peso. However, the euro declined slightly against the South Korean won and the Indian rupee based on annual average rates.

More on foreign currency translation on pp. 127 et seq.

Sector-specific environment

Trends in automobile production and vehicle population significantly affect the results of operations of the Schaeffler Group's Automotive OEM and Automotive Aftermarket business. The global trend in industrial production provides an indication of the development of the Industrial division's business.

Automobile production

Global **automobile production,** measured as the number of passenger cars and light commercial vehicles produced, increased by 2.1% to approx. 95.1 million (IHS, February 2018). A strong first quarter of 2017 was followed by noticeably lower growth rates during the remainder of the year.

The Europe region reported significant growth in automobile production of 3.9%. While Turkey, France, and Russia generated above-average growth rates, especially Germany and Spain experienced declines. Growth in India, which is also part of the Europe region, remained relatively high despite momentum declining there. Automobile production in the Americas region was down 0.9% compared to prior year, since very significant increases in Brazil and Mexico did not fully offset the considerable contraction in Canada and particularly in the U.S. Greater China region growth in automobile production came in at 2.6%, significantly less than the high prior-year level. The main reason for the decreased momentum was a reduction in buying incentives provided by the government. Automobile production in the Asia/Pacific region rose by 2.1%, supported, in particular, by a very strong first half of the year in Japan, while South Korea experienced a slight decline.

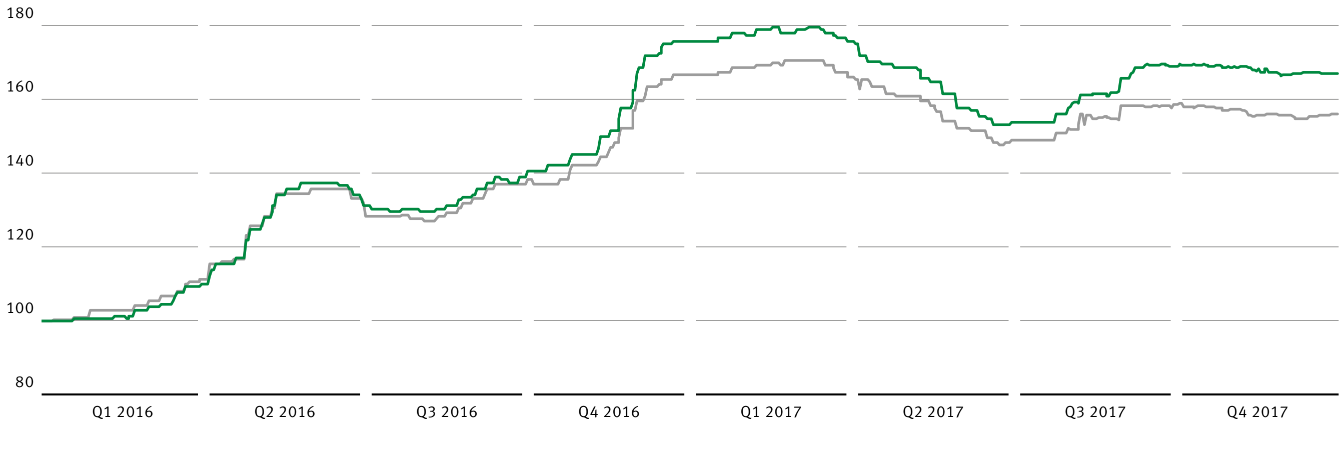
Automobile production No. 039

	Change in %	million units
Europe	**3.9**	**28.7**
	5.0	27.7
Americas	**-0.9**	**20.2**
	0.0	20.4
Greater China	**2.6**	**28.1**
	14.1	27.4
Asia/ Pacific	**2.1**	**18.0**
	-2.2	17.6
World	**2.1**	**95.1**
	4.8	93.1

2017 2016

Source: IHS (February 2018).
Regions reflect the regional structure of the Schaeffler Group.

Prices of selected steels No. 040
in percent (12/31/2015 = 100)



Source: Bloomberg, based on hot- and cold-rolled strip Northern Europe from Platts (EUR/metric ton).

Vehicle population and average vehicle age

The global **vehicle population,** measured as the number of passenger cars and light commercial vehicles, rose by 3.9% to approx. 1.3 billion in 2017 (IHS, February 2018), and the average **vehicle age**[1] increased slightly to 9.5 years.

In the Schaeffler Group's Europe region, the vehicle population expanded by 2.8% to just under 530 million; the mean vehicle age rose to 11.7 years. India experienced an above-average increase in vehicle population levels. The vehicle population in the Americas region increased by 2.1% to approx. 420 million, with growth in South America slightly exceeding that in the three NAFTA states. The average age of the vehicle population rose to 9.8 years. In the China region, the vehicle population grew by 12.3% to approx. 200 million; its average age rose to 5.2 years. The vehicle population in the Asia/Pacific region was up 2.5% at 175 million, mainly driven by growth in Southeast Asia. The average vehicle age increased to 8.4 years.

Industrial production

Global **industrial production,** measured as gross value added based on constant prices and exchange rates, grew by 3.6% (Oxford Economics, December 2017).

Industrial production in the Europe region rose by 2.2%, mainly driven by the encouraging trend in Germany, where growth was noticeably higher than in previous years, not least due to higher foreign demand. India, on the other hand, reported significantly less dynamic growth. In the Americas region, industrial production rose by 2.4%. Both the U.S. and Latin America (primarily Brazil) recovered from the weak prior year. In Mexico, however, production once again remained flat with the prior year. The

Vehicle population No. 041

		Change in %	million units
Europe	2017	**2.8**	**529.2**
	2016	2.9	514.8
Americas	2017	**2.1**	**421.7**
	2016	2.6	413.0
Greater China	2017	**12.3**	**200.2**
	2016	14.5	178.3
Asia/ Pacific	2017	**2.5**	**175.8**
	2016	2.4	171.5
World	2017	**3.9**	**1,326.9**
	2016	4.2	1,277.6

Source: IHS (February 2018).
Regions reflect the regional structure of the Schaeffler Group.

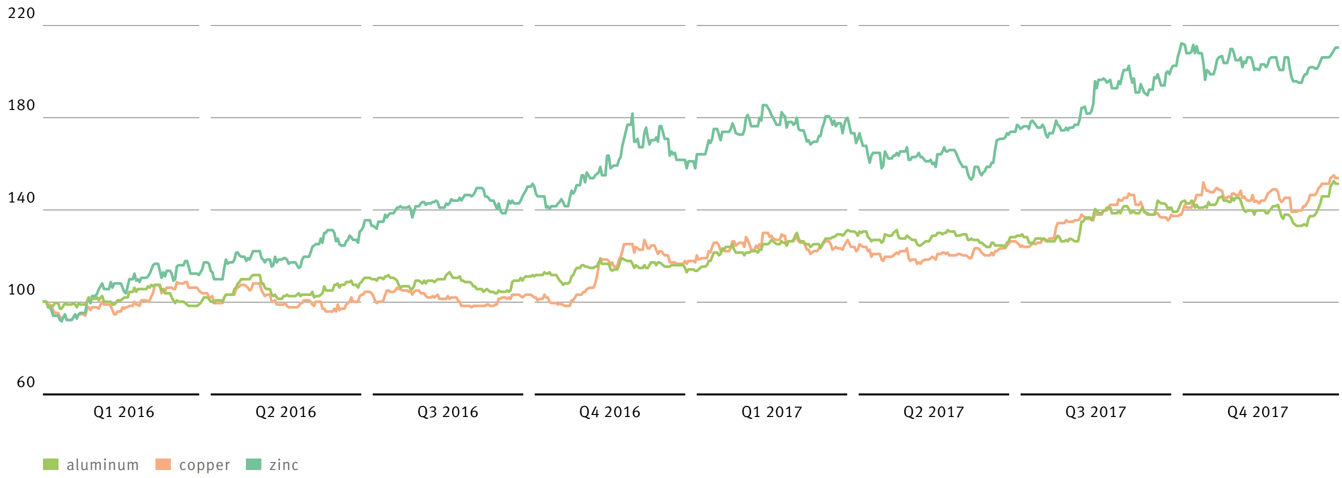
Industrial production No. 042

		Change in %
Europe	2017	**2.2**
	2016	2.7
Americas	2017	**2.4**
	2016	-1.6
Greater China	2017	**6.2**
	2016	5.6
Asia/ Pacific	2017	**3.9**
	2016	1.9
World	2017	**3.6**
	2016	2.4

Source: Oxford Economics (December 2017).
Regions reflect the regional structure of the Schaeffler Group.

[1] Average vehicle age, worldwide and for the Schaeffler Group's various regions, was calculated based on approx. 84% of the global vehicle population (IHS, February 2018).

Prices of aluminum, copper, and zinc No. 043
in percent (12/31/2015 = 100)



Source: Bloomberg, based on London Metal Exchange (USD/metric ton).

Greater China region's industrial production was up significantly by 6.2%, although growth was slightly less dynamic in the second half of the year. Industrial production in the Asia/Pacific region increased by 3.9%, mainly driven by the favorable trend in Japan; South Korea reported more dynamic growth as well.

Procurement markets

The Schaeffler Group uses various materials, especially various types of steel, aluminum, zinc, as well as plastics and lubricants. Commodity market price trends affect the Schaeffler Group's cost to varying degrees and in some instances with some delay, depending on the terms of the relevant supplier contracts.

Prices in the **procurement markets** for most of the Schaeffler Group's significant input materials increased during the year. Comparing annual averages to prior year showed higher price levels across the board.

Steel is used to manufacture rolling bearings and automotive components. Depending on the source region, average prices for cold- and hot-rolled steel increased by between approx. 13 to just under 40% compared to prior year. The price of metallurgical coal, an important input material for steel and especially carbon-based castings, rose by approx. 30%.

Aluminum is primarily used for pressure die castings and stamped and bent parts, while applications for zinc include coating mechanical components. Copper is mainly required for use in electric motors and mechatronic components. Higher global demand combined with a decrease in supply in China drove up the annual average price of aluminum by more than 20%. The copper price increased by over 25%, with reasons including higher growth rates in industrial production. The mean price of zinc was nearly 40% higher than the prior year average.

The Schaeffler Group uses plastics, for instance to produce cages for rolling bearings, as lubricants designed to reduce friction in components, and as preservatives. Plastics and lubricants are often made based on crude oil. Increased demand and the continuation of the OPEC agreement on limiting production volumes brought the crude oil price to its highest level in two years. The annual average was still just under 25% higher than the prior year average. Based on the ICIS Global Petrochemical Index (IPEX), average prices of processed petrochemical products, including the plastics used by the Schaeffler Group, rose by over 15% compared to the prior year average.

2.2 Course of business

Overview of results of operations 2017

The Schaeffler Group continued its positive revenue trend in 2017, buoyed especially by the encouragingly dynamic growth in the second half of the year. The Automotive business once again grew faster than the market, i.e. global production of passenger cars and light commercial vehicles. The measures to improve efficiency and reduce costs in the Industrial division were consistently executed and are proving effective.

The Schaeffler Group's **revenue** increased by 5.1% to EUR 14,021 m in 2017 (prior year: EUR 13,338 m). Excluding the impact of currency translation, revenue increased by 5.9%, which was attributable to both divisions. All of the Schaeffler Group's regions, and especially Greater China, contributed to this growth.

The market and competitive environment of the Automotive division continued to be characterized by the dynamic evolution of mobility in 2017, which entails ongoing technological change and the accompanying high capital expenditures. In this challenging environment, the division increased its revenue by 5.1% to EUR 10,869 m (prior year: EUR 10,338 m). Excluding the impact of currency translation, the division generated 5.9% in additional revenue. Revenue growth for the fourth quarter, excluding the impact of currency translation, amounted to 8.3%. Thanks to the strong third and fourth quarters the Automotive division once again expanded faster than global production volumes for passenger cars and light commercial vehicles, which grew by 2.1% during the year.

With global industrial production increasing, the Industrial division expanded its revenue for the year by 5.1% to EUR 3,152 m (prior year: EUR 3,000 m). Excluding the impact of currency translation, the division generated revenue growth of 5.7% primarily due to higher volumes in the Greater China region. In the fourth quarter, the Industrial division grew its revenue by 9.0%, excluding the impact of translation. These figures demonstrate that the Industrial division has returned to a long-term growth path.

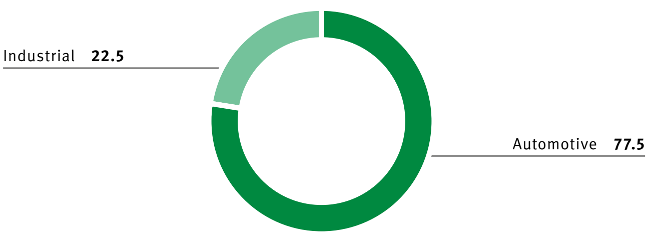
The Schaeffler Group's EBIT for the reporting period amounted to EUR 1,528 m (prior year: EUR 1,556 m), resulting in an EBIT margin of 10.9% (prior year: 11.7%). Before special items[2] of EUR 56 m, EBIT amounted to EUR 1,584 m (prior year: EUR 1,700 m). The group's **EBIT margin before special items** amounted to 11.3% (prior year: 12.7%). The Industrial division's EBIT margin before special items improved to 8.1% (prior year: 7.3%), thus continuing to stabilize. Meanwhile, the Automotive division's EBIT margin before special items declined to 12.2% (prior year: 14.3%), primarily due to increased pricing pressure in the automotive original equipment business in combination with rising costs for new product launches and higher other expenses in connection with increased research and development expenses.

Net income increased by 14.3% from EUR 872 m to EUR 997 m. Excluding net income attributable to non-controlling interests of EUR 17 m (prior year: EUR 13 m), net income attributable to shareholders of the parent company amounted to EUR 980 m, 14.1% more than in the prior year (prior year: EUR 859 m). Earnings per common share amounted to EUR 1.47 (prior year: EUR 1.29). Earnings per common non-voting share amounted to EUR 1.48 (prior year: EUR 1.30).

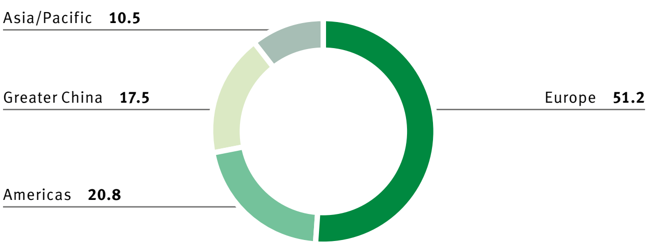
The Schaeffler Group generated **free cash flow** of EUR 488 m in 2017, EUR 247 m less than the prior year amount of EUR 735 m. One reason for the decrease was cash flow from operating activities declining from EUR 1,876 m to EUR 1,778 m, one of the reasons being non-persistent cash outflows in 2017. Another reason was the increase in capital expenditures (capex) by 11.1% to EUR 1,273 m (prior year: EUR 1,146 m) or 9.1% of revenue (prior year: 8.6%) in 2017.

Schaeffler Value Added before special items **(SVA)** amounted to EUR 787 m during the reporting period (prior year: EUR 939 m), representing a return on capital employed **(ROCE)** before special items of 19.9% (prior year: 22.3%). The decline was the result of the weaker earnings trend compared to the prior year as well as an increase in average capital employed.

Schaeffler Group revenue by division No. 044
in percent



Schaeffler Group revenue by region No. 045
in percent by market view



[2] Please refer to pp. 60 et seq. for the definition of special items.

Significant events 2017

Fitch assigns investment grade rating to Schaeffler AG

On April 25, 2017, rating agency Fitch Ratings published its first rating of Schaeffler AG. Fitch assigned a rating of BBB- (investment grade) to Schaeffler AG with a stable outlook. The bonds were also rated BBB-. Thus, Schaeffler AG is now rated by three rating agencies – Fitch, Moody's, and Standard & Poor's.

Dividend – increase to 50 cents per common non-voting share

On April 26, 2017, Schaeffler AG's annual general meeting passed a resolution to pay a dividend of EUR 0.49 per common share (prior year: EUR 0.34; special dividend EUR 0.15) and EUR 0.50 per common non-voting share (prior year: EUR 0.35; special dividend EUR 0.15) to Schaeffler AG's shareholders for 2016. This represents a dividend of 34.1% of net income attributable to shareholders before special items, falling within the dividend payout ratio of 30 to 40% planned by the company.

Schaeffler accelerates transformation

The Schaeffler Group's Strategy Dialog held on July 10 to 13, 2017, was devoted to the necessary decisions on the direction to be taken with respect to certain strategic issues. One of these was the decision to create an independent E-Mobility business division bringing together all products and system solutions for hybrid and pure battery-electric vehicles as of January 01, 2018. Further, the company is setting up an additional competence center for E-Mobility in China, alongside the existing German E-Mobility competence center in Buehl, to accommodate the increasing importance of the Chinese market in the field of E-Mobility. In the Industrial division, the entire industry-specific business with mechatronic systems and digital services as well as the required related components have been combined in an independent organizational unit Industry 4.0 since January 01, 2018. The strategic decisions were made based on the model of an integrated automotive and industrial supplier and the company's strategy "Mobility for tomorrow" with its three key opportunities for the future – E-Mobility, Industry 4.0, and Digitalization.

Indian subsidiaries being merged

On August 30, 2017, the Schaeffler Group announced its intention to merge its three subsidiaries in India – Schaeffler India Ltd. (previously FAG Bearings India Ltd.), INA Bearings India Private Ltd., and LuK India Private Ltd. The merger is subject to the required local regulatory approvals and the consent of the minority shareholders. The transaction is expected to close in the third quarter of 2018. The objective of the transaction is to simplify the existing structure, reduce complexity, and create a strong Schaeffler entity in India in order to better realize the potential for future growth in India. Based on the strategy "Mobility for tomorrow" and the "Agenda 4 plus One" excellence program, the company is also taking another important step toward establishing the "Schaeffler" brand as a global umbrella brand and ensuring a uniform brand identity worldwide. The company will be known as "Schaeffler India Limited" and remain listed. The transaction increases Schaeffler AG's indirect interest in Schaeffler India Limited from currently approx. 51% to approx. 74%.

Schaeffler sets up third division

At its meeting on October 05, 2017, the Executive Committee of the Supervisory Board of Schaeffler AG accepted the proposal of the Board of Managing Directors to separate the Automotive Aftermarket from the Automotive division of Schaeffler AG and to set it up as a third stand-alone division as of January 01, 2018. As a consequence, the Schaeffler Group will divide its business into three divisions – Automotive OEM, Automotive Aftermarket, and Industrial.

On that basis, the Supervisory Board of Schaeffler AG decided to appoint Michael Söding to become member of the Board of Managing Directors of Schaeffler AG effective January 01, 2018. He has assumed responsibility for the Automotive Aftermarket business at board level. Previously, Michael Söding had been Head of Automotive Aftermarket within the Automotive division since 2009.

The three divisions of the Schaeffler Group will in future be managed from decentralized divisional headquarters located in Buehl, Langen, and Schweinfurt. The Automotive OEM division will be headquartered in Buehl. The new Automotive Aftermarket division will be managed from Langen. The Industrial division continues to be located in Schweinfurt. The corporate head office of the Schaeffler Group is in Herzogenaurach.

Investing in Aftermarket Kitting Operation (AKO)

In November 2017, the Board of Managing Directors of Schaeffler AG and its Supervisory Board approved a EUR 180 m investment to build a new state-of-the-art assembly and packaging center called "Aftermarket Kitting Operation" (AKO) in the "Star Park" industrial estate in the city of Halle (Saale) in Saxony-Anhalt. Occupying an area of about 40,000 square meters, the new facility will assemble and package kits from Schaeffler's inventory of automotive aftermarket spare parts and repair solutions. The new assembly and packaging center will further optimize the Schaeffler Group's Automotive Aftermarket processes and generate sustained improvements in quality of delivery.

Execution of M&A strategy continued

On October 04, 2017, the Schaeffler Group concluded a purchase agreement for 100% of the shares in autinity systems GmbH. The Chemnitz-based IT company specializes in digital machine data recording and evaluation. The acquisition represents another important step in implementing the Schaeffler Group's Digital Agenda and is part of the M&A strategy adopted by the company. The M&A strategy supports the strategy "Mobility for tomorrow" by targeting additional technological capabilities for Industrial and Automotive in seven strategic focus areas.

One year after acquiring a majority interest in Compact Dynamics GmbH, the Schaeffler Group acquired the remaining 49% interest in this company from SEMIKRON International GmbH on December 12, 2017. Compact Dynamics GmbH, based in Starnberg, is a development specialist in the field of innovative electric drive concepts with a focus on high-performance drives and integrated lightweight construction in small volume production and motor sport applications. The acquisition expands Schaeffler's expertise in the field of electric motors and power electronics for developing and manufacturing electric drives.

Changes in Board membership

At its meeting on July 17, 2017, the Supervisory Board of Schaeffler AG appointed Dietmar Heinrich (previously Regional CEO Europe) to the Board of Managing Directors. On August 01, 2017, Dietmar Heinrich took up his role as Chief Financial Officer of Schaeffler AG, replacing Dr. Ulrich Hauck. The Supervisory Board also decided to extend the contract of Dr. Stefan Spindler, CEO Industrial, for a term of five years ending on April 30, 2023. Jürgen Ziegler was appointed to the Schaeffler Group's Executive Board effective August 01, 2017, succeeding Dietmar Heinrich as Regional CEO Europe.

In November 2017, Oliver Jung, Chief Operating Officer, informed the Supervisory Board that he will not renew the contract for his position on the Board of Managing Directors, which expires on September 30, 2018. The Supervisory Board took note of Oliver Jung's wish.

Results of operations compared to outlook 2017

Comparison to outlook 2017 No. 046

	Actual 2016	Outlook 2017	Actual 2017
Revenue growth [1]	3.4%	4 to 5%	5.9%
EBIT margin before special items [2]	12.7%	11 to 12% [3]	11.3%
Free cash flow	EUR 735 m	~ EUR 500 m [4]	EUR 488 m

[1] Compared to prior year; excluding the impact of currency translation.
[2] Please refer to pp. 60 et seq. for the definition of special items.
[3] Adjusted to 11 to 12% (original outlook 12 to 13%) on June 26, 2017.
[4] Adjusted to ~ EUR 500 m (original outlook ~ EUR 600 m) on June 26, 2017.

The Schaeffler Group had issued guidance regarding revenue growth of 4 to 5% for 2017, excluding the impact of currency translation. This guidance was based on the assumption that global automobile production would expand by approx. 1.5% and worldwide industrial production would grow slightly. Based on these considerations, the company expected to generate an EBIT margin before special items of 12 to 13%. In addition, the company expected approx. EUR 600 m in free cash flow. On June 26, 2017, the Board of Managing Directors decided to reduce its guidance for the EBIT margin before special items to 11 to 12% due to a substantially lower earnings development in the Automotive division in the second quarter of 2017 compared to the prior year. At the same time, the guidance for free cash flow was reduced from approx. EUR 600 m to approx. EUR 500 m. The company confirmed its revenue guidance.

Excluding the impact of currency translation, the Schaeffler Group's revenue grew by 5.9% in 2017. Thus, the Schaeffler Group has exceeded its revenue target for 2017 of 4 to 5%. The Automotive division raised its revenue by 5.9% compared to the prior year, excluding the impact of currency translation. The Industrial division reported additional revenue of 5.7% excluding the impact of currency translation.

The EBIT margin before special items of 11.3% falls within the company's earnings guidance of 11 to 12% (previously 12 to 13%), which it had reduced on June 26, 2017.

Free cash flow for 2017 amounted to EUR 488 m, also reaching the outlook reduced to approx. EUR 500 m (previously approx. EUR 600 m) on June 26, 2017. Free cash flow included EUR 27 m in net cash outflow for M&A activities.

Schaeffler Group

Revenue EUR 14,021 m

EBIT margin before special items 11.3%

Positive revenue trend continued – revenue growth at 5.9% at constant currency // Both divisions contribute to the encouraging trend // Growth continues to gather momentum in the second half of the year – strong Q4 with growth of 8.5% at constant currency // Double-digit growth in the Greater China region in 2017 // EBIT before special items at EUR 1.6 bn // Earnings quality below prior year – both divisions' EBIT margins stabilized in the second half of 2017 // R&D activities expanded considerably // Earnings per common non-voting share increased to EUR 1.48 (prior year: EUR 1.30)

Schaeffler Group earnings No. 047

in € millions	2017	2016	Change in %
Revenue	**14,021**	**13,338**	**5.1**
• at constant currency			5.9
Revenue by division			
Automotive	10,869	10,338	5.1
• at constant currency			5.9
Industrial	3,152	3,000	5.1
• at constant currency			5.7
Revenue by region [1)]			
Europe	7,183	7,077	1.5
• at constant currency			1.4
Americas	2,910	2,803	3.8
• at constant currency			4.6
Greater China	2,456	2,053	19.6
• at constant currency			24.1
Asia/Pacific	1,472	1,405	4.8
• at constant currency			5.6
Cost of sales	-10,175	-9,552	6.5
Gross profit	**3,846**	**3,786**	**1.6**
• in % of revenue	27.4	28.4	-
Research and development expenses	-846	-751	12.6
Selling and administrative expenses	-1,413	-1,343	5.2
Earnings before financial result and income taxes (EBIT)	**1,528**	**1,556**	**-1.8**
• in % of revenue	10.9	11.7	-
Special items [2)]	56	144	-61.1
EBIT before special items	**1,584**	**1,700**	**-6.8**
• in % of revenue	11.3	12.7	-
Financial result	-192	-341	-43.7
Income taxes	-339	-343	-1.2
Net income [3)]	980	859	14.1
Earnings per common non-voting share (basic/diluted, in €)	1.48	1.30	13.8

[1)] Based on market (customer location).
[2)] Please refer to pp. 60 et seq. for the definition of special items.
[3)] Attributable to shareholders of the parent company.

2.3 Earnings

Schaeffler Group earnings

The Schaeffler Group increased its revenue by 5.1% to EUR 14,021 m in 2017 (prior year: EUR 13,338 m). Excluding the impact of currency translation, revenue grew by 5.9%. Both divisions contributed to this encouraging performance. Thanks to the strong third and fourth quarters, the Automotive division generated 5.9% in additional revenue, excluding the impact of currency translation. The Industrial division grew its revenue by 5.7% excluding the impact of currency translation, reporting a growth rate excluding the impact of currency translation of 9.0% for the fourth quarter of 2017. These figures demonstrate that the Industrial division has returned to a long-term growth path.

All regions of the Schaeffler Group contributed to the increase in revenue in 2017. Revenue in the Europe region was up 1.5% (+1.4% at constant currency), with both divisions reporting similar growth rates. The Americas region reported growth of 3.8% (+4.6% at constant currency). Along with the Automotive business, the Industrial division's business also made a positive impact, growing again after declining in the prior year. The Greater China region once again reported the most dynamic growth in the reporting year. Revenue there was up 19.6% (+24.1% at constant currency) thanks to the encouraging performance of both divisions. The Asia/Pacific region generated a 4.8% revenue growth rate (+5.6% at constant currency) with the support of both divisions.

Cost of sales increased by 6.5% to EUR 10,175 m (prior year: EUR 9,552 m) during the year. Gross profit improved by 1.6% or EUR 60 m to EUR 3,846 m (prior year: EUR 3,786 m). The company's gross margin declined to 27.4% (prior year: 28.4%). Affected by the impact of sales prices and currency translation it could not fully offset, the Automotive division saw its gross margin fall to 27.2% (prior year: 28.5%). The gross margin of the Industrial division, on the other hand, rose to 28.3% (prior year: 27.9%), since a favorable volume impact more than offset the adverse impact of sales prices and currency translation.

Research and development expenses increased significantly by 12.6% to EUR 846 m in the reporting period (prior year: EUR 751 m), representing an R&D ratio of 6.0% (prior year: 5.6%) of revenue. Apart from inflation-related cost increases, the increase is especially attributable to a focused expansion of the headcount in connection with the strategic alignment of the company's research and development capacities in order to lay the foundation for future growth.

Selling and administrative expenses increased by 5.2% to EUR 1,413 m (prior year: EUR 1,343 m) in the reporting year, mainly due to higher selling expenses (+6.0%). These higher expenses resulted primarily from increased logistics expenses driven by rising volumes, due, among other things, to the significant expansion of the business in the Greater China region. Total functional costs rose by 7.9% to EUR 2,259 m (prior year: EUR 2,094 m), growing to 16.1% of revenue (prior year: 15.7%).

EBIT decreased by EUR 28 m or 1.8% to EUR 1,528 m (prior year: EUR 1,556 m) during the reporting period. The Schaeffler Group's EBIT margin was 10.9% (prior year: 11.7%). In 2017, the group's EBIT was adversely affected by EUR 56 m in special items (prior year: EUR 144 m), including EUR 17 m in special items for legal cases resulting from provisions for claims for damages. In addition, the company recognized EUR 39 m in restructuring expenses incurred to set up a shared service center in Europe in 2017. The prior year included EUR 86 m in special items for legal cases resulting from provisions for claims for damages in antitrust cases and for other compliance cases. The company also recognized restructuring expenses of EUR 45 m in connection with the second wave of the program "CORE" in the prior year. Additionally, the prior year was adversely affected by other special items of EUR 13 m resulting from streamlining the production portfolio. Based on these items, EBIT before special items declined to EUR 1,584 m (prior year: EUR 1,700 m) in 2017, and the EBIT margin before special items dropped to 11.3% (prior year: 12.7%). The decline was primarily due to the decrease in gross margin as described above and the significantly expanded R&D activities, mainly in the Automotive division. In addition, the EBIT margin was also affected by an adverse impact of currency translation.

The Schaeffler Group's financial result improved by EUR 149 m to EUR -192 m (prior year: EUR -341 m) in 2017.

Schaeffler Group financial result No. 048

in € millions	2017	2016
Interest expense on financial debt [1]	-123	-286
Interest income on shareholder loans	0	49
Gains and losses on derivatives and foreign exchange	-17	-33
Fair value changes on embedded derivatives	-14	-30
Interest income and expense on pensions and partial retirement obligations	-38	-45
Other	0	4
Total	**-192**	**-341**

[1] Incl. amortization of transaction costs and prepayment penalties.

Interest expense on financial debt amounted to EUR 123 m in 2017 (prior year: EUR 286 m) and included prepayment penalties of EUR 13 m (prior year: EUR 48 m) and EUR 5 m (prior year: EUR 31 m) in deferred transaction costs derecognized.

In 2016, IHO Verwaltungs GmbH prepaid its loans payable to Schaeffler AG in full. As a result, the Schaeffler Group no longer earned any interest income on loans to shareholders in 2017 (prior year: EUR 49 m).

Net foreign exchange losses on financial assets and liabilities and net losses on derivatives amounted to EUR 17 m (prior year: EUR 33 m). These include the impact of translating the financing instruments denominated in U.S. dollars to euros and hedges of these instruments using cross-currency swaps.

Fair value changes on embedded derivatives, primarily prepayment options for external financing instruments, resulted in net losses of EUR 14 m (prior year: EUR 30 m).

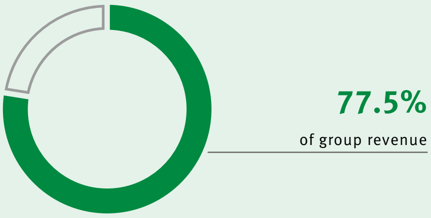
Income tax expense amounted to EUR 339 m in 2017 (prior year: EUR 343 m), resulting in an effective tax rate of 25.4% (prior year: 28.2%) The change compared to the prior year resulted primarily from lower non-deductible expenses of EUR 24 m (prior year: EUR 32 m) and from additional income tax benefits related to prior years of EUR 29 m (prior year: EUR 7 m). The U.S. tax reform had comparatively little impact on the Schaeffler Group's deferred taxes.

Net income attributable to shareholders of the parent company for 2017 was EUR 980 m (prior year: EUR 859 m). Net income before special items amounted to EUR 1,022 m (prior year: EUR 962 m). The Board of Managing Directors and the Supervisory Board will propose a dividend for 2017 of EUR 0.54 (prior year: EUR 0.49) per common share and EUR 0.55 (prior year: EUR 0.50) per common non-voting share to the annual general meeting. This represents a dividend of 35.4% (prior year: 34.1%) of net income attributable to shareholders before special items.

Basic and diluted earnings per common share increased to EUR 1.47 (prior year: EUR 1.29) in 2017. Basic and diluted earnings per common non-voting share amounted to EUR 1.48 (prior year: EUR 1.30). The number of shares used to calculate earnings per common share and earnings per common non-voting share was 500 million (prior year: 500 million) and 166 million (prior year: 166 million), respectively.

Automotive division

Revenue EUR 10,869 m



EBIT margin before special items 12.2%

Revenue up 5.9% at constant currency – strong Q3 and Q4 2017 // Growth driven by Automotive OEM as well as by Aftermarket business // Growth once again exceeds global automobile production // Revenue growth in all regions – China business maintains highly dynamic growth // Earnings quality below prior year // Higher expenses for R&D: activities for E-Mobility and for improving drives reducing fuel consumption and emissions expanded // Independent business division for E-Mobility starting January 01, 2018

Automotive division earnings No. 049

in € millions	2017	2016	Change in %
Revenue	**10,869**	**10,338**	**5.1**
• at constant currency			5.9
Revenue by business division			
BD Engine Systems	2,787	2,646	5.3
• at constant currency			6.7
BD Transmission Systems	4,620	4,346	6.3
• at constant currency			7.4
BD Chassis Systems	1,588	1,533	3.6
• at constant currency			4.2
BD Automotive Aftermarket	1,874	1,813	3.4
• at constant currency			3.2
Revenue by region [1]			
Europe	5,380	5,305	1.4
• at constant currency			1.3
Americas	2,335	2,242	4.1
• at constant currency			4.9
Greater China	1,984	1,675	18.4
• at constant currency			22.9
Asia/Pacific	1,170	1,116	4.8
• at constant currency			5.8
Cost of sales	-7,915	-7,389	7.1
Gross profit	**2,954**	**2,949**	**0.2**
• in % of revenue	27.2	28.5	-
Research and development expenses	-713	-618	15.4
Selling and administrative expenses	-908	-833	9.0
EBIT	**1,283**	**1,373**	**-6.6**
• in % of revenue	11.8	13.3	-
Special items [2]	47	108	-56.5
EBIT before special items	**1,330**	**1,481**	**-10.2**
• in % of revenue	12.2	14.3	-

Prior year information presented based on 2017 segment structure.
[1] Based on market (customer location).
[2] Please refer to pp. 60 et seq. for the definition of special items.

Automotive division earnings

Automotive division revenue increased by 5.1% to EUR 10,869 m (prior year: EUR 10,338 m) in 2017. Excluding the impact of currency translation, the growth rate was 5.9%. Thus, in 2017, the division once again expanded faster than the market, i.e. global production volumes for passenger cars and light commercial vehicles, which grew by 2.1% in 2017. This expansion was largely attributable to encouragingly dynamic growth in the second half of 2017, driven by both the Automotive OEM and the Aftermarket business.

Overall, revenue trends varied widely across market regions in 2017. The Europe region reported slight revenue growth of 1.4% (+1.3% at constant currency), less than average regional growth in production volumes (+3.9%). The Americas region reported 4.1% (+4.9% at constant currency) in additional revenue, growing faster than regional vehicle production, which declined by 0.9%. The Automotive division once again significantly expanded its revenue in the Greater China region, especially due to product ramp-ups in the Automotive OEM business. The Automotive division generated a total of 18.4% (+22.9% at constant currency) in additional revenue in Greater China, while regional vehicle production increased by 2.6%. Reasons for the increase Asia/Pacific region revenue by 4.8% (+5.8% at constant currency) included product ramp-ups, with vehicle production there rising by 2.1%.

The Automotive division business is organized in the Engine Systems, Transmission Systems, Chassis Systems, and Automotive Aftermarket business divisions (BD), all of which reported revenue growth in 2017.

The **Engine Systems BD** generated revenue growth of 5.3% (+6.7% at constant currency) in 2017, largely driven by the valve train product groups, mainly fully variable valve train systems (primarily Multiair). The camshaft phasing units product group also saw significant increases, especially for electric phasing systems. In addition, the innovative thermal management module, which is required in both internal combustion engines and future mobility concepts, also performed very well.

Transmission Systems BD revenue rose by 6.3% (+7.4% at constant currency), with revenue from components for automated transmissions, such as torque converters and dual clutches, generating double-digit growth rates. Revenue in the dual-mass flywheel product group was up significantly as well. The business division's growth was primarily driven by product ramp-ups in the Greater China region.

The **Chassis Systems BD** generated revenue growth of 3.6% (+4.2% at constant currency) mainly based on the solid growth in revenue from the newest generation of wheel bearings in the Greater China region.

The **Automotive Aftermarket BD** increased revenue by 3.4% (+3.2% at constant currency) in 2017, mainly due to increased requirements in the independent aftermarket in the Americas region.

Cost of sales rose by 7.1% to EUR 7,915 m (prior year: EUR 7,389 m) in 2017, growing faster than revenue. Gross profit amounted to EUR 2,954 m (prior year: EUR 2,949 m). The gross margin declined by 1.3 percentage points to 27.2% (prior year: 28.5%), mainly due to adverse pricing effects, which could not be compensated by corresponding production cost optimization.

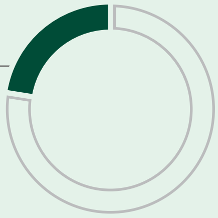
Functional costs increased by 11.7% to EUR 1,621 m (prior year: EUR 1,451 m), rising to 14.9% of revenue (prior year: 14.0%). The main driver of this increase was the rise in research and development expenses by 15.4% to EUR 713 m (prior year: EUR 618 m) or 6.6% (prior year: 6.0%) of revenue. Apart from the increased activities in the field of E-Mobility, which has already won several volume production orders, the higher research and development expenses also reflect projects aimed at further optimizing the drive train based on an internal combustion engine. Selling and administrative expenses of EUR 908 m were 9.0% ahead of prior year (prior year: EUR 833 m). The increase is primarily the result of higher logistics expenses driven by higher volumes that were mainly attributable to significantly expanded business in the Greater China region.

EBIT for the reporting period amounted to EUR 1,283 m (prior year: EUR 1,373 m), and the division's EBIT margin was 11.8% (prior year: 13.3%). In 2017, the division's EBIT was adversely affected by EUR 47 m in special items (prior year: EUR 108 m), including EUR 17 m in special items for legal cases resulting from provisions for claims for damages. In addition, the division recognized its share of restructuring expenses incurred to set up a shared service center in Europe amounting to EUR 30 m in 2017. The prior year included EUR 82 m in special items for legal cases resulting from provisions for claims for damages in antitrust cases and for other compliance cases. Furthermore, EUR 13 m in expenses relating to the Automotive division in connection with the second wave of the program "CORE" (consolidation of shared functions and plant structures) were recognized in the prior year. Additionally, the prior year was adversely affected by other special items of EUR 13 m resulting from streamlining the production portfolio. Based on these items, EBIT before special items declined to EUR 1,330 m (prior year: EUR 1,481 m) in 2017, and the EBIT margin before special items fell to 12.2% (prior year: 14.3%). Apart from the lower gross margin, reasons for the decline include rising R&D costs and other expenses. E-Mobility R&D activities were expanded considerably in order to lay the foundation for future growth. The EBIT margin was also affected by an adverse impact of currency translation.

Industrial division

Revenue EUR 3,152 m

22.5%
of group revenue



EBIT margin before special items 8.1%

Industrial division back on long-term growth path: revenue increases by 5.7% at constant currency – growth rate for Q4 at 9.0% // Mainly driven by power transmission, offroad, and raw materials sector clusters // Significant additional revenue in the Greater China region // Margins stabilized further – gross and EBIT margins increased over prior year // Cost and efficiency measures are consistently executed and proving effective

Industrial division earnings No. 050

in € millions	2017	2016	Change in %
Revenue	**3,152**	**3,000**	**5.1**
• at constant currency			5.7
Revenue by region [1]			
Europe	1,803	1,772	1.8
• at constant currency			1.7
Americas	575	561	2.5
• at constant currency			3.3
Greater China	472	378	24.9
• at constant currency			29.3
Asia/Pacific	302	289	4.5
• at constant currency			4.9
Cost of sales	-2,260	-2,163	4.5
Gross profit	**892**	**837**	**6.6**
• in % of revenue	28.3	27.9	-
Research and development expenses	-133	-133	0.0
Selling and administrative expenses	-505	-510	-1.0
EBIT	245	**183**	**33.9**
• in % of revenue	7.8	6.1	-
Special items [2]	9	36	-75.0
EBIT before special items	**254**	**219**	**16.0**
• in % of revenue	8.1	7.3	-

Prior year information presented based on 2017 segment structure.
[1] Based on market (customer location).
[2] Please refer to pp. 60 et seq. for the definition of special items.

Industrial division earnings

Industrial division revenue increased by 5.1% to EUR 3,152 m (prior year: EUR 3,000 m) in 2017. Excluding the impact of currency translation, the division generated 5.7% in additional revenue and has thus returned to a growth path. This growth was mainly driven by significant increases in the power transmission, offroad, and raw materials sector clusters, all three of which reported double-digit growth rates. The industrial automation and Industrial Distribution sector clusters also made significant contributions to the division's growth, while revenue in the aerospace and railway sector clusters grew slightly. The two-wheelers and wind sector clusters, however, experienced declining revenue.

The Industrial business is primarily managed based on regions. On this basis, the Europe, Americas, Greater China, and Asia/Pacific regions operate as profit centers responsible for the Industrial business in their respective markets.

In the **Europe region,** revenue rose by 1.8% (+1.7% at constant currency), mainly due to higher sales in Industrial Distribution. The raw materials, offroad, power transmission, and industrial automation sector clusters also reported considerably higher revenue. Revenue in the wind, aerospace, and railway sector clusters, however, declined from the prior year period. The two-wheelers sector cluster was flat with prior year.

The **Americas region** reported a considerable increase in revenue of 2.5% (+3.3% at constant currency) during the reporting period. This trend was primarily driven by double-digit revenue growth rates in the raw materials, offroad, and power transmission sector clusters. The aerospace sector cluster and Industrial Distribution generated revenue growth as well. The railway, wind, two-wheelers, and industrial automation sectors experienced declining revenue in 2017.

The **Greater China region** reported significant revenue growth of 24.9% (+29.3% at constant currency), with all significant sector clusters reporting double-digit growth rates. The region's encouraging revenue trend was bolstered significantly by considerable increases in demand in the power transmission, wind, industrial automation, railway, and raw materials sector clusters. Industrial Distribution revenue was in line with prior year.

In the **Asia/Pacific region,** revenue increased by 4.5% (+4.9% at constant currency), driven, in particular, by the aerospace, offroad, and power transmission sector clusters. The sector clusters railway, industrial automation and two-wheelers, and industrial distribution generated revenue growth as well. The significant decrease in demand in the raw materials sector cluster had an adverse influence on the region's revenue trend.

Industrial division cost of sales increased by 4.5% to EUR 2,260 m (prior year: EUR 2,163 m), growing less than revenue. In total, the Industrial division improved its gross profit by EUR 55 m or 6.6% to EUR 892 m (prior year: EUR 837 m). The division's gross margin of 28.3% was 0.4 percentage points ahead of the prior year level (prior year: 27.9%). The division offset price reductions as well as cost increases, primarily due to collectively bargained wage and salary increases, with operational improvements in costs and economies of scale. The fourth quarter of 2017 was adversely affected by quality-related expenses and by temporary productivity losses resulting from extremely high utilization of capacity. The division plans to step up its investments in additional capacity in 2018.

Functional costs of EUR 638 m (prior year: EUR 643 m) were slightly below the prior year level. Functional costs as a percentage of revenue fell to 20.2% (prior year: 21.4%). Research and development expenses amounted to EUR 133 m (prior year: EUR 133 m), and selling and administrative expenses were EUR 505 m (prior year: EUR 510 m). The cost reduction measures of the program "CORE" more than offset inflation-related cost increases, particularly in personnel expenses, as well as higher group overheads.

The Industrial division increased its EBIT for 2017 to EUR 245 m (prior year: EUR 183 m), while its EBIT margin stabilized further, improving by 1.7 percentage points to 7.8% (prior year: 6.1%). EBIT was adversely affected by EUR 9 m in special items representing the Industrial division's share of restructuring expenses incurred to set up a shared service center in Europe in 2017. The prior year was adversely affected by EUR 36 m in special items, including EUR 32 m in restructuring expenses for the stepped-up efficiency measures aimed at revitalizing the Industrial division as part of the second wave of the program "CORE". In addition, the division had recognized EUR 4 m in expenses for legal cases in the prior year. Based on these items, EBIT before special items improved to EUR 254 m (prior year: EUR 219 m) in 2017, and the EBIT margin before special items increased to 8.1% (prior year: 7.3%). The increase was the result of an increase in gross profit as described above and the success of the program "CORE", with cost and efficiency measures consistently executed and beginning to prove effective for the long-term. Currency translation had an adverse effect on the division's EBIT margin, however.

Performance indicators and special items

Reconciliation

No. 051

	2017	2016	2017	2016	2017	2016
Income statement (in € millions)		Total		Automotive		Industrial
EBIT	**1,528**	**1,556**	**1,283**	**1,373**	**245**	**183**
• in % of revenue	10.9	11.7	11.8	13.3	7.8	6.1
Special items	**56**	**144**	**47**	**108**	**9**	**36**
• Legal cases	17	86	17	82	0	4
• Restructuring	39	45	30	13	9	32
• Other	0	13	0	13	0	0
EBIT before special items	**1,584**	**1,700**	**1,330**	**1,481**	**254**	**219**
• in % of revenue	11.3	12.7	12.2	14.3	8.1	7.3
EBITDA	**2,295**	**2,293**				
Special items	**56**	**144**				
• Legal cases	17	86				
• Restructuring	39	45				
• Other	0	13				
EBITDA before special items	**2,351**	**2,437**				
Net income [1]	**980**	**859**				
Special items	**56**	**144**				
• Legal cases	17	86				
• Restructuring	39	45				
• Other	0	13				
– Tax effect [2]	-14	-41				
Net income before special items [1]	**1,022**	**962**				
Statement of financial position (in € millions)	**12/31/2017**	**12/31/2016**				
Net financial debt	2,370	2,636				
/ EBITDA	2,295	2,293				
Net financial debt to EBITDA ratio	**1.0**	**1.1**				
Net financial debt	2,370	2,636				
/ EBITDA before special items	2,351	2,437				
Net financial debt to EBITDA ratio before special items	**1.0**	**1.1**				
Value-based management (in € millions)	**2017**	**2016**				
EBIT	1,528	1,556				
/ Average capital employed	7,966	7,613				
ROCE (in %)	**19.2**	**20.4**				
EBIT before special items	1,584	1,700				
/ Average capital employed	7,966	7,613				
ROCE before special items (in %)	**19.9**	**22.3**				
EBIT	1,528	1,556				
– Cost of capital	797	761				
Schaeffler Value Added (SVA)	**731**	**795**				
EBIT before special items	1,584	1,700				
– Cost of capital	797	761				
SVA before special items	**787**	**939**				

[1] Attributable to shareholders of the parent company.
[2] Based on the group's effective tax rate for the relevant year.

The information on the Schaeffler Group's earnings, net assets, and financial position is based on the requirements of International Financial Reporting Standards (IFRS) and, where applicable, German commercial law and German Accounting Standards (GAS).

In addition to the disclosures required by these standards, the Schaeffler Group also discloses certain performance indicators that are not defined in the relevant financial reporting standards. The company presents these measures in accordance with the Guidelines on Alternative Performance Measures issued by the European Securities and Markets Authority, ESMA. Therefore, these indicators should be considered supplementary information. They are designed to provide comparability over time and across sectors and are calculated by making certain adjustments to, or calculating ratios between, line items contained in the income statement, statement of financial position, or statement of cash flows prepared in accordance with applicable financial reporting standards.

Performance indicators

These performance indicators include EBIT, EBITDA, the net debt to EBITDA ratio, ROCE, and SVA. The key indicators used in evaluating the company's operations are EBIT and the EBIT margin. **EBIT** is defined as earnings before financial result and income taxes. The EBIT margin represents EBIT as a percentage of revenue. In addition to EBIT, the company calculates **EBITDA,** which represents EBIT before amortization of intangible assets, depreciation of property, plant and equipment, and impairment losses. It is primarily used to calculate the **net debt to EBITDA ratio.** This ratio is used to evaluate the financing structure and is the ratio of net financial debt to EBITDA, where net financial debt is defined as the sum of current and non-current financial debt net of cash and cash equivalents. The Schaeffler Group's key value-based performance indicator is **ROCE** as well as **SVA,** which is closely linked to ROCE.

More on ROCE and SVA on pp. 30 et seq.

The Schaeffler Group also calculates certain additional performance measures not defined in the relevant financial reporting standards. These are defined and discussed in the relevant chapters.

Special items

In order to make the evaluation of the company's results of operations as transparent as possible, the Schaeffler Group reports the indicators described above before special items (=adjusted). Special items are items which the Board of Managing Directors considers to render the financial indicators less meaningful for evaluating the sustainability of the Schaeffler Group's profitability due to their nature, frequency, and/or size. Net income attributable to shareholders of the parent company before special items in EBIT is also presented in order to facilitate calculating the dividend payout ratio.

In addition to presenting special items, the company also aims to make the evaluation of the company's results of operations as transparent as possible by presenting its revenue figures excluding the impact of currency translation. Revenue figures at constant currency, i.e. excluding the impact of currency translation, are calculated by translating functional currency revenue using the same exchange rate for both the current and the prior year or comparison reporting period.

Special items are categorized as legal cases, restructuring, and other.

2.4 Financial position and finance management

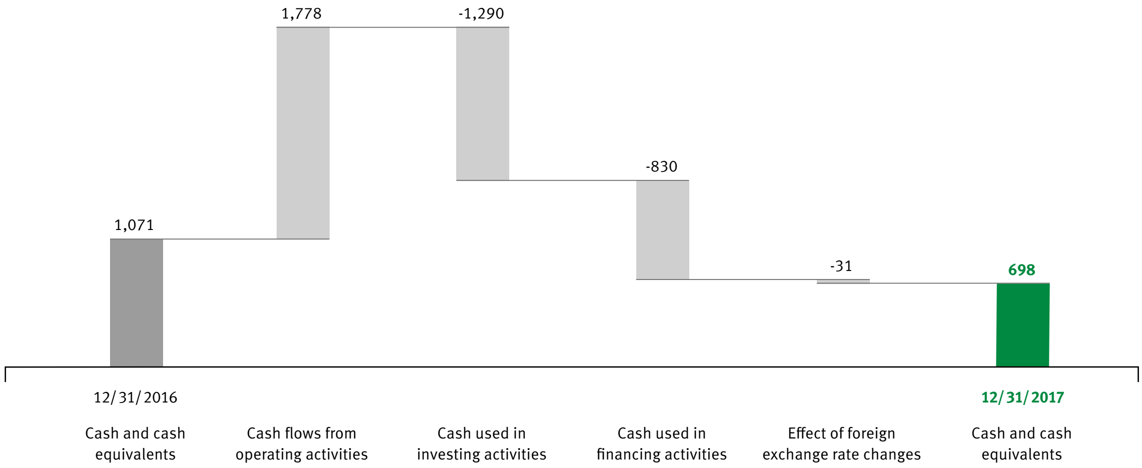
Cash flow and liquidity

The Schaeffler Group generated free cash flow of EUR 488 m (prior year: EUR 735 m) in 2017.

Cash flow No. 052

in € millions	2017	2016	Change in %
Cash flows from operating activities	1,778	1,876	-5.2
Cash used in investing activities	-1,290	-1,141	13.1
Free cash flow	**488**	**735**	**-33.6**
Cash used in financing activities	-830	-466	78.1
Net increase (decrease) in cash and cash equivalents	**-342**	**269**	**-**
Effects of foreign exchange rate changes on cash and cash equivalents	-31	3	-
Cash and cash equivalents as at beginning of period	1,071	799	34.0
Cash and cash equivalents	**698**	**1,071**	**-34.8**

Change in cash and cash equivalents No. 053
in € millions



Cash flow from operating activities for 2017 declined by EUR 98 m to EUR 1,778 m (prior year: EUR 1,876 m), adversely affected by non-persistent cash outflows related to legal cases and restructuring. In addition, the prior year included interest received on a loan receivable by Schaeffler AG from IHO Verwaltungs GmbH. Since the loan was repaid in full in 2016, no such interest was received in 2017. Cash outflows related to expanding working capital amounted to EUR 31 m and were slightly higher than the prior year amount of EUR 22 m. The significant increase in inventories was partially offset by a reduction in trade receivables under a receivable sale program. Sales of receivables resulted in a cash inflow of EUR 150 m. The working capital ratio, defined as working capital as a percentage of revenue, was 19.0% at December 31, 2017 (prior year: 20.3%).

Capital expenditures on property, plant and equipment and intangible assets (capex) amounted to EUR 1,273 m (prior year: EUR 1,146 m) in 2017.

In addition, the acquisition of Compact Dynamics GmbH and autinity systems GmbH resulted in a cash outflow of EUR 47 m, while the disposals of Schaeffler Motorenelemente AG & Co. KG and the fine blanking activities in Switzerland led to a cash inflow of EUR 20 m. Thus, net cash outflow for M&A activities amounted to EUR 27 m in 2017.

These developments resulted in **free cash flow** for 2017 of EUR 488 m (prior year: EUR 735 m).

EUR 830 m in cash was used in **financing activities** (prior year: EUR 466 m) during the year. EUR 328 m of the EUR 330 m in dividends paid during the year represented the dividends paid to Schaeffler AG's shareholders. A total of EUR 587 m in cash was used to redeem a USD bond and to terminate the related cross-currency derivatives in May 2017. EUR 350 m of the Revolving Credit Facility (RCF) was utilized in connection with these transactions, but was repaid in full by year-end. A new EUR 250 m loan agreement obtained to finance long-term logistics projects resulted in a cash inflow to the Schaeffler Group of EUR 90 m (prior year: EUR 0 m).

Cash and cash equivalents decreased by EUR 373 m to EUR 698 m as at December 31, 2017 (prior year: EUR 1,071 m).

At December 31, 2017, cash and cash equivalents consisted primarily of bank balances. EUR 293 m (prior year: EUR 325 m) of this amount related to countries with foreign exchange restrictions and other legal restrictions. In addition, the Schaeffler Group has a Revolving Line of Credit of EUR 1.3 bn (prior year: EUR 1.3 bn), of which EUR 12 m (prior year: EUR 13 m) were utilized at December 31, 2017, primarily in the form of letters of credit.

Capital expenditures

The Schaeffler Group's growth strategy is based, among other things, on investments in new products and technologies as well as in expanding the group's global production network. Investing in intangible assets and property, plant and equipment is key to driving the Schaeffler Group's growth.

The Schaeffler Group increased its capital expenditures on property, plant and equipment and intangible assets (capex) by 11.1% to EUR 1,273 m (prior year: EUR 1,146 m) in 2017. Capital expenditures amounted to 9.1% (prior year: 8.6%) of revenue (capex ratio). By far the largest share of total capital expenditures related to the Europe and Greater China regions.

Capital expenditures by region (capex) No. 054

	in € millions	Change in € millions
Europe	**772** 657	+115
Americas	**172** 209	-37
Greater China	**277** 234	+43
Asia/Pacific	**52** 46	+6
Schaeffler Group	**1,273** 1,146	+127

2017 2016

Regions reflect the regional structure of the Schaeffler Group.

Total additions to intangible assets and property, plant and equipment amounted to EUR 1,287 m (prior year: EUR 1,115 m). Approx. 81% of these additions related to the Automotive division and approx. 19% to the Industrial division. In order to strengthen its competitive position, the Schaeffler Group primarily invested in strategically aligning its logistics activities, expanding capacity, and in equipment and machinery for product start-ups.

In the Europe region, the company decided to make a significant investment by building a state-of-the-art integrated assembly and packaging center known as "Aftermarket Kitting Operation" (AKO) in Saxony-Anhalt near Halle (Saale). The new assembly and packaging center will further optimize the Schaeffler Group's Automotive Aftermarket processes and generate sustained improvements in quality of delivery. Another significant element of the strategic alignment of the group's logistics activities is the central distribution center "EDC Central" (Kitzingen), which forms part of the "European Distribution Center" (EDC) project. Construction in Kitzingen is nearly complete.

More on AKO and EDC on page 20

Apart from these projects, the company invested mainly in equipment and machinery for new product start-ups in the Europe region. For instance, the first assembly lines for electric axles and hybrid modules were set up in Herzogenaurach. The group also continued to expand its production capacity at the Central and Eastern European production plants. For instance, a new plant was opened in Svitavy, Czech Republic, in 2017. The plant focuses on manufacturing thermal management modules for applications in both internal combustion engines and future mobility concepts.

In the **Americas region,** the Schaeffler Group invested especially in expanding capacity and in equipment and machinery for new product start-ups of future electrified drive concepts. The recent addition of new capacity at the Wooster location in the U.S. permits the Schaeffler Group to continue to meet the high demand for components for automatic transmissions, torque converters, and torque converter lockup clutches in addition to producing hybrid modules. In Puebla, Mexico, the Schaeffler Group primarily invested in expanding capacity for continuously variable transmissions (CVT) as well as torque converters, and torque converter lockup clutches. At the Irapuato location in Mexico, investments mainly related to expanding production capacities and new product start-ups.

In the **Greater China region,** the company made targeted investments in expanding capacity and to realize new product start-ups in the Automotive division. Significant investments related to the Engine and Transmission Systems business divisions, mainly for products that form part of the strategy "Mobility for tomorrow". Key investments in the Industrial division were made to expand production and logistics capacities for the standard rolling bearing business to be able to optimally meet the continuing high demand in the high-volume business.

In the **Asia/Pacific region,** the Schaeffler Group invested primarily in the production locations in South Korea, Vietnam, and Thailand. In South Korea, apart from replacements in the standard rolling bearing business of the Industrial division, the company mainly invested in equipment and machinery for new product start-ups in the Automotive division. In addition, a new plant to produce rolling bearings is under construction in Vietnam. It will expand the range of radial insert ball bearings for industrial customers. In Thailand, the Schaeffler Group invested mainly in new product start-ups in the Transmission Systems business division.

Financial debt

The group's net financial debt decreased by EUR 266 m to EUR 2,370 m (prior year: EUR 2,636 m) in 2017.

Net financial debt No. 055

in € millions	12/31/2017	12/31/2016	Change in %
Bonds	1,994	2,719	-26.7
Facilities Agreement	983	982	0.1
Capital investment loan	89	0	-
Other financial debt	2	6	-66.7
Total financial debt	**3,068**	**3,707**	**-17.2**
Cash and cash equivalents	698	1,071	-34.8
Net financial debt	**2,370**	**2,636**	**-10.1**

The net debt to EBITDA ratio, defined as the ratio of net financial debt to earnings before financial result, income taxes, depreciation, amortization, and impairment losses (EBITDA), amounted to 1.0 at December 31, 2017 (prior year: 1.1). The net debt to EBITDA ratio before special items was 1.0 (prior year: 1.1).

The gearing ratio, the ratio of net financial debt to shareholders' equity including non-controlling interests, decreased to 93.0% as at December 31, 2017 (prior year: 132.0%).

On May 24, 2017, the Schaeffler Group fully redeemed the bond with a principal of USD 700 m, a coupon of 4.25%, and an original maturity of May 2021. The redemption was funded using available liquidity and by utilizing EUR 350 m of the Revolving Credit Facility. On November 23, 2017, the Schaeffler Group reduced the amount drawn under the Revolving Credit Facility to a remaining balance of EUR 150 m by repaying EUR 200 m from available liquidity. On December 27, 2017, the Schaeffler Group repaid the remaining balance of EUR 150 m outstanding under the Revolving Credit Facility in full.

On December 15, 2017, Schaeffler AG signed a loan agreement to finance long-term logistics projects. These logistics projects, which form part of the "European Distribution Center" (EDC) project, are the central distribution center "EDC Central" (Kitzingen) and the European assembly and packaging center known as "Aftermarket Kitting Operation (AKO)". The total amount of the loan is EUR 250 m, of which EUR 90 m (prior year: EUR 0 m) were drawn as at December 31, 2017. The loan has a term until 2022 plus certain renewal options.

On April 25, 2017, rating agency Fitch Ratings published its first rating of Schaeffler AG. Fitch assigns a rating of BBB- (investment grade) to Schaeffler AG with a stable outlook. The bonds were assigned an issuance rating of BBB-, the same as the company rating.

Rating agency Standard & Poor's raised the outlook for the company's rating from stable to positive on September 26, 2017. The following summary shows the ratings assigned to the Schaeffler Group by the three rating agencies Fitch, Moody's, and Standard & Poor's as at December 31:

Schaeffler Group ratings No. 056
as at December 31

	2017	2016	2017	2016
		Company		Bonds
Rating agency		Rating/Outlook		Rating
Fitch	BBB-/stable	-	BBB-	-
Moody's	Baa3/stable	Baa3/stable	Baa3	Baa3
Standard & Poor's	BB+/positive	BB+/stable	BB+	BB+

The Schaeffler Group had the following loans outstanding at December 31, 2017:

Schaeffler Group loans No. 057

Tranche	Currency	Principal in millions 12/31/2017	Principal in millions 12/31/2016	Carrying amount in € millions 12/31/2017	Carrying amount in € millions 12/31/2016	Coupon 12/31/2017	Coupon 12/31/2016	Maturity
Term Loan	EUR	1,000	1,000	991	992	Euribor 1) + 1.20%	Euribor 1) + 1.20%	07/18/2021
Revolving Credit Facility 2)	EUR	1,300	1,300	-8	-10	Euribor 1) + 0.80%	Euribor 1) + 0.80%	07/18/2021
Capital investment loan 3)	EUR	250	0	89	0	Euribor 1) + 1.00%	n/a	12/15/2022
Total				**1,072**	**982**			

1) Euribor floor of 0.00%.
2) EUR 12 m (December 31, 2016: EUR 13 m) were drawn down as at December 31, 2017, primarily in the form of letters of credit.
3) EUR 90 m (December 31, 2016: EUR 0 m) were drawn down as at December 31, 2017.

In addition, the Schaeffler Group had further committed lines of credit in the equivalent of approx. EUR 154 m (prior year: approx. EUR 160 m), primarily for the U.S. and China. Approx. EUR 111 m (prior year: approx. EUR 160 m) of these committed facilities were unutilized at December 31, 2017.

The following bonds issued by Schaeffler Finance B.V., Barneveld, Netherlands, were outstanding as at December 31, 2017. All Schaeffler bonds are listed on the Euro MTF market of the Luxembourg Stock Exchange.

Schaeffler Group bonds No. 058

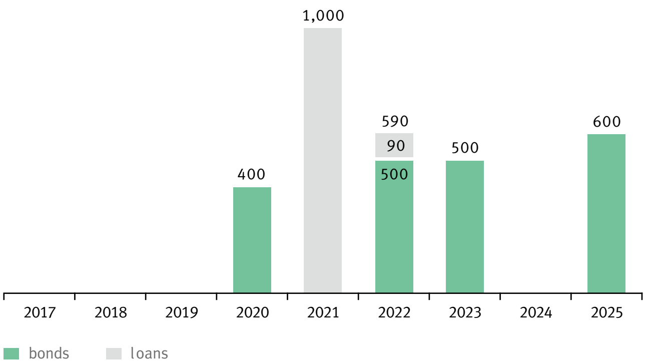
		12/31/2017	12/31/2016	12/31/2017	12/31/2016		
ISIN	Currency	Principal in millions		Carrying amount in € millions		Coupon	Maturity
XS1212469966	EUR	400	400	398	397	2.50%	05/15/2020
US806261AJ29 [1]	USD	0	700	0	658	4.25%	05/15/2021
XS1067864022	EUR	500	500	498	498	3.50%	05/15/2022
US806261AM57	USD	600	600	502	571	4.75%	05/15/2023
XS1212470972	EUR	600	600	596	595	3.25%	05/15/2025
Total				**1,994**	**2,719**		

[1] Redeemed in full on May 24, 2017.

Under its existing debt financing agreements, the Schaeffler Group is subject to certain constraints including a requirement to meet a leverage covenant. Compliance with this financial covenant is monitored continually and reported to the lending banks on a regular basis. As in the prior year, the company has complied with the leverage covenant throughout 2017 as stipulated in the debt agreements.

The company's maturity profile, which consists of the term loan, the capital investment loan, and the bonds issued by Schaeffler Finance B.V., Barneveld, Netherlands, was as follows as at December 31, 2017:

Maturity profile No. 059
Principal outstanding as at December 31, 2017, in € millions



Finance management

The objective of the Schaeffler Group's **finance management** is to ensure that sufficient liquidity is available to the group and to its foreign and domestic subsidiaries at all times. Finance management primarily comprises capital management and liquidity management.

Corporate **capital management** provides the financial resources required by Schaeffler Group entities, ensures the long-term availability of liquidity, and secures the Schaeffler Group's credit standing. Capital management also administers and continually improves the company's existing financial debt consisting of its external group financing arrangements. To this end, the Schaeffler Group has laid the foundations for efficiently obtaining debt and equity funding via the capital markets. The Schaeffler Group's management will continue to focus on the group's ability to place financial instruments with a broad range of investors and to further improve financing terms. To this end, the company particularly intends to maintain the investment grade rating it initially gained in 2016 for the long-term.

External group financing is primarily provided by money and capital market instruments as well as syndicated and bilateral lines of credit from international banks. One such line of credit is a contractually agreed RCF of EUR 1,300 m available to cover any short- to medium-term liquidity needs. In addition, the Schaeffler Group uses receivable sale programs to a limited extent to manage liquidity and improve its working capital. For this purpose, the company has access to an ABCP program (asset-backed commercial paper) of revolving sales of trade receivables with a committed volume of EUR 150 m (prior year: EUR 0 m). Additionally, the Schaeffler Group has the ability to selectively use a further receivable sale program without a fixed committed volume.

The Schaeffler Group has a policy of financing its domestic and foreign subsidiaries from internal sources. In accordance with this policy, subsidiaries' financing needs are met using internal loans to the extent possible and economically justifiable. As a result, subsidiaries are primarily financed by loans provided by Schaeffler AG and one other subsidiary. As part of the company's **liquidity management** measures, liquidity is balanced between group companies on a short- and medium-term basis using primarily cash pools or intercompany loans. In a few cases, Corporate Treasury obtains lines of credit for subsidiaries from local banks for legal, tax, or other reasons. Local financing is primarily used to cover fluctuations in working capital.

Centralized finance management performed by the Corporate Treasury department also ensures a uniform presence in the capital markets and when dealing with rating agencies, eliminates structural differences between the various groups of creditors, and strengthens the group's bargaining position with respect to banks and other market participants. In addition, centralized finance management facilitates the centralized allocation of liquidity as well as groupwide management of financial risk (foreign exchange and interest) on a net basis.

2.5 Net assets and capital structure

The Schaeffler Group had EUR 11,537 m in **total assets** as at December 31, 2017 (prior year: EUR 11,564 m).

Consolidated statement of financial position (abbreviated) No. 060

in € millions	12/31/2017	12/31/2016	Change in %
ASSETS			
Total non-current assets	6,178	5,979	3.3
Total current assets	5,359	5,585	-4.0
Total assets	**11,537**	**11,564**	**-0.2**
SHAREHOLDERS' EQUITY AND LIABILITIES			
Total shareholders' equity	2,548	1,997	27.6
Total non-current liabilities	5,676	6,361	-10.8
Total current liabilities	3,313	3,206	3.3
Total shareholders' equity and liabilities	**11,537**	**11,564**	**-0.2**

Non-current assets rose by EUR 199 m to EUR 6,178 m as at December 31, 2017 (prior year: EUR 5,979 m), primarily due to an increase in property, plant and equipment of EUR 358 m. Additions to intangible assets and property, plant and equipment amounted to EUR 1,287 m and were partially offset by the termination of the cross-currency swaps in connection with the bond redemption as well as negative changes in the fair value of the remaining non-current derivatives. In addition, deferred tax assets dropped by EUR 80 m; reasons for the decline include the bond redemption and a slight increase in the discount rate for pension obligations.

Current assets decreased by EUR 226 m to EUR 5,359 m (prior year: EUR 5,585 m) in 2017. The decrease was largely attributable to the reduction in cash and cash equivalents (see "Cash flow", pp. 61 et seq.). Trade receivables decreased by EUR 26 m in 2017. At December 31, 2017, trade receivables with a carrying amount of EUR 123 m (prior year: EUR 0 m) net of retained default risks had been sold under the ABCP program. The decrease was partially offset by an increase in inventories and favorable changes in the fair value of derivatives used to hedge currency risk.

Shareholders' equity including non-controlling interests rose by EUR 551 m to EUR 2.548 m as at December 31, 2017 (prior year: EUR 1,997 m). Net income of EUR 997 m increased shareholders' equity. The increase was partially offset by EUR 328 m in dividends paid to Schaeffler AG's shareholders. Other comprehensive loss totaled EUR 116 m as at December 31, 2017, and consisted mainly of the impact of translating the net assets of foreign group companies (EUR -247 m), of remeasurements of pensions and similar obligations (EUR 81 m), and of cash flow hedges (EUR 50 m). The equity ratio was 22.1% at December 31, 2017 (December 31, 2016: 17.3%).

Non-current liabilities declined by EUR 685 m to EUR 5,676 m as at December 31, 2017 (prior year: EUR 6,361 m). The decline was largely due to the redemption of the USD bond in May 2017. The decrease in provisions for pensions and similar obligations by EUR 58 m, which resulted primarily from a slight increase in the average discount rate to 2.2% (December 31, 2016: 2.1%), and a decrease in other financial liabilities also contributed to the decline. These decreases were partially offset by a new capital investment loan of EUR 90 m and an increase in provisions, including EUR 39 m related to setting up a shared service center in Europe.

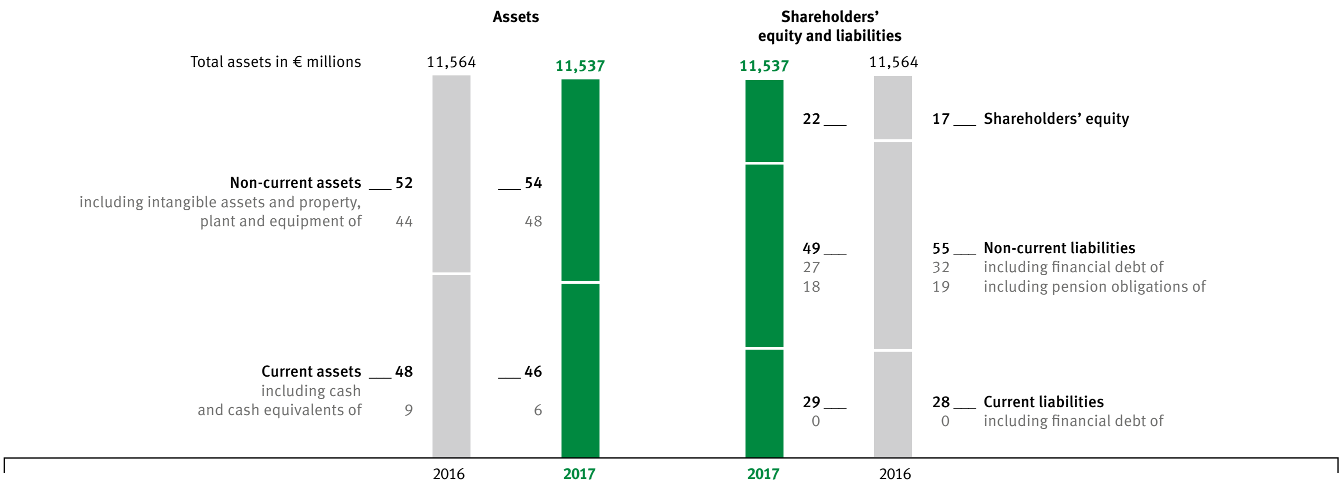
Current liabilities increased by EUR 107 m to EUR 3,313 m (prior year: EUR 3,206 m) as at December 31, 2017. The increase was largely attributable to higher trade payables, partially offset by reductions in other provisions and in restructuring provisions.

The acquisitions and disposals of companies had no significant impact on the Schaeffler Group's net assets and capital structure in the reporting year.

The Schaeffler Group's significant off-balance sheet commitments include obligations under operating rental and lease agreements and contingent liabilities. The Schaeffler Group's

Structure of the consolidated statement of financial position No. 061

in %



obligations under non-cancelable operating rental and lease agreements totaled EUR 133 m at December 31, 2017 (prior year: EUR 123 m); obligations under finance leases were insignificant.

2.6 Overall assessment of the 2017 business year

The Board of Managing Directors considers 2017 a satisfactory year overall. In a highly dynamic market and competitive environment, which is profoundly changing the Automotive as well as the Industrial business, the Schaeffler Group generated **revenue growth** of 5.9% excluding the impact of currency translation in 2017, exceeding its guidance for the year of 4 to 5% (at constant currency). The positive growth trend in the latter half of the year was particularly encouraging. Both of the company's divisions contributed to this encouraging performance. While Automotive division revenue increased by 5.9% excluding the impact of currency translation in 2017, thus once again outperforming global automobile production, the Industrial division grew its revenue by 5.7% excluding the impact of currency translation. In the fourth quarter of 2017, the Industrial division expanded by 9.0% excluding the impact of currency translation. These figures demonstrate that the Industrial division has returned to a long-term growth path.

However, the company's original expectations for the EBIT margin before special items and free cash flow were not met. On June 26, 2017, the Board of Managing Directors of Schaeffler AG decided to reduce its guidance for the EBIT margin before special items from previously 12 to 13% to 11 to 12% due to a substantially lower earnings development in the Automotive division in the second quarter of 2017 compared to the prior year. At the same time, the guidance for free cash flow was reduced from previously approx. EUR 600 m to approx. EUR 500 m. The Schaeffler Group met the amended earnings guidance by generating an **EBIT margin before special items** of 11.3%. While the Automotive division's EBIT margin before special items declined to 12.2% this year, due to lower earnings in the Automotive division compared to the prior year, the Industrial division reported an increase in its EBIT margin before special items to 8.1%. The measures taken under the program "CORE" to improve efficiency and reduce costs are beginning to prove effective for the long-term.

The Schaeffler Group generated **free cash flow** of EUR 488 m, achieving the amended guidance of approx. EUR 500 m. The strategic indicator Schaeffler Value Added before special items **(SVA),** which serves as an indicator of the amount of shareholder value added during the year, amounted to EUR 787 m in 2017 (prior year: EUR 939 m), representing a return on capital employed **(ROCE)** before special items of 19.9% (prior year: 22.3%).

The company continued to execute its strategy "Mobility for tomorrow" in 2017. Its "Agenda 4 plus One" excellence program and its 20 initiatives have laid the foundation to make the Schaeffler Group even more future-proof. Like any transformation program, the "Agenda 4 plus One" will initially result in one-time charges and investments that will impact the company's earnings, including in 2018. The company has decided to accelerate the implementation of the program in 2018. The Schaeffler Group adheres to its Financial Ambitions for 2020. With the strategy "Mobility for tomorrow", the Board of Managing Directors views key fundamentals for long-term growth and adding value to be in place.

2.7 Net assets, financial position, and earnings of Schaeffler AG

Schaeffler AG is a corporation domiciled in Germany with its registered office located at Industriestraße 1-3, 91074 Herzogenaurach. It acts as a management holding company and is responsible for directing the Schaeffler Group and managing its business as well as its financing; it also employs the staff at the Schaeffler Group's corporate head office.

The Board of Managing Directors of Schaeffler AG is responsible for the key management functions of the Schaeffler Group. Schaeffler AG's situation is largely determined by the Schaeffler Group's operating performance.

The following discussion relates to the separate financial statements of Schaeffler AG prepared in accordance with the requirements of the German Commercial Code (HGB) and the German Stock Corporations Act (AktG).

Schaeffler AG earnings

Income statement of Schaeffler AG (abbreviated) No. 062

in € millions	2017	2016	Change in %
Revenue	100	88	13.6
Cost of sales	-94	-84	11.9
Gross profit	**6**	**4**	**50.0**
General and administrative expenses	-60	-71	-15.5
Net other operating income	101	118	-14.4
Income from equity investments	675	600	12.5
Interest result	-171	-289	-40.8
Income taxes	-98	204	-
Earnings after income taxes	**453**	**566**	**-20.0**
Net income for the year	**453**	**566**	**-20.0**
Retained earnings brought forward	0	0	0.0
Retained earnings	**453**	**566**	**-20.0**

As Schaeffler AG is the ultimate parent company of the Schaeffler Group, it generated revenue from managing the group, including from public relations activities, treasury, legal consulting, tax consulting, compliance, human resources, internal audit, quality management, and general management.

In performing its function as management holding company of the Schaeffler Group, Schaeffler AG incurred EUR 60 m (prior year: EUR 71 m) in general and administrative expenses.

As part of its financing function, Schaeffler AG performed most of the Schaeffler Group's hedging activities related to currency risk. Foreign exchange gains and losses related to the group's financing arrangements and hedges of currency risk arising from operations represent a significant proportion of net other operating income.

Income from equity investments consisted entirely of withdrawals from Schaeffler Technologies AG & Co. KG.

Interest expense included interest paid and accrued on the company's institutional loans of EUR 16 m (prior year: EUR 25 m). The proceeds of the bond issuance, which Schaeffler Finance B.V. transferred to Schaeffler AG via intercompany loans, resulted in interest paid and accrued of EUR 84 m (prior year: EUR 169 m). The prepayment penalty of EUR 13 m (prior year: EUR 48 m) payable in connection with the early redemption of a bond was also transferred to Schaeffler AG.

Income tax expense for 2017 amounted to EUR 98 m (prior year: income tax benefit of EUR 204 m) and consisted entirely of current tax expense of EUR 98 m (prior year: EUR 109 m). Schaeffler AG has had deferred tax assets since 2016. It has opted out of recognizing deferred tax assets in accordance with section 274 (1) sentence 2 HGB. Consequently, the company did not have any deferred tax expense or benefit in 2017 (prior year: benefit of EUR 313 m from the reversal of deferred tax liabilities).

Net income for the year amounted to EUR 453 m (prior year: EUR 566 m) in 2017 and equalled retained earnings for 2017.

The Board of Managing Directors and the Supervisory Board will propose a dividend for 2017 of EUR 0.54 (prior year: EUR 0.49) per common share and EUR 0.55 (prior year: EUR 0.50) per common non-voting share to the annual general meeting.

Schaeffler AG financial position and net assets

Balance sheet of Schaeffler AG (abbreviated) No. 063

in € millions	12/31/2017	12/31/2016	Change in %
ASSETS			
Fixed assets	14,302	14,229	0.5
Current assets	8,744	12,239	-28.6
Excess of plan assets over post-employment benefit liability	9	8	12.5
Total assets	**23,055**	**26,476**	**-12.9**
SHAREHOLDERS' EQUITY AND LIABILITIES			
Shareholders' equity	7,059	6,934	1.8
Provisions	314	268	17.2
Liabilities	15,676	19,266	-18.6
Deferred income	6	8	-25.0
Total shareholders' equity and liabilities	**23,055**	**26,476**	**-12.9**

Fixed assets consisted primarily of shares in Schaeffler Technologies AG & Co. KG.

Short-term loans and other financial receivables included in current assets related to Schaeffler AG's cash pooling function and responsibility for the internal group financing of the Schaeffler Group. Other receivables largely consisted of Schaeffler AG's claim to the net income of Schaeffler Technologies AG & Co. KG of EUR 675 m (prior year: EUR 3,600 m) that had not yet been paid out to Schaeffler AG as at December 31, 2017. Schaeffler Technologies AG & Co. KG paid EUR 3.6 bn in respect of prior years' net income to Schaeffler AG in 2017. Schaeffler AG in turn used these funds entirely to pay off existing liabilities due to Schaeffler Technologies AG & Co. KG.

Schaeffler AG managed the Schaeffler Group's cash pool and held bank balances of EUR 189 m (prior year: EUR 635 m) at the end of the reporting period.

On April 26, 2017, Schaeffler AG's annual general meeting passed a resolution to pay a dividend of EUR 328 m to Schaeffler AG's shareholders and to add the remaining retained earnings of EUR 238 m to revenue reserves.

Provisions rose by EUR 46 m to EUR 314 m (prior year: EUR 268 m), primarily due to higher income tax provisions for expected income tax payments and higher provisions for pensions and similar obligations.

Liabilities included primarily short-term loans payable to affiliated companies related to Schaeffler AG's cash pooling function and responsibility for the internal group financing of the Schaeffler Group. Amounts payable to affiliated companies included amounts payable to Schaeffler Finance B.V. of EUR 2,104 m (prior year: EUR 2,772 m) largely relating to the transfer of the proceeds from the bond issuances by Schaeffler Finance B.V. In May 2017, Schaeffler Finance B.V. redeemed one USD bond. The redemption was funded using available liquidity and a portion of the Revolving Credit Facility and was transferred to Schaeffler Finance B.V. by repaying an existing loan.

The signing of a new loan agreement increased the company's bank debt by EUR 93 m to EUR 1,093 m (prior year: EUR 1,000 m).

More on financial debt on pp. 64 et seq.

Closing statement on the dependency report

Closing statement on the report on relations with affiliated companies prepared by the Board of Managing Directors in accordance with section 312 AktG.

Schaeffler AG has been a company dependent on IHO Verwaltungs GmbH, Herzogenaurach, in accordance with section 312 AktG since October 24, 2014. Therefore, the Board of Managing Directors of Schaeffler AG has prepared a report on relations with affiliated companies by the Board of Managing Directors in accordance with section 312 (1) AktG, which contains the following closing statement:

"In the legal transactions and measures listed in the report on relations with affiliated companies, our company has in each legal transaction received appropriate compensation in the circumstances known to us at the time the legal transactions were executed or the measures were executed or not executed, and has not been disadvantaged by the fact that such measures were executed or not executed".

2.8 Other components of the group management report

The following chapters are also part of the combined management report:

- "Corporate governance report including the corporate governance declaration in accordance with section 289f HGB and section 315d HGB" beginning on page 85,
- "Governance structure" beginning on page 97,
- "Remuneration report" beginning on page 101, and
- "Governing bodies of the company" beginning on page 114.

The following references also form part of the combined management report.

Corporate governance report including corporate governance declaration in accordance with section 289f HGB and 315d HGB, including the declaration of conformity pursuant to section 161 AktG at: www.schaeffler.com/ir

Combined separate non-financial report in accordance with section 289b (3), section 315b (3), and section 298 (2) HGB at: www.schaeffler.com/nachhaltigkeit/nfr2017

3. Supplementary report

No material events expected to have a significant impact on the net assets, financial position, or results of operations of the Schaeffler Group occurred after December 31, 2017.

4. Report on opportunities and risks

The Schaeffler Group's risk management system is an integral component of its governance structure and covers both risks and opportunities. The Schaeffler Group is exposed to a large number of potential risks that can adversely affect its business. To be able to appropriately respond to these risks, the company has a risk management system in place to ensure that risks, particularly those to the company's continued existence as a going concern and to its development, are identified on a timely basis.

Risks are defined as possible future developments or events that can lead to adverse deviations from budgeted results, while opportunities are future developments or events that can lead to favorable deviations from budgeted results. When assessing risks, the company considers the impact on its EBIT margin (earnings), free cash flow (financial position), and statement of financial position (net assets), depending on the risk category.

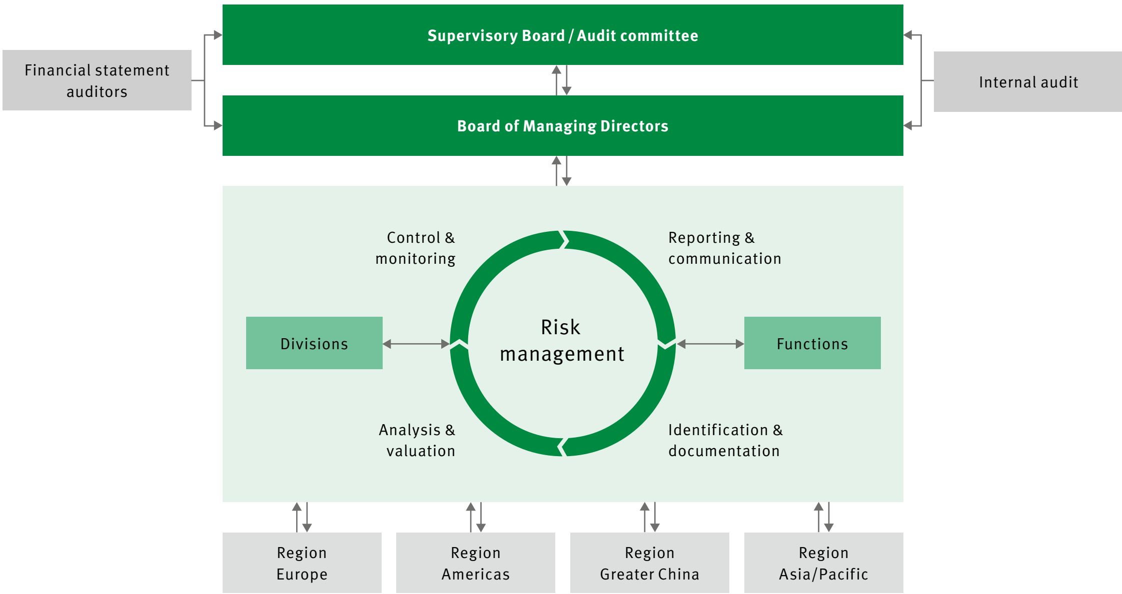
4.1 Risk management system

The Schaeffler Group intentionally takes risks in order to meet its corporate objectives. The objective of the risk management system is to identify these risks on a timely basis and to manage them in accordance with the company's risk appetite. This applies particularly to risks to the company's continued existence as a going concern and to its development, which are responded to with appropriate action. Consciously addressing identified risks and regularly monitoring risk factors is designed to increase risk awareness and ensure a continuous improvement process.

The groupwide risk management system is based on the management-oriented enterprise risk management (ERM) approach, which in turn has its basis in the globally recognized framework of the Committee of Sponsoring Organizations of the Treadway Commission (COSO). As described in this framework, the processes of the risk management system are linked to financial reporting and the internal control system. The Schaeffler Group's risk management process described below is based on the COSO ERM framework.

Responsibility for the risk management system rests with the Board of Managing Directors of Schaeffler AG. The Board of Managing Directors regularly reports to the Schaeffler AG audit committee and ensures that necessary risk management measures are approved. Details of the risk management system are largely set out in a risk management guideline issued by the Board of Managing Directors and published within the Schaeffler Group, making it available to all employees. It contains a description of the process, the allocation of responsibilities, and the structure of the risk management system. The Board of Managing Directors has asked Corporate Risk Management to review and update the risk management system on an ongoing basis and to ensure that existing uniform groupwide standards are implemented and complied with. All instructions from Corporate Risk Management are binding on all individuals responsible for risk.

Structure of risk management system No. 064



The risk management system consists of a multi-phase process spanning various levels and organizational units in order to appropriately reflect the matrix structure of the Schaeffler Group. In a bottom-up process, risks are identified and analyzed at the subsidiary level. Based on this analysis, the next step is a top-down analysis by the appropriate global management of the functions and divisions. They assess the risks identified within the subsidiaries, taking into account all interdependencies within the Schaeffler Group. This approach ensures that all dimensions of the Schaeffler Group's matrix structure are reflected in the risk management system. Risks are identified at all material Schaeffler AG subsidiaries on a semiannual basis. Operating management is responsible for identifying risks. The time period for identifying risks is three years, longer than the outlook horizon.

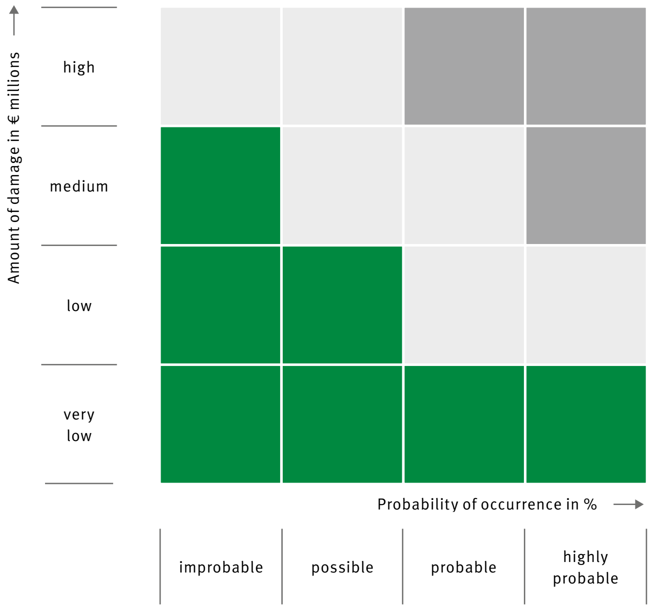
The guideline also defines a groupwide catalog of risk categories to ensure that all risks along the value chain are identified. Identified risks have to be assigned to predefined risk categories. This catalog must be completely reviewed by all those responsible for risk in order to ensure uniform and complete identification of risks. To make risk assessment comparable, suggested risk assessments have been provided for all risk categories.

Subsidiaries included are selected using a defined selection process based on revenue and earnings measures as well as risk factors specific to the business. The performance measures revenue and EBIT are applied depending on the business model of each subsidiary. This selection process ensures that all Schaeffler Group subsidiaries that are relevant from a materiality perspective are included in the risk management system. In 2017, 44 of 152 Schaeffler Group entities were included, representing 94% of revenue and 93% of the Schaeffler Group's EBIT.

The risk management system only deals with risks exceeding a threshold of EUR 5 m on a net basis. Risks are assessed based on their amount of damage and their probability of occurrence. The assessment classifies the amount of damage of each risk in one of four categories: very low, low, medium, and high. Classification is performed based on the amount of damage for one year. The probability of occurrence is assessed using percentages and is classified in the four categories improbable, possible, probable, and highly probable. The combination of estimated amount of damage and probability of occurrence determines the risk class, which is classified as either low, medium, or high based on its impact on net assets, the financial position, and earnings. Risks are assigned to the various risk classes using the risk matrix.

In assessing risks, the Schaeffler Group differentiates between gross exposures and net exposures. Measures already in place can reduce the gross exposure with respect to both amount of damage and probability of occurrence. The net exposure represents the amount of damage and the probability of occurrence after taking into account any risk mitigation measures in place at the reporting date.

Risk matrix No. 065



Impact assessment

Amount of damage in €	
‹ 10 million	very low
› = 10 million - ‹ 25 million	low
› = 25 million - ‹ = 50 million	medium
› 50 million	high

Probability of occurrence in %	
‹ 25%	improbable
25% - ‹ 50%	possible
50% - 75%	probable
› 75%	highly probable

Risk classes
low medium high
Impact on net assets, financial position, and earnings

Identified risks are actively managed to achieve the company's intended level of risk mitigation. Management takes measures to avoid or reduce risks or to provide safeguards against them. Any risks that cannot be mitigated by taking appropriate action are classified as business risks. Risks with a low impact on the Schaeffler Group are managed by operating management. Risks with a medium or high impact, however, are also managed by the Board of Managing Directors of Schaeffler AG. Within its area of responsibility, the Board of Managing Directors decides what measures are required and ensures that they are implemented and kept up to date. The current risk assessment is regularly reported to the Board of Managing Directors and the audit committee.

Corporate Risk Management reports to the Board of Managing Directors on the risk situation semiannually, which ensures that the Board of Managing Directors is continually updated on the current risk situation of the Schaeffler Group and its change over time. All net exposures with a medium or high impact are reported to the Board of Managing Directors. These reports also include an aggregated summary of identified opportunities. Between regular reporting dates, emerging risks are reported using a defined ad hoc process, ensuring timely communication of emerging risks to the Board of Managing Directors.

Internal audit regularly satisfies itself that the risk management system is effective.

In response to the growing complexity of the risk management system and to ensure data is protected, Schaeffler has captured risks in a risk management tool developed specifically for this purpose.

4.2 Internal control system

Paralleling the risk management system, the Schaeffler Group has a system of internal controls over financial reporting (ICS) ensuring the accuracy of the accounting system and the related financial reporting.

Like the risk management system, the Schaeffler Group's ICS is conceptually based on a COSO Framework. The components defined in the Framework are applied to all levels of the group, especially including the compilation of the separate and consolidated financial statements of Schaeffler AG.

The financial statement information reported by Schaeffler AG and its subsidiaries via a uniform groupwide chart of accounts represents the base data for the compilation of the separate and consolidated financial statements. Many subsidiaries receive support from an internal shared service organization in this process. The Schaeffler Group obtains assistance from external specialists in dealing with certain complex issues requiring extensive specialized knowledge (such as the valuation of pension obligations).

Conceptual and process-related requirements and deadlines, as well as analyses and reasonability checks at group and company level, ensure that the separate and consolidated financial statements of Schaeffler AG are compiled, prepared, and issued in accordance with the law, to a high level of quality, and on time.

The following significant features of the system of internal controls over financial reporting have been implemented within the Schaeffler Group as part of this process:

- An accounting manual sets out uniform accounting policies, taking into account new IFRS financial reporting standards required to be applied for the first time.
- Closing instructions issued quarterly provide Schaeffler AG subsidiaries with information on all relevant issues regarding the content as well as the processes and deadlines for compiling the financial statements.
- Tasks and responsibilities regarding the compilation of the separate and consolidated financial statements are clearly defined and assigned.
- The operating units and the various staff members involved in the process stay in close contact on matters concerning accounting, financial statement compilation, and quality assurance with respect to financial statement compilation.

The process for compiling the separate and consolidated financial statements itself is secured by numerous control activities, taking into account materiality. In particular, these include extensive systems-based reasonability checks, controls using reviews (by a second member of staff) performed on a regular basis, and analyses and reasonability checks of the quarterly and annual consolidated financial statements at the corporate level.

As at each year-end, management assesses the appropriateness and effectiveness of the ICS in place. To this end, the Schaeffler Group uses a standardized methodology to identify the group companies and processes relevant to ICS, define the required controls, and document them in accordance with uniform requirements. This is then followed up with a review of the effectiveness of the defined controls that is performed using a risk-based approach, either by the reporting unit itself, by internal audit, or as part of the audit of the consolidated financial statements. This review involves evaluating and assessing risks as well as reporting on them to management with the relevant responsibility at all organizational levels of the companies and the group. Where control weaknesses exist, actions to eliminate these weaknesses have to be defined.

Regardless of the assessed level of the Schaeffler Group's internal control system, the effectiveness of any internal control system is inherently limited. No control system, no matter how effective, can prevent or detect all inaccuracies.

These arrangements as well as their continuous improvement are designed to provide reasonable assurance that the ICS prevents significant misstatements of the financial statements and consolidated financial statements and to ensure quality standards are maintained in compilation, preparation, and issuance.

The Board of Managing Directors considers the system of internal controls over the compilation of the annual and consolidated financial statements of Schaeffler AG to be effective for 2017.

4.3 Risks

The risks set out below could take on a medium or high impact on the Schaeffler Group's earnings, financial position, and net assets within the planning horizon. Risks are divided into strategic, operating, legal, and financial risks and are described in decreasing order of the magnitude of their impact on the Schaeffler Group's net assets, financial position, and earnings. Unless the extent to which one or both divisions are affected by these risks is explicitly described, the discussion of the risks relates to both of the Schaeffler Group's divisions.

Strategic risks

The key operating risks of the Schaeffler Group are described below.

Electric mobility

Electrification of automobiles is progressing, and as a result, the further development of conventional drive trains is coming under pressure. Firstly, improvements to conventional drive trains will become less relevant, and secondly, existing products and applications will be replaced. The Schaeffler Group has established its E-Mobility business division with the intention of further expanding a portfolio of products for this field that is designed to offset any potential future losses in revenue from conventional drive trains. Should the initiatives undertaken not have the desired effect, this could have a medium impact on the Schaeffler Group's financial position and earnings.

Country risks

Changes in the social, political, legal, or economic stability in certain markets could hamper the Schaeffler Group's operations or planned expansion projects. The current heightened uncertainty about the future of the EU, particularly regarding the negotiations for the withdrawal of the United Kingdom, could make customers hesitant to buy and could result in additional adverse currency impacts. Depending on the specific nature of new barriers to trading with the EU market (assuming a hard Brexit), duties payable and increased administrative expenses could have a medium impact on the net assets, financial position, and earnings of the Schaeffler Group. The Schaeffler Group continually monitors the withdrawal process and, in addition, has established a task force to coordinate its local and global activities in this area.

Protecting the environment is a high priority for the Schaeffler Group. Since the Schaeffler Group's production and manufacturing locations are located all over the world, they are subject to a wide variety of environmental standards. The locations meet high environmental standards, a fact highlighted by the large number of locations certified under EMAS. New legislation or changes in the legal environment, both at the national and at the international level, could entail risks jeopardizing trouble-free production that could adversely affect the Schaeffler Group's value added. These risks could have a medium impact on the Schaeffler Group's net assets, financial position, and earnings. Since the group's environmental management system, which has been rolled out worldwide, is constantly being improved and enhanced, occurrence of these risks is considered improbable.

Strategic market and technology risks

The markets for the products offered by the Schaeffler Group are subject to significant technological change, continuously developing technological standards, changing customer preferences, and constantly emerging innovative products. Existing technologies and products may be entirely replaced by newly developed and marketed technologies and newly introduced products. For instance, the Schaeffler Group holds an excellent competitive position with respect to drive trains based on the internal combustion engine. This exceptional position may be jeopardized by the loss of the competitive advantage as well as by expiration of key patents.

Schaeffler currently relies on a high degree of vertical integration and comprehensive production expertise, that facilitate improvements in the production process and ultimately safeguard the company's ability to maintain its margins. The evolution of the company's business from being component-driven toward being more systems-based is ongoing, and this change could reduce the proportion of value added by Schaeffler. The company is taking a variety of measures to address this trend, including, for instance, strategically enhancing its production system to be more modular and building strategic supplier relationships.

The Schaeffler Group's competitiveness depends fundamentally on its ability to keep up with the technological developments discussed above, maintain its technology leadership, and continue to manufacture innovative products cost effectively. Not achieving this objective would represent a medium risk to the Schaeffler Group's financial position and earnings that would last beyond the planning horizon.

The Schaeffler Group operates in a highly competitive and technologically fast-paced environment. The Automotive division's high-margin component business is facing considerable pricing pressure driven by increasing demands for price reductions on the part of customers, purchasing cooperatives, and certain focused and leaner competitors, especially in the emerging markets. The company is currently not fully passing these demands for extensive price reductions on to its own suppliers and cannot absorb them entirely with its existing structure.

Like the Automotive division, the Industrial division is also increasingly faced with competitors from emerging countries that are aggressively exerting pressure on market prices, considerably so in some cases. Customers increasingly prefer standardized products over customer-specific developments, and this trend benefits competitors from emerging countries as well.

Both of these trends require the Schaeffler Group to constantly improve its efficiency and diversify into new lines of business in order to safeguard and further expand its market position. The increasing pricing pressure could have a medium impact on the Schaeffler Group's financial position and earnings.

Digitalization

Digitalization is progressing rapidly and has already completely transformed certain sectors. The Schaeffler Group recognized the issue of digitalization early on, has developed a digitalization strategy – its "Digital Agenda" – and is in the process of implementing it at a rapid pace. The pace of implementation and adaptation represents an important success factor in this regard and, therefore, also a risk. Digitalization is also affecting the work place and will lead to changes in the working environment. As part of the "Digital Agenda", employees with varying skills and qualifications are increasingly confronted with new products, processes, and structures requiring extensive training and also re-qualification. The Schaeffler Group has focused its activities on this issue on a timely basis. However, should the Schaeffler Group nevertheless be unable to overcome these challenges as quickly as necessary, this could have a medium impact on the group's financial position and earnings.

Operating risks

The key operating risks of the Schaeffler Group are listed below.

Procurement risks

The Schaeffler Group's purchasing function ensures optimal supply of goods and services to the company, focusing on quality, cost, and delivery performance. Extensive cooperation with suppliers increases the quality of goods and services supplied. Improving logistics connections to suppliers helps secure supply.

Procurement risks arise mainly from fluctuations in market prices, particularly for purchases of raw materials. Adverse fluctuations in market prices could have a high impact on the Schaeffler Group's financial position and earnings. By negotiating prices and utilizing synergies resulting from numerous cross-regional projects and programs, the Schaeffler Group was able to obtain competitive procurement prices.

Market developments

As the Schaeffler Group is a global supplier in the automotive and industrial sector, demand for Schaeffler products is to a large extent driven by global economic conditions. The demand for products of the Automotive division depends considerably on the overall economic trend. This also applies to the engineering sector and industrial growth markets such as renewable energy. In addition, demand is subject to cyclical fluctuations.

In the Automotive division, demand is not only affected by global economic conditions, but also by other factors such as changes in consumption patterns, fuel prices, interest rate levels, and others. The large number of economic factors affecting global demand for automobiles leads to significant volatility in automobile production, which makes forecasting sales exactly considerably more difficult. Demand for Industrial products is influenced by a wide range of factors due to the large variety of business fields in which the Schaeffler Group operates. Renewable energy depends heavily on government subsidies. Sales of production machinery, on the other hand, depend on new developments and the resulting need for capital expenditures. Aerospace benefits from various new technological developments. Individual drivers can be identified for each sector.

The Schaeffler Group faces numerous competitors in its various business fields. As a result, the company is exposed to the risk of being displaced by existing or new competitors and of its products being replaced by product innovations or by new technological features. The Schaeffler Group mainly competes with other international suppliers, and to some degree also with regional suppliers, on price, quality, reliability of supply, and design, as well as on the ability to offer technological support and service worldwide. Should the company become no longer able to compete on one of these factors, customers may decide to obtain products and services from competitors.

Loss of market share could have a medium impact on the Schaeffler Group's earnings and financial position. As a result of the intense competition in the automotive supply sector, Schaeffler considers the risk of losing market share in the Automotive division higher than in the Industrial division.

Close cooperation with the Schaeffler Group's key customers on product development and strict product quality control measures reduce the likelihood of substitution.

The ability to deliver and delivery performance represent a key competitive factor, which is constantly being enhanced by systematic improvements in production and delivery logistics. The company is building high-performance distribution centers for the Industrial division and the Automotive Aftermarket aimed at improving market supply and delivery performance with fewer logistics locations. Ensuring that contractual delivery dates are met could have a high impact on the Schaeffler Group's financial position and earnings.

Production risk

As the Schaeffler Group's production is very capital-intensive, a large proportion of its costs are fixed. At several locations, ensuring the best-possible utilization of capacity requires having only one of a given type of machine available. The failure of one of these bottleneck machines can lead to a bottleneck in supply to internal and external customers. The period between failure of the bottleneck machine and when alternative means of production are set up is key. Alternative means of production can either be set up by a Schaeffler Group plant with comparable production lines or provided by an alternative supplier. Establishing safety stock can also help reduce losses. To minimize the probability of occurrence, the risk is mitigated by extensive maintenance. However, failure of a bottleneck machine represents a medium risk to the Schaeffler Group's financial position and earnings.

Warranty and liability risks

One significant factor in customers' decision to purchase the products offered by the Schaeffler Group is their high quality. To secure this level of quality for the long-term, the Schaeffler Group employs a certified quality management system, supported by additional quality improvement processes. However, there is a risk that poor quality products end up getting delivered, causing product liability risk. The use of defective products can lead to damage, unplanned repairs, or recalls on the part of the customer which can result in liability claims or reputational damage. Furthermore, deteriorating product quality can result in increased warranty and liability risk vis-à-vis the Schaeffler Group's customers. The Schaeffler Group responds to such risks by adopting strict quality control measures and continually improving its production processes in order to minimize the probability of warranty and liability risks materializing. Individual risks becoming reality could have a medium impact on the Schaeffler Group's financial position and earnings. All product liability risks are insured. The extent of actual reimbursements that can be claimed from insurers can only be assessed on a case-by-case basis.

Product piracy risks

The Schaeffler product brands INA, LuK, and FAG are associated with a high standard of quality, making them increasingly susceptible to product piracy. Counterfeit products are normally sold at significantly reduced prices, which can lead to increased pressure on the Schaeffler Group's prices. Combating product piracy is a high priority for the Schaeffler Group. The Schaeffler Group protects intellectual property not only using global patents and industrial property rights but also by actively combatting counterfeit products, which damage its image as well as its revenue. Based on the large number of counterfeit products seized, the Schaeffler Group estimates the impact of this issue on its earnings and financial position to be medium.

Legal risks

The Schaeffler Group's operations give rise to legal risks, for instance those resulting from non-compliance with relevant regulations. Legal risks are reflected in provisions recognized in accordance with financial reporting standards.

Compliance risks

As a company with operations worldwide, Schaeffler has to comply with varying laws and regulations around the globe. It is possible that violations of existing law occur despite careful observance of such legal requirements. Identified instances of non-compliance are immediately addressed with appropriate action. The consequences of these instances of non-compliance could have a medium impact on the Schaeffler Group's net assets, financial position, and earnings as well as on its reputation. The Schaeffler Group cooperates with the authorities with respect to any current and future investigations of possible instances of non-compliance and responds appropriately to weaknesses identified.

More on the company's compliance management system on pp. 98 et seq.

The company uses a material compliance management system to help it meet its commitment to using only components and raw materials that comply with the applicable laws and regulations. However, there is a risk that legal requirements and changes therein are not identified in time and that products are distributed in the market in violation of the law. This could have a medium impact on the Schaeffler Group's financial position and earnings.

Litigation

Certain Schaeffler Group companies are involved in various legal cases or could become involved in additional litigation. These could lead to claims for damages or to other claims. In addition, the company's or their opponents' legal expenses could be significant. These legal cases are mainly related to the Schaeffler Group's sales and purchases of goods and services. Existing legal cases could have a medium impact on the Schaeffler Group's financial position and earnings.

Antitrust proceedings

Current and future investigations and proceedings regarding violations of antitrust law could have an adverse impact on the financial position and earnings of the Schaeffler Group as well as on its reputation. Possible payment obligations in connection with these investigations and proceedings may result in unplanned cash outflows. The Schaeffler Group cooperates with the investigating authorities in current and future investigations as a matter of principle. The imposition of penalties cannot be ruled out. In Spain and Korea, the company has appealed judgments imposing penalties.

In addition, claims for damages have been filed against Schaeffler Group companies as a result of known antitrust proceedings. These claims could have a medium impact on the Schaeffler Group's financial position and earnings. The Schaeffler Group has recognized appropriate provisions for possible charges to earnings.

Financial risks

Financial risks include tax risks and pension risks, as well as the impact of changes in foreign exchange rates and liquidity risks.

Tax risks

The Schaeffler Group is subject to tax audits worldwide. Tax authorities' interpretation of the tax law or of relevant facts made in current or future tax audits may differ from that of the Schaeffler Group. This may lead to adjustments to tax bases and increases in the tax liability. An additional tax payment as a result of an adjustment to the tax base could have a high impact on the Schaeffler Group's financial position.

Pension risks

The Schaeffler Group has extensive pension obligations, particularly in Germany, the U.S., and the United Kingdom. The obligations in the Anglo-Saxon countries are financed by pension funds. Pension obligations are measured using actuarial valuations based on assumptions regarding possible future events, such as the discount rate, increases in wages, salaries, and pensions, and statistical life expectancy. Plan assets may be invested in various asset classes, such as equity instruments, fixed-income securities, or real estate, which are subject to fluctuations in value. A change in the parameters listed above could have a medium impact on the Schaeffler Group's net assets, particularly in Germany and the United Kingdom.

Currency risks

The Schaeffler Group is exposed to a wide range of currency risks due to its international reach. The largest such currency risks from operations result from fluctuations in the U.S. dollar and Chinese renminbi exchange rates.

Currency risks from financing activities arise mainly from the impact of changes in the U.S. dollar exchange rate on the portion of the bond issued in U.S. dollars that is not hedged.

Currency risks from operations and from financing activities are continually monitored and reported. Currency risk is managed at the corporate level. Currency risks are aggregated across the group and hedged using hedging instruments. Hedging instruments used include forward exchange contracts and cross-currency swaps. Currency risks, market values of foreign currency derivatives, and developments in foreign exchange markets are continuously monitored and managed as part of the risk management system.

To the extent competitors from other currency areas can offer lower prices due to movements in exchange rates, changes in foreign exchange rates can adversely affect the Schaeffler Group's competitive position. The Schaeffler Group's manufacturing locations are spread around the world, enabling the group to reduce the impact of changes in exchange rates on its competitive position. However, exchange rate trends could have a medium impact on the Schaeffler Group's earnings and financial position.

Liquidity risks

The risk that the Schaeffler Group will not be able to meet its payment obligations as they come due is referred to as liquidity risk. The Schaeffler Group differentiates between short-, medium- and long-term liquidity risks.

Liquidity risks can arise if financing needs cannot be met by existing equity or debt financing arrangements. The Schaeffler Group's financing requirements were met throughout 2017 by existing financing instruments and by the refinancing arrangements completed.

To avoid unforeseen short- or medium-term liquidity needs to the extent possible, short- and medium-term liquidity risk is monitored and managed using a rolling liquidity budget with a forecasting period of up to twelve months. Short-term fluctuations in cash flow are monitored daily and can be offset using lines of credit. To this end, the Schaeffler Group has an RCF of EUR 1.3 bn and other bilateral lines of credit held by various subsidiaries.

The Schaeffler Group's loan and bond agreements, which are generally long-term, contain certain constraints including a requirement to meet certain financial covenants. The creditors are entitled to call the debt prior to maturity under certain circumstances, including if covenants are not met, which would result in the debt becoming due immediately. Compliance with financial covenants is monitored on an ongoing basis and regularly reported to the lending banks. To date, the company has complied with the financial covenants as stipulated in the debt agreements. The Schaeffler Group also expects to comply with these covenants in the future.

Any non-compliance with the covenants contained in the debt agreements as well as any liquidity requirements exceeding those that can be covered by the existing lines of credit could have a medium impact on the Schaeffler Group's net assets, financial position, and results of operations. It is considered improbable that these situations will actually occur.

Risk assessment No. 066

	Amount of damage in €	Probability of occurrence in %	Risk class	Change from prior year
Strategic risks				
• Electric mobility	high	possible	medium	↗
• Country risks	high	possible	medium	new
• Strategic market risks	medium	probable	medium	↗
• Technology risks	medium	possible	medium	new
• Digitalization	medium	possible	medium	→
Operating risks				
• Procurement risks	medium	highly probable	high	new
• Delivery performance	medium	highly probable	high	new
• Market development	high	improbable	medium	→
• Loss of market share	high	improbable	medium	→
• Production risk	high	improbable	medium	→
• Warranty and liability risks	high	improbable	medium	→
• Product piracy risks	low	probable	medium	→
Legal risks				
• Compliance risks	high	improbable	medium	→
• Litigation	medium	possible	medium	→
• Antitrust proceedings	low	probable	medium	→
Financial risks				
• Tax risks	high	probable	high	↘
• Pension risks	high	possible	medium	→
• Currency risks	high	possible	medium	↗
• Liquidity risk	high	improbable	medium	→

↗ increased → unchanged ↘ reduced

4.4 Opportunities

The responsibility for identifying and utilizing opportunities lies with operating management. Their objective is to identify these opportunities on a timely basis and to take appropriate action to utilize them. Opportunities identified are discussed with the Board of Managing Directors as part of the Strategy Dialog and strategies are then derived based on these discussions. During this process, the relevant opportunities for growth are prioritized, specific targets are derived, and actions and resources required to achieve operating targets for the future direction of the Schaeffler Group are determined.

An aggregated overview of the opportunities identified in the Strategy Dialog is included in the reports regularly provided to the Board of Managing Directors and the Supervisory Board of Schaeffler AG. Opportunities are documented in the risk management tool.

The Schaeffler Group's most significant opportunities lie in strategic trends and in changes to the legal environment that may lead to increased demand for Schaeffler products.

Strategic opportunities

The Schaeffler Group with its range of products and services and its global presence is in a good position to participate in the expected megatrends of the future.

The Schaeffler Group's strategic and operational opportunities specifically result from the following factors:

Globalization

Shifting activities to local markets could enable the Schaeffler Group to tap opportunities for reducing cost and to improve proximity to the customer. The company also identifies and realizes additional potential worldwide. This also bolsters the company's competitive position vis-à-vis competitors from low-wage countries.

Potential in emerging countries

Increasing affluence in the emerging countries results in the development of a growing middle class there. The newly emerging group of buyers can lead to increasing demand for automobiles and industrial goods. The Schaeffler Group is a supplier to all well-known manufacturers and suppliers, which provides a general opportunity to participate in increased demand.

The company has invested in significant additional resources in order to increase its local presence in the emerging countries and plans to continue to pursue this growth strategy.

Electric mobility

Increasing demands on automobile manufacturers to reduce fuel consumption and emissions as well as increased safety requirements provide the Schaeffler Group with an opportunity to increase its revenue per vehicle. A related issue is the increasing complexity of systems, which provides the opportunity to add new functionalities to its product range. Reducing emissions by improving the technology of conventional internal combustion engines offers further opportunities to the Schaeffler Group, as do the plug-in hybrids currently being developed, which consist of a highly efficient internal combustion engine and an electric drive. Hybridized vehicles require expertise in the classic field of engine/transmission as well as in newer product fields such as hybrid modules and electric axles. The E-Mobility business division coordinates its wide range of activities relating to alternative types of drives, allowing the Schaeffler Group to benefit from comprehensive systems know-how.

Urban mobility

The increasing number of people living in megacities is making public transportation within cities, such as metros, rapid transit systems, and streetcars, as well as between cities, e.g. by high-speed train, more and more attractive and important. Especially rail vehicles represent an extremely interesting growing market for the Schaeffler Group. Reliable and innovative rolling bearing solutions for applications ranging from undercarriage to the drive train are key to modern rail vehicles – and also promise growth for mechatronic products in the age of digitalization in mobility. In addition, the high stresses and resulting wear and tear as well as safety regulations make this market a market of the future with respect not only to original equipment but also to the Aftermarket business.

Global mobility

Increasing globalization is inherently associated with an increase in the volume of air traffic. As a result, growth in the aerospace sector is forecasted to be steady. In this sector, issues such as reducing CO_2, reducing weight, and optimizing fuel consumption are increasingly gaining in importance. The Schaeffler Group is already actively participating in these developments.

Urbanization

People are increasingly moving to larger cities and metropolises, whether for their job, cultural events, or consumer spending. As a result, energy and water consumption is expected to continue to rise in these central locations in the future. In addition, the increasing electrification of automobiles will drive a growing need for energy. The rising demand for energy and the beginning transition to renewable energy both lead to an inevitable demand for energy from renewable sources. Especially in the wind business, the Schaeffler Group is already successfully operating in the market. Continually expanding the existing expertise in these business fields offers additional future opportunities for growth.

Trends related to automobile manufacturers

In the last few years, automobile manufacturers have increasingly created global platforms aimed at standardizing components and vehicle systems in order to save costs by increasing efficiency. Consequently, automobile manufacturers are looking for suppliers that can supply standardized components worldwide. In return, they reduce the number of suppliers and concentrate on a few global suppliers. Suppliers such as the Schaeffler Group benefit from this trend due to their global presence and their ability to supply products to the same technological and quality standards worldwide.

Operational opportunities

Development of vehicle population

The absolute vehicle population drives growth in the Automotive Aftermarket. Growth depends on various factors, such as demand (determined by kilometers driven and the composition of the vehicle population), services offered, as well as products offered. Besides the vehicle population, increasing content per vehicle provides additional opportunities.

Industry 4.0

The internet of things finding its way into factories has started a fourth industrial revolution. Future scenarios in practice often referred to under the heading "Industry 4.0" are characterized by highly individualized products in very flexible manufacturing conditions. In future, companies will network their machinery, warehousing systems and equipment around the world. The accompanying global digitalization is progressing at an enormous speed everywhere. Highly interconnected machines and plants can facilitate progress in manufacturing, including by employing this type of machine in the company's own production. Along with production technology, Industry 4.0 also comprises digitally connecting components and machines. The Schaeffler Group's products can be found wherever something is turning and primary data can be obtained. This allows bearings to be monitored continually and their operation to be improved based on the results.

Digitalization

The topic of "Digitalization" connects both divisions. It will significantly transform the entire economy and its traditional processes. The convergence of the real world and the digital world will produce new business models and a lasting increase in value creation. The Schaeffler Group's "Digital Agenda" comprises four key elements: Products & Services, Machines & Processes, Analyses & Simulation, and User Experience & Customer Value. With its "Digital Agenda", the Schaeffler Group is concentrating both on internal processes and on products and solutions for its customers. It is not only internally that the company aims to increase the efficiency of its processes, use available data more intensively, and more effectively link production locations, machines, and buildings. It also aims to expand on its customers' existing business models and help them develop new ones.

Legal opportunities

The Schaeffler Group's legal opportunities specifically result from the following factors:

Emission standards

Constantly tightening exhaust emission standards (Euronorm, CAFE standard) are putting increased pressure on automobile manufacturers to use energy efficient solutions in their vehicle drives, consisting of the internal combustion engine and the transmission. The Schaeffler Group as their development partner can support the search for solutions with its innovative strength, creating innovations that manufacturers can turn into a competitive edge.

Average fleet consumption

Besides emission standards, government pressure on automobile manufacturers is also increasing with respect to the fuel consumption of the vehicles they produce: Governments are prescribing certain limits for fleet consumption, to be achieved via their model mix. This also helps drive developments needed to reduce emissions, benefiting primarily technology-oriented suppliers like the Schaeffler Group, since the requirements established by the market and the law make a strong development partnership between the automobile manufacturer and its suppliers a necessity.

Financial opportunities

The Schaeffler Group's financial opportunities specifically result from the following factors:

Rating

Rating agencies Standard & Poor's and Moody's have been assigning a company rating to the Schaeffler Group and issuance ratings to its outstanding bonds since January 2012. In addition, Fitch became the third rating agency to assign such ratings, in April 2017. An improvement in the ratings published by the three rating agencies can provide the Schaeffler Group with more favorable financing conditions and open up new opportunities to obtain financing. Moody's maintained Schaeffler AG's company rating at Baa3 (investment grade) with a stable outlook throughout 2017. Standard & Poor's kept its rating unchanged at BB+ (sub-investment grade), but upgraded the outlook from stable to positive on September 26, 2017. Fitch published its first rating of Schaeffler AG on April 25, 2017, and has kept its rating for the company constant at BBB- (investment grade) with a stable outlook since then. At December 31, 2017, all three rating agencies' issuance ratings for the Schaeffler Group's outstanding bonds was equal to the corresponding company rating, i.e. Baa3 (Moody's), BB+ (Standard & Poor's), and BBB- (Fitch).

Financial markets

Favorable trends in interest and foreign exchange rates can positively impact the Schaeffler Group's financial result and earnings. The company constantly monitors the financial markets in order to detect any possible impact on the Schaeffler Group on a timely basis and identify any potential need for action.

4.5 Overall assessment of Schaeffler Group opportunities and risks

The Board of Managing Directors estimates that the Schaeffler Group's situation with respect to risks has deteriorated compared to the prior year. This change is due to new risks being included and a change in the assessed impact of certain medium risks.

The outlook issued by the Schaeffler Group is not in jeopardy, including from the existing risks. In addition to the specific risks described in the group management report, unexpected developments significantly damaging or harming the company's production process, customer relationship, or reputation can occur at any time.

The overall assessment of the significant opportunities and risks does not indicate any risks which, either individually or in combination with other risks, jeopardize the company's continued existence as a going concern.

5. Report on expected developments

5.1 Expected economic and sales market trends

The International Monetary Fund (IMF) anticipates that the global economy will continue to gather momentum in 2018 (January 2018). The IMF expects global gross domestic product to grow by 3.9%. Oxford Economics anticipates the same growth rate (January 2018). In light of these forecasts, the Schaeffler Group expects global economic growth of just under 4% in 2018.

The expected development of the global economy is subject to a number of uncertainties. Should the international equities markets experience persistently falling prices, this would adversely affect the real economy. In addition, if the global financing environment tightens up more than currently expected, for instance in the form of an unforeseen increase in interest rates, this could especially hamper the development of the emerging countries and could also destabilize the global financial markets. China remains susceptible to an unexpected setback in growth, especially considering the debt problem in that country. Finally, global economic growth might be impaired by increasing trade protectionism and an escalation of existing geopolitical conflicts.

The negotiations between the United Kingdom and the EU are currently focusing on future trade relations between the two economies. Based on their current status, it appears unlikely that the two parties will fail to reach an agreement – which would result in the United Kingdom withdrawing from the EU unsystematically and trade regulations reverting to the rules of the World Trade Organization. Additionally, it is currently expected that there will be a transition period until the end of 2020, during which the United Kingdom will remain a member of the EU single market and the European Union Customs Union. However, if it becomes clear early-on that the result of the negotiations will be adverse to the United Kingdom, this could lead to (further) economic distortions prior to the withdrawal – primarily in the United Kingdom itself, but, due to existing trade ties, in other EU countries as well.

Taking into account the forecasts of research institute IHS (February 2018), the Schaeffler Group expects automobile production, measured in terms of the number of passenger cars and light commercial vehicles produced, to increase by about 2% in 2018. The Schaeffler Group anticipates growth of about 3.5% for the Europe region and a growth rate of about 1.5% for the Americas region. The Greater China region is expected to experience a growth rate of about 3%, while automobile production in the Asia/Pacific region is forecasted to decline by about 1%.

In light of the IHS forecasts (February 2018), the Schaeffler Group expects the global vehicle population, measured in terms of the number of passenger cars and light commercial vehicles, to decline slightly in 2018 compared to 2017, with the average vehicle age remaining nearly unchanged.

The Schaeffler Group anticipates industrial production to grow at a similar rate in 2018 as it did in 2017 (Oxford Economics, December 2017).

5.2 Schaeffler Group outlook

Outlook 2018 – group No. 067

Schaeffler Group	**Actual 2017**	**Outlook 2018**
Revenue growth [1]	5.9%	5 to 6%
EBIT margin before special items [2]	11.3%	10.5 to 11.5%
Free cash flow [3]	EUR 515 m [4]	~ EUR 450 m

[1] Compared to prior year; excluding the impact of currency translation.
[2] Please refer to pp. 60 et seq. for the definition of special items.
[3] Before cash in- and outflows for M&A activities.
[4] Adjusted comparative figure before cash in- and outflows for M&A activities.

The Schaeffler Group expects its revenue to grow by 5 to 6% excluding the impact of currency translation in 2018.

In addition, the company expects to generate an EBIT margin before special items of 10.5 to 11.5% in 2018.

The Schaeffler Group also anticipates approx. EUR 450 m in free cash flow before cash in- and outflows for M&A activities for 2018. In a change from the guidance provided for this indicator in the prior year, beginning in 2018, the Schaeffler Group will report free cash flow before cash in- and outflows for M&A activities. The adjusted comparative figure, free cash flow before cash in- and outflows for M&A activities for 2017, amounts to EUR 515 m.

Outlook 2018 – divisions No. 068

Automotive OEM	**Actual 2017**	**Outlook 2018**
Revenue growth [1]	6.5%	6 to 7%
EBIT margin before special items [2]	10.8% [3]	9.5 to 10.5%
Automotive Aftermarket	**Actual 2017**	**Outlook 2018**
Revenue growth [1]	3.2%	3 to 4%
EBIT margin before special items [2]	19.0% [3]	16.5 to 17.5%
Industrial	**Actual 2017**	**Outlook 2018**
Revenue growth [1]	5.7%	3 to 4%
EBIT margin before special items [2]	8.0% [3]	9 to 10%

[1] Compared to prior year; excluding the impact of currency translation.
[2] Please refer to pp. 60 et seq. for the definition of special items.
[3] Comparative figure based on 2018 segment structure.

The Schaeffler Group anticipates that its Automotive OEM division will continue to outperform the global automobile production of passenger cars and light commercial vehicles, expected to expand by about 2%, in 2018. Based on this expected outperformance, the Schaeffler Group expects its Automotive OEM division to generate revenue growth excluding the impact of currency translation of 6 to 7% (2017: 6.5%). This expectation is supported by orders won in the 2017 reporting period, known as lifetime sales, of EUR 11.5 bn, representing a “book-to-bill ratio”, the ratio of order intake to revenue for the year, of 1.3x. The company also expects an EBIT margin before special items of between 9.5 and 10.5% for 2018 (2017: 10.8%) for the Automotive OEM division.

Given the stable growth in the global vehicle population and a nearly unchanged average vehicle age, the Aftermarket business will likely continue to grow as well. Based on its own observation of the market, the group expects the Automotive Aftermarket division to generate revenue growth - excluding the impact of currency translation – of 3 to 4% (2017: 3.2%) and an EBIT margin before special items of 16.5 to 17.5% in 2018 (2017: 19.0%).

In the Industrial division, an encouraging trend in order intake combined with the economic environment in certain sectors suggests a slight increase in revenue in 2018. Based on these considerations, the company expects its Industrial division to generate 3 to 4% (2017: 5.7%) in revenue growth in 2018, excluding the impact of currency translation. In addition, the Industrial division anticipates generating an EBIT margin before special items of between 9 and 10% in 2018 (2017: 8.0%).

Herzogenaurach, February 19, 2018

The Board of Managing Directors

Corporate Governance

* Included in the group management report.

1. Corporate governance report including the corporate governance declaration in accordance with section 289f HGB and section 315d HGB

Corporate governance stands for responsible management focused on adding long-term value. Efficient cooperation between the Board of Managing Directors and the Supervisory Board as well as openness and transparency in corporate and financial communications are key aspects of the Schaeffler Group's corporate governance that strengthen the confidence of stakeholders in the company's management and supervision.

The following is a report by the Board of Managing Directors and the Supervisory Board on the corporate governance of Schaeffler AG in accordance with item 3.10 of the German Corporate Governance Code. The corporate governance report also comprises the corporate governance declaration in accordance with section 289f HGB and 315d HGB, including the declaration of conformity pursuant to section 161 AktG, which is a separate component of the group management report. However, according to section 317 (2) sentence 6 HGB, this information is not subject to audit; as a result, the audit is only required to determine whether these disclosures were provided.

Corporate governance report including corporate governance declaration in accordance with section 289f HGB and 315d HGB, including the declaration of conformity pursuant to section 161 AktG at: www.schaeffler.com/ir

1.1 Declaration of conformity pursuant to section 161 AktG

In December 2017, the Board of Managing Directors and the Supervisory Board issued the following declaration of conformity pursuant to section 161 AktG:

Declaration by the Board of Managing Directors and the Supervisory Board of Schaeffler AG pursuant to § 161 of the German Stock Corporation Act (AktG) on the German Corporate Governance Code

Since the release of its last declaration of conformity in December 2016, Schaeffler AG complies with the recommendations of the "Governmental Commission German Corporate Governance Code" as amended on May 5, 2015 and on February 7, 2017, respectively ("Code") with the exception described below and will also comply with the recommendations in the future with the exception described below:

> The Code recommends in item 5.4.1 para. 2, that the Supervisory Board shall specify concrete objectives regarding its composition and also set an age limit for the members of the Supervisory Board. The Supervisory Board of Schaeffler AG will not set such age limit because it is of the opinion that this criterion is not informative with respect to the suitability of a person to perform as a member of the Supervisory Board.

Herzogenaurach, December 2017

For the Supervisory Board	For the Board of Managing Directors
Georg F. W. Schaeffler Chairman of the Supervisory Board	Klaus Rosenfeld Chief Executive Officer

1.2 Corporate governance principles

The Schaeffler Group's manner of conducting business is based on integrity, fairness, and mutual respect. Transparency, trust, and teamwork are the three key success factors for achieving this. Transparency generates trust, and trust is the foundation of good teamwork. The Schaeffler Group **Code of Conduct** provides guidance in this area. The principles set out in the Schaeffler Group Code of Conduct apply equally to everyone – the Board of Managing Directors, management, and all employees.

Compliance is part of the company's culture. It is centered around customer relationships and acting with integrity.

Similarly, thinking long-term and acting responsibly have always characterized the Schaeffler Group's corporate culture as a listed family business. It is very important to the Schaeffler Group to combine economic success with acting responsibly toward the environment, people, and society. The corporate values, "Sustainable", "Innovative", "Excellent", and "Passionate", form the basis for sustainable profitable growth for the benefit and in the interest of the group's customers and business partners, employees and managers, as well as its shareholders and family shareholders. Based on this, the Board of Managing Directors has issued and published a **sustainability strategy** covering the following fields of action: (1) Sustainable management, (2) Customers and products, (3) Environment and energy, (4) Employees and society.

More on the company's corporate governance principles at: www.schaeffler.com/sustainability

1.3 Mode of operation of the Board of Managing Directors and the Supervisory Board and membership and mode of operation of their committees

Schaeffler AG's governance structure follows the two-tier model set out in the German Stock Corporations Act. The Board of Managing Directors has direct responsibility for managing the company. The members of the Board of Managing Directors are jointly responsible for managing the company. The Chief Executive Officer coordinates the activities of the members of the Board of Managing Directors. The Supervisory Board appoints, supervises, and advises the Board of Managing Directors and is involved in decisions that are fundamental to the company. The Chairman of the Supervisory Board coordinates the work of the Supervisory Board.

Board of Managing Directors

The Schaeffler Group is managed by the Board of Managing Directors of Schaeffler AG. Its actions and decisions are guided by the company's best interest and, therefore, take into account the interests of shareholders, employees, and other stakeholders of the company in order to add long-term value. The members of the Board of Managing Directors run the business in accordance with the law, the company's articles of association, and the internal rules of procedure, taking into account the obligation to obtain approval set out in the Supervisory Board's internal rules of procedure. The Board of Managing Directors is directly responsible for managing the company, sets objectives and the company's strategic direction, consults on them with the Supervisory Board, manages the implementation of the company's strategy, and regularly discusses the status of its implementation with the Supervisory Board. It is also responsible for the annual budget and long-range plan and for preparing the company's quarterly and semiannual financial reports, the separate financial statements of Schaeffler AG, the consolidated financial statements, and the combined management report of the company and the group.

The Board of Managing Directors also ensures that legal requirements and internal guidelines are complied with and promotes such compliance by group companies and their employees. It puts in place appropriate measures that are tailored to the company's risk situation (compliance management system) and discloses their main features. A whistleblowing system gives employees the opportunity, including appropriate protection, to report violations of the law within the company; this opportunity is also provided to third parties.

More on compliance on pp. 97 et seq.

The internal rules of procedure of the Board of Managing Directors set out the activities of the Board of Managing Directors, the issues that are the responsibility of the Board of Managing Directors, the majorities required to pass resolutions, and the areas of responsibility of the various members of the Board of Managing Directors. Based on the Schaeffler Group's organizational structure, the Board of Managing Directors consists of the Group CEO and the CEOs of the divisions and corporate functions. Under the internal rules of procedure, specific management responsibilities are assigned to each member of the Board of Managing Directors. Their responsibility for jointly managing the company remains unaffected. Each member of the Board of Managing Directors is directly responsible for his or her assigned area of responsibility, taking into account the joint responsibility of the Board of Managing Directors.

The Schaeffler Group is managed using a three-dimensional matrix consisting of the divisions, the functions, and the regions. The Regional CEOs report directly to the CEO. Together, the Board of Managing Directors and the Regional CEOs represent the Schaeffler Group's Executive Board.

Membership of the Board of Managing Directors

Under the "Act on Equal Access for Men and Women to Leadership Positions in the Private and Public Sectors", Schaeffler AG's Supervisory Board, being the body responsible for making appointments to the Board of Managing Directors, is required to set a target for the proportion of women on the Board of Managing Directors. At its meeting on May 10, 2017, the Supervisory Board established that the Board of Managing Directors of Schaeffler AG has to have at least one female member.
The deadline for meeting this target is June 30, 2022, and the Board of Managing Directors already met this target since Corinna Schittenhelm was appointed to the Board of Managing Directors on January 01, 2016.

Consistent with the group's international stature and wide variety of sectors, the Board of Managing Directors considers diversity when making appointments to leadership positions. It aims to give appropriate consideration to women and has set targets for the proportion of women within Schaeffler AG at the two levels of management immediately below the Board of Managing Directors in accordance with sections 76 (4) and 111 (5) AktG. The targeted proportion of women of 5% at the first level of management immediately below the Board of Managing Directors was met as at June 30, 2017. The 12% target for the second level of management immediately below the Board of Managing Directors was not met. As at June 30, 2017, the proportion of women at the second level of management amounted to 6%. The main reason for the failure to meet this target was an organizational transfer within the Schaeffler Group that significantly increased Schaeffler AG's number of employees in 2016. The positions at the second level of management in the newly-added areas were largely filled with men, which resulted in a deterioration of the proportion of women. Although the number of employees remained constant, the proportion of women at the second level of management has already improved to 9% as at December 31, 2017, since the company specifically strived to fill vacant positions with women provided they had the appropriate qualifications. Moreover, at its meeting on June 19, 2017, the Board of Managing Directors set new targets for the proportion of women of 8% at the first level of management and 12% at the second level of management immediately below the Board of Managing Directors, to be met by June 30, 2022.

In addition to considering the relevant technical qualifications, the Supervisory Board also strives for diversity when making appointments to the Board of Managing Directors, and adopted a diversity scheme in accordance with section 289f (2) (6) HGB for the Board of Managing Directors of Schaeffler AG at its meeting on December 15, 2017. The diversity criteria selected were gender, age, professional experience, and internationality:

- **Gender:** The Board of Managing Directors should have at least one female member. This target was met in 2017. In the long term, the Supervisory Board should strive to increase the number of female members on the Board of Managing Directors beyond the established target. The targets set by the Board of Managing Directors for the two levels of management immediately below the Board of Managing Directors should be met.
- **Age:** The Board of Managing Directors should have an appropriate age distribution. Along with several younger members, this Board should also have members with a greater amount of professional and life experience. The average age of all members of the Board of Managing Directors should be approx. 55 years. Members may serve on the Board of Managing Directors until their 68th birthday. In making appointments to the Board of Managing Directors, consideration should be given to ensuring a balanced age distribution and promoting a greater number of younger executives. The targets established were met in 2017.
- **Professional experience:** The members of the Board of Managing Directors should bring diverse professional experience to the Board. Along with sufficient professional background in the fields of engineering and business, they should also have additional professional experience, especially in fields relevant to the Schaeffler Group's future business, such as mechatronics, electrical engineering, digitalization, and IT. In making appointments to the Board of Managing Directors, consideration should be given to their education and training, professional career, and their current responsibilities. The targets established were met in 2017.
- **Internationality:** Sufficient international experience should be represented on the Board of Managing Directors to appropriately reflect the international nature of the Schaeffler Group's business. The members of the Board of Managing Directors should have different nationalities. The objective should be that all members of the Board of Managing Directors have experience working abroad and/or are experienced in international business. Having at least one member with a non-German nationality, ideally from a market relevant to Schaeffler, on the Board of Managing Directors in the long-term is considered desirable. To be appointed to the Board of Managing Directors, a candidate must have international experience. At the first and second level of management immediately below the Board of Managing Directors, the majority of employees should have experience working abroad and be experienced in international business. The targets established were met in 2017.

At the reporting date, no member of the Board of Managing Directors held more than three positions on supervisory boards of non-group public companies or similarly demanding positions on supervisory bodies of non-group companies.

More on the members of the Board of Managing Directors, their areas of responsibility, and any positions they hold on supervisory boards of other companies on pp. 116 et seq.

Supervisory Board

The Supervisory Board is responsible for advising and monitoring the Board of Managing Directors in managing the company. The Board of Managing Directors has to involve the Supervisory Board in any decisions that are fundamental to the company. Specifically, the internal rules of procedure set out which legal transactions and measures taken by the Board of Managing Directors require approval by the Supervisory Board or the executive committee. The Supervisory Board fulfills its responsibilities in accordance with the requirements of the law, the company's articles of association, and the internal rules of procedure. The internal rules of procedure of the Supervisory Board govern the Board's organization and activities.

The Supervisory Board appoints the members of the Board of Managing Directors and sets their remuneration.

More on the remuneration of the Board of Managing Directors on pp. 101 et seq.

The Supervisory Board holds a minimum of two meetings during each of the first and second six months of the calendar year to discuss current issues and pass any resolutions required. Additional meetings are held when and if the interests of the company require. For reasons of effectiveness, resolutions are at times passed in writing or by telephone.

Membership of the Supervisory Board

Under the requirements of the German Co-Determination Act, the Supervisory Board of Schaeffler AG, which is subject to co-determination on the basis of parity, consists of twenty members. Ten of these members are appointed by the annual general meeting, and ten members are elected by the employees in accordance with the requirements of the German Co-Determination Act.

Since Schaeffler AG is a publicly listed company subject to codetermination based on parity, its Supervisory Board consists of at least 30% female and at least 30% male members in accordance with section 96 (2) AktG. Section 25 EGAktG stipulates that the legal gender quota is effective for new elections held on or after January 01, 2016; current positions can be held until the end of their regular term. The minimum quota applies to the Supervisory Board as a whole (joint compliance). However, both the shareholder representatives and the employee representatives are entitled to object to joint compliance by a majority resolution; in this case, the quota has to be met separately by the shareholder representatives as well as by the employee representatives (separate compliance). The employee representatives unanimously objected to joint compliance with the gender quota on December 10, 2015. The Supervisory Board currently has four female members, three women are employee representatives and one woman represents the shareholders. As a result, the employee representatives meet the legally required quota. The shareholder representative's quota is currently at 10%.

In accordance with item 5.4.1 of the German Corporate Governance Code, the Supervisory Board has set the following concrete targets for its membership, considering the company's specific situation and appropriately taking into account the company's international operations, any potential conflicts of interest, the number of independent Supervisory Board members, and a set limit on the length of time a member may serve on the Supervisory Board, as well as diversity: The Supervisory Board has stated the following objectives for its membership:

- Members should have the knowledge, skills, and technical experience required to properly perform their duties and be able to devote sufficient time to these duties.
- The Supervisory Board aims to maintain the current proportion of members with an international background.
- Under the assumption that all employee representatives on the Supervisory Board can be considered independent, the Supervisory Board aims to have a minimum of 15 independent members (as defined in item 5.4.2 of the German Corporate Governance Code).
- Members of the Supervisory Board should not serve on the governing body of or in a consulting capacity to significant competitors of the Schaeffler Group.
- The Supervisory Board should not include more than two former members of the Board of Managing Directors.
- Members of the Supervisory Board should not normally serve on the Board for more than three terms of office.

In addition to the objectives set out above, the Supervisory Board developed a profile of expertise for the Board as a whole at its meeting on December 15, 2017. According to this profile, the Supervisory Board should collectively cover the following areas of technical expertise. Having at least one member of the Supervisory Board cover an area of expertise is considered sufficient. The profile of expertise assumes that every member of the Supervisory Board has the personal qualifications required to successfully carry out the responsibilities of a member of the Supervisory Board, i.e. integrity, sufficient time, commitment, and discretion.

- **Sector knowledge:** The Supervisory Board should have knowledge of and experience with the automotive sector and with the sectors in which the Industrial division operates.
- **Law/compliance:** The Supervisory Board should have members with basic knowledge of stock corporation and corporate law and of the compliance field.
- **Finance:** The Supervisory Board should be knowledgeable about and experienced in finance, financial reporting, auditing, risk management, and systems of internal controls.
- **Leadership:** The Supervisory Board should have members experienced in leadership. This includes experience in managing and supervising companies.
- **Research and development:** The Supervisory Board should also be knowledgeable about and experienced in research and development, preferably in future-oriented fields such as E-Mobility and Digitalization.

The current Supervisory Board meets these objectives and covers the areas of expertise set out above. Proposals by the Supervisory Board to the annual general meeting for the election of shareholder representatives to the Supervisory Board will reflect these objectives and strive to cover the fields of expertise listed above.

Along with the objectives and the profile of expertise, the Supervisory Board also adopted a diversity scheme in accordance with section 289f (2) (6) HGB for the Supervisory Board of Schaeffler AG on December 15, 2017. The diversity criteria selected were gender, professional experience, and internationality. These criteria are designed to ensure, in combination with the other criteria for the membership of the Supervisory Board, that the opinions and knowledge represented on the Supervisory Board are sufficiently diverse for the proper performance of its duties.

- **Gender:** Section 96 (2) AktG stipulates that the Supervisory Board has to consist of at least 30% female and at least 30% male members. The employee representatives unanimously objected to joint compliance with the gender quota on December 10, 2015. The Supervisory Board currently has four female members, three women are employee representatives and one woman represents the shareholders. As a result, the employee representatives meet the legally required quota. The employer representative's quota is currently at 10%. Nominees for replacement appointments and for the regular election of shareholder representatives in 2019 are limited to candidates whose election will ensure that the legal requirements are met.
- **Professional experience:** The members of the Supervisory Board should bring diverse professional experience to the Board. The Supervisory Board should have members with professional experience in fields that are relevant to the Schaeffler Group's business, especially to the group's future business in the fields of E-Mobility and Digitalization. Candidates' professional experience is to be taken into account when selecting the Supervisory Board's nominees for election to the Supervisory Board by the annual general meeting.
- **Internationality:** The Supervisory Board should have an appropriate number of members with an international background (descent, professional education, or work). This being the case for at least four of its members is considered adequate by the Supervisory Board. In addition, further members of the Supervisory Board should be experienced in international business. Internationality is to be taken into account when selecting the Supervisory Board's nominees for election by the annual general meeting.

Members of the Supervisory Board and their curricula vitae at: www.schaeffler.com/supervisory-board

The Supervisory Board as a whole has the knowledge, skills, and technical experience required to properly perform its duties. The Supervisory Board as a whole is familiar with the industries and sectors in which the Schaeffler Group operates, and it has the professional experience and internationality required under the diversity scheme. Conflicts of interest related to members of the Supervisory Board must be disclosed to the Supervisory Board immediately; there were no such conflicts of interest in 2017. No member of the Supervisory Board currently serves on a governing body or in a consulting role with respect to a key competitor or is a former member of the Board of Managing Directors.

More on avoiding conflicts of interest on page 90

The Supervisory Board has not set an age limit for its members, because it is of the opinion that this criterion is not informative with respect to the suitability of a person to perform as a member of the Supervisory Board. This deviation from the German Corporate Governance Code has been included in the declaration of conformity pursuant to section 161 AktG.

The Supervisory Board considers all shareholder representatives except for Maria-Elisabeth Schaeffler-Thumann and Georg F. W. Schaeffler to be independent. These are: Prof. Dr. Hans-Jörg Bullinger, Dr. Holger Engelmann, Prof. Dr. Bernd Gottschalk, Dr. Siegfried Luther, Robin Stalker, Dr. Otto Wiesheu, Prof. KR Ing. Siegfried Wolf, and Prof. Dr.-Ing. Tong Zhang.

The Chairman of the Supervisory Board is elected by the Supervisory Board from among its members. He coordinates the activities of the Supervisory Board, chairs its meetings, and represents the Supervisory Board externally. As recommended in item 5.2 (2) of the German Corporate Governance Code, the Chairman of the Supervisory Board is available for discussions with investors, in close coordination with the Board of Managing Directors and focusing on Supervisory Board-related issues.

Membership and mode of operation of Supervisory Board committees

Under its internal rules of procedure, the Supervisory Board establishes a total of four committees.

The mediation committee established in accordance with sections 27 (3) and 31 (3) of the German Co-Determination Act is responsible for proposing to the Supervisory Board a candidate for appointment to the Board of Managing Directors if the two-thirds majority required for an appointment was not obtained initially. The members of the mediation committee are Maria-Elisabeth Schaeffler-Thumann as well as Norbert Lenhard, Georg F. W. Schaeffler, and Jürgen Wechsler; Georg F. W. Schaeffler chairs the committee.

The nomination committee proposes to the Supervisory Board appropriate candidates for election to the Supervisory Board by the annual general meeting. The members of the nomination committee are the Chairman of the Supervisory Board, Georg F. W. Schaeffler, as well as Dr. Holger Engelmann, Prof. Dr. Bernd Gottschalk, and Maria-Elisabeth Schaeffler-Thumann; Georg F. W. Schaeffler is the committee's chairman.

The executive committee consists of Barbara Resch and Maria-Elisabeth Schaeffler-Thumann as well as Norbert Lenhard, Georg F. W. Schaeffler, Jürgen Wechsler, and Prof. KR Ing. Siegfried Wolf; Georg F. W. Schaeffler is the committee's chairman. The executive committee advises and assists the Chairman of the Supervisory Board and his Deputy in their Supervisory Board responsibilities. It prepares the meetings of the Supervisory Board. Another significant responsibility of the executive committee is preparing personnel decisions to be made by the Supervisory Board. It makes recommendations regarding new appointments or reappointments to and dismissals from the Board of Managing Directors. It also prepares the Supervisory Board's decision regarding the remuneration system and individual remuneration of the members of the Board of Managing Directors. In addition, the executive committee passes resolutions regarding the approval of certain legal transactions and measures specified in the Supervisory Board's internal rules of procedure on behalf of the Supervisory Board, to the extent such delegation is not prohibited by section 107 (3) (3) AktG.

The audit committee is responsible for preparing the Supervisory Board's decision on adoption of the separate financial statements and approval of the consolidated financial statements. To this end, it is responsible for the preliminary review of the separate and consolidated financial statements, the management report, the group management report and the combined management report, the proposals for the appropriation of earnings, and for discussing the long-form audit report with the auditors. It is also responsible for the preliminary review of the report on relations with affiliated companies and the non-financial report as well as for preparing the Supervisory Board's nomination of the auditors to be appointed by the annual general meeting.

The audit committee makes a recommendation to the Supervisory Board regarding auditors to be appointed, together with its reasons for the recommendation; where the audit has been put out to tender, the recommendation includes at least two candidates. The audit committee engages the auditors, determines the areas of focus for the audit, and agrees the audit fees with the auditors. In addition, the audit committee monitors the independence of the external auditors, and, as such, is responsible for approving engagements for non-audit services. The audit committee also monitors the qualifications and efficiency of the auditors as well as the rotation of audit team members. On behalf of the Supervisory Board, the audit committee advises and oversees the Board of Managing Directors regarding financial reporting, the financial reporting process, the effectiveness of the internal control system, the risk management system, Internal Audit, the financial statement audit, and compliance.

The audit committee consists of six members. His position automatically makes the Chairman of the Supervisory Board a committee member. The chairman of the audit committee shall be independent and can be neither a former member of the Board of Managing Directors nor the Chairman of the Supervisory Board; he shall be particularly knowledgeable about and experienced in the application of accounting principles as well as internal control procedures. As the former chief financial officer of the Bertelsmann Group, the chairman of the audit committee, Dr. Siegfried Luther, meets these requirements. The committee includes another financial expert, Robin Stalker. The other committee members are Dr. Reinold Mittag, Georg F. W. Schaeffler, Salvatore Vicari, and Jürgen Worrich.

Cooperation between Board of Managing Directors and Supervisory Board

The Board of Managing Directors and the Supervisory Board cooperate closely for the good of the company. Thus, the Board of Managing Directors regularly consults with the Supervisory Board on the strategic direction of the company and discusses the status of strategy implementation with the Supervisory Board.

On a regular basis, the Board of Managing Directors provides comprehensive and timely information to the Supervisory Board on all matters of relevance to the company with respect to strategy implementation, planning and budgeting, results of operations, risk management, and compliance. It discusses deviations of results of operations from budgets and targets and the reasons for those deviations. Documents required for decisions, especially the separate financial statements, the consolidated financial statements, and the long-form audit report, are provided to the members of the Supervisory Board in due time. The Board of Managing Directors is required to submit any fundamental legal transactions and measures to the Supervisory Board or the executive committee for approval. The cooperation between the Board of Managing Directors and the Supervisory Board is characterized by mutual trust and a culture of open discussion as well as maintaining strict confidentiality.

The Chairman of the Supervisory Board regularly keeps in contact with the Board of Managing Directors, particularly with the Chief Executive Officer, between meetings as well, and discusses with him issues related to the company's strategy implementation, planning and budgeting, results of operations, risk management, and compliance. The Chief Executive Officer immediately informs the Chairman of the Supervisory Board of important events significant to evaluating the company's situation and development as well as for managing the company.

Avoiding conflicts of interest

The members of the Board of Managing Directors and of the Supervisory Board are required to immediately disclose any conflict of interest to the Supervisory Board. Significant transactions between the company and members of the Board of Managing Directors or parties related to them require the Supervisory Board's approval. Consulting and other service contracts as well as contracts for specific deliverables between the company and members of the Supervisory Board also require approval by the Supervisory Board. The Supervisory Board reports to the annual general meeting on any conflicts of interest and their resolution. Neither the members of the Board of Managing Directors nor those of the Supervisory Board have experienced any conflicts of interest in 2017.

1.4 Other information on corporate governance

Transparency

The company provides information on the situation of the company at the same time and on an equal footing to institutional investors, shareholders, financial analysts, business partners, employees, and the interested public by regular, transparent, and up-to-date communication. All significant information, such as ad hoc releases and press releases, as well as presentations given at analysts' conferences, all financial reports, and the financial calendar are published on the Schaeffler Group's website. Investor Relations maintains close contact with shareholders on an ongoing basis.

Relationships with shareholders and annual general meeting

Shareholders exercise their rights at the annual general meeting. The annual general meeting passes resolutions on granting discharge to the Board of Managing Directors and the Supervisory Board, appropriating retained earnings, capital transactions, amendments to the company's articles of association, and appointing auditors. It has to be held during the first eight months of each year.

The company has issued common non-voting and common shares. Common non-voting shares do not convey voting rights, but entitle the holder to a preferred dividend of EUR 0.01 per share.

Shareholders have to register for the annual general meeting in due time in order to attend the annual general meeting. An invitation and other documents (e.g. annual report) containing information on the items on the agenda of the annual general meeting are provided to shareholders before the annual general meeting. This information is also available from the company's website.

Financial reporting and financial statement audit

The main source of information for shareholders and third parties are the consolidated financial statements and the group management report as well as interim financial information.

Schaeffler AG compiles its separate financial statements in accordance with the requirements of the German Commercial Code (HGB) and the German Stock Corporations Act (AktG). The consolidated financial statements and the group management report are prepared by the Board of Managing Directors in accordance with the principles set out in International Financial Reporting Standards (IFRS) as adopted by the EU and are audited by the auditors and reviewed by the Supervisory Board. Before any interim financial information is made public, the Board of Managing Directors discusses such information with the Supervisory Board or the audit committee. The consolidated financial statements and the group management report are made publicly available within 90 days after the end of the year, mandatory interim financial information within 45 days after the end of the reporting period.

In addition, the consolidated financial statements include a discussion of transactions with shareholders considered related parties under applicable financial reporting standards.

It was agreed with Schaeffler AG's auditors that the Chairman of the Supervisory Board and the chairman of the audit committee would be informed promptly of any grounds for disqualification or indications of bias arising during the audit to the extent they are not remedied immediately. It was also agreed that the auditors would report on all findings and events coming to their attention during the performance of their audit that are significant to the responsibilities of the Supervisory Board. Under the agreement, the auditors have to inform the Supervisory Board and note in their long-form audit report if, during the course of the audit, they become aware of any facts rendering the declarations on the German Corporate Governance Code issued by the Board of Managing Directors and the Supervisory Board inaccurate. The audit committee monitors the auditors' independence. In a letter dated March 02, 2017, the auditors have issued a binding independence letter for the year ended December 31, 2017.

Georg F. W. Schaeffler
Chairman of the Supervisory Board

2. Report of the Supervisory Board

Ladies and Gentlemen,

The Supervisory Board has dutifully performed the duties mandated by law, the company's articles of association, and its internal rules of procedure during the year. The Supervisory Board has provided advice to the Board of Managing Directors and supervised its activities. In doing so, it was directly involved on a timely basis in all decisions that were of fundamental importance to the company and the group. The Board of Managing Directors regularly informed the Supervisory Board in written and oral reports about the company's results of operations. The Board of Managing Directors briefed the Supervisory Board on an ongoing basis and in detail about the development of revenue and earnings of the group and the divisions, the financial position, short- and long-term plans and budgets, as well as compliance and risk management matters. The Board of Managing Directors briefed the Supervisory Board in a timely fashion on any important transactions. In addition, the Board of Managing Directors and the Supervisory Board discussed and refined the Schaeffler Group's strategy in detail.

The members of the Supervisory Board were also available for discussions with the Board of Managing Directors between meetings. The Chairman of the Supervisory Board regularly kept in contact with the Board of Managing Directors and particularly with the Chief Executive Officer, and ensured that he was kept informed about all current matters and developments on an ongoing basis.

More on corporate governance on pp. 85 et seq.

Members of the Supervisory Board and its committees

There was one change in the membership of the Supervisory Board during the reporting period. Yvonne Münch left the Supervisory Board on March 07, 2017 because she was employed by a group company that was sold to a third party. The appointment of Andrea Grimm to the Supervisory Board by a court became effective on April 08, 2017.

The committees of the Supervisory Board remained unchanged in 2017. The following committees have been established:

- Mediation committee established in accordance with section 27 (3) German Co-Determination Act:
  Georg F. W. Schaeffler (Chairman), Norbert Lenhard, Maria-Elisabeth Schaeffler-Thumann, and Jürgen Wechsler
- Executive committee:
  Georg F. W. Schaeffler (Chairman), Norbert Lenhard, Barbara Resch, Maria-Elisabeth Schaeffler-Thumann, Jürgen Wechsler, and Prof. KR Ing. Siegfried Wolf
- Audit committee:
  Dr. Siegfried Luther (Chairman), Dr. Reinold Mittag, Georg F. W. Schaeffler, Robin Stalker, Salvatore Vicari, and Jürgen Worrich
- Nomination committee:
  Georg F. W. Schaeffler (Chairman), Dr. Holger Engelmann, Prof. Dr. Bernd Gottschalk, and Maria-Elisabeth Schaeffler-Thumann

In 2017, the Supervisory Board once again dealt with matters concerning its membership. This involved developing a profile of expertise and a diversity scheme for the entire Supervisory Board. The Supervisory Board also developed a diversity scheme for the Board of Managing Directors.

The Supervisory Board continues to consider the number of its independent members (as defined in the German Corporate Governance Code) sufficient. The Supervisory Board views all shareholder representatives on the Supervisory Board as independent as defined in item 5.4.2 of the GCGC, except for Maria-Elisabeth Schaeffler-Thumann and Georg F. W. Schaeffler.

There were no conflicts of interest related to members of the Board of Managing Directors or the Supervisory Board in 2017.

Appointments to the Board of Managing Directors

The company's Board of Managing Directors consists of Klaus Rosenfeld (Chief Executive Officer), Prof. Dr.-Ing. Peter Gutzmer (Deputy Chief Executive Officer), Dietmar Heinrich (since August 01, 2017), Oliver Jung, Prof. Dr. Peter Pleus, Corinna Schittenhelm, Dr. Stefan Spindler, and Matthias Zink. After Dr. Ulrich Hauck had left (until July 31, 2017), Dietmar Heinrich was appointed to the Board of Managing Directors for a term of three years effective August 01, 2017, after Dr. Ulrich Hauck (until July 31, 2017) had left. In addition, the Supervisory Board decided on July 17, 2017, to extend Dr. Spindler's term of office by five years effective May 01, 2018.

In accordance with the internal rules of procedure of the Board of Managing Directors, Klaus Rosenfeld is responsible for the CEO functions, Prof. Dr.-Ing. Peter Gutzmer for Technology, Dietmar Heinrich for Finance, Prof. Dr. Peter Pleus and Matthias Zink for the Automotive division, Dr. Stefan Spindler for the Industrial division, Oliver Jung for Operations, and Corinna Schittenhelm is responsible for Human Resources. The company established a new "Automotive Aftermarket" division as of January 01, 2018. On October 06, 2017, the Supervisory Board appointed Michael Söding as the member of the Board of Managing Directors responsible for the newly-established division for a term of three years beginning on January 01, 2018.

Topics of Supervisory Board plenary meetings

The Supervisory Board held four regular meetings, one strategy meeting, and two extraordinary meetings in 2017. In addition, one resolution was passed in writing, and several conference calls were held in which the Board of Managing Directors briefed the Supervisory Board on certain transactions.

The Supervisory Board met for an extraordinary meeting via conference call on February 03, 2017, to discuss the preliminary achievement of targets and objectives related to the variable remuneration of the Managing Directors.

At its first regular meeting of the year on March 03, 2017, the Supervisory Board was briefed on the company's most recent results of operations and discussed the separate and consolidated financial statements of the Schaeffler Group for 2016, adopted the separate financial statements, and approved the consolidated financial statements, the closing statement on the dependency report, and the proposal for the appropriation of earnings. In addition, it approved the report of the Supervisory Board to the annual general meeting 2017 and the Supervisory Board's proposed resolutions on the items on the agenda of the annual general meeting. The Supervisory Board also passed a resolution regarding the achievement of targets and objectives related to the variable remuneration of the Managing Directors. Finally, the meeting discussed the results of the review of the appropriateness of the Managing Directors' remuneration performed by Ernst & Young GmbH Wirtschaftsprüfungsgesellschaft. Ernst & Young GmbH Wirtschaftsprüfungsgesellschaft concluded that the total direct remuneration of the members of Schaeffler AG's Board of Managing Directors is customary and appropriate in comparison to that of other companies of comparable size within the same industry and country in terms of the amount, structure, and features of remuneration instruments.

At its regular meeting on May 10, 2017, apart from dealing with certain personnel matters, the Supervisory Board set the target for the proportion of female members of the Board of Managing Directors in accordance with section 111 (5) AktG. In addition, the Supervisory Board was briefed on the company's results of operations and the results for the 1st quarter of 2017. The meeting also heard a report on the Schaeffler Group's Technology Dialog.

At the extraordinary meeting held via conference call on July 17, 2017, the Supervisory Board appointed Dietmar Heinrich to the Board of Managing Directors and extended the employment contract of Dr. Stefan Spindler for his position on the Board of Managing Directors.

On October 05, 2017, the Supervisory Board held its strategy meeting, in which the Board of Managing Directors presented its strategy considerations for the Schaeffler Group. The proposals were discussed in detail.

At its third regular meeting on October 06, 2017, the Supervisory Board heard a report on the Schaeffler Group's most recent results of operations and the results of the first half of 2017. There was also a report on the "European Distribution Center" and "Aftermarket Kitting Operation" projects. In addition, Michael Söding was appointed to the Board of Managing Directors.

In a resolution passed in writing on November 06, 2017, the Supervisory Board approved the "Aftermarket Kitting Operation" project.

At its fourth and final regular meeting on December 15, 2017, the Supervisory Board was briefed on the Schaeffler Group's most recent results of operations and the results of the third quarter of 2017. It also approved the budget for 2018 and the long-range plan for the years 2018 to 2022. There was a report on the Chassis Systems business division. In addition, the Supervisory Board approved the financing arrangements for the "European Distribution Center" and "Aftermarket Kitting Operation" projects. Apart from dealing with personnel matters, the Supervisory Board approved the profile of expertise for the Supervisory Board as a whole and the diversity schemes for the Board of Managing Directors and the Supervisory Board on December 15, 2017. The Supervisory Board also approved the updated declaration on the German Corporate Governance Code (section 161 AktG) and engaged KPMG AG Wirtschaftsprüfungsgesellschaft to review the non-financial report (section 111 (2)(4) AktG).

Topics of Supervisory Board committee meetings

The executive committee of the Supervisory Board held a total of four regular meetings in 2017 and passed one resolution in writing. Executive committee meetings were used to prepare the corresponding plenary meeting of the Supervisory Board, especially the personnel decisions to be made by the Supervisory Board. The executive committee also approved external activities of members of the Board of Managing Directors. In addition, the regular executive committee meeting on October 05, 2017, approved the Schaeffler Group's enhanced organizational structure proposed by the Board of Managing Directors. A resolution approving a settlement agreement between Schaeffler Technologies AG & Co. KG and Allianz Global Corporate & Specialty SE was passed in writing on November 23, 2017.

The audit committee held four regular meetings in 2017. In addition to addressing the separate and consolidated financial statements including the non-financial report and the dependency report the audit committee dealt, in particular, with the interim reports as at March 31, 2017, June 30, 2017, and September 30, 2017. Compliance, internal audit, risk management, and the internal control system were reported on at audit committee meetings on a regular basis. In addition, the audit committee was kept up-to-date on the status of a FREP examination and on the services provided by the auditors. The audit committee also heard reports on the implementation of IFRS 15 and on R&D controlling. Non-audit services provided by the auditors were discussed and approved. The process for reviewing the auditors' non-audit services was reviewed as well. The audit committee recommended to the 2017 annual general meeting that it appoint KPMG AG Wirtschaftsprüfungsgesellschaft auditors of the separate and consolidated financial statements and auditors for purposes of reviews of interim financial statements and financial information. The audit committee engaged KPMG AG Wirtschaftsprüfungsgesellschaft as auditors and determined areas of focus for the audit. The audit committee also proposed engaging KPMG AG Wirtschaftsprüfungsgesellschaft to review the non-financial report.

The nomination and mediation committees did not hold any meetings during the reporting period.

The chairmen of the executive and audit committees reported on the committees' activities to the corresponding subsequent plenary meeting of the Supervisory Board.

The members of the Supervisory Board and the members of the committees attended more than half of the meetings of the Supervisory Board and the committees they were on in 2017.

Separate and consolidated financial statements 2017

KPMG AG Wirtschaftsprüfungsgesellschaft has audited the separate financial statements, the consolidated financial statements, and the combined management report as at December 31, 2017, prepared by the Board of Managing Directors in accordance with German commercial law, including the accounting records and the accounting-related internal control system as well as the early warning risk identification system. The consolidated financial statements of Schaeffler AG as at and for the year ended December 31, 2017, were prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union and the additional requirements of German commercial law pursuant to section 315e (1) German Commercial Code.

KPMG AG Wirtschaftsprüfungsgesellschaft has also audited the report on relations with affiliated companies ("dependency report") prepared by the Board of Managing Directors in accordance with section 312 German Stock Corporations Act. The report covers the period from January 01, 2017, to December 31, 2017.

The auditors have issued unqualified audit opinions on the separate financial statements and the consolidated financial statements. They also found that the Board of Managing Directors has made the arrangements required by section 91 (2) German Stock Corporations Act for the timely identification of risks, and that the early warning risk identification system is suitable for identifying on a timely basis any developments jeopardizing the existence of the company as a going concern.

KPMG AG Wirtschaftsprüfungsgesellschaft has issued the following unqualified audit opinion on the dependency report in accordance with section 313 (3) AktG:

"In accordance with our conscientious audit and assessment, we confirm that the statements of fact in the report are correct, the consideration given by the company in the course of the transactions listed in the report was not unreasonably high, and the measures listed in the report are not an occasion for an assessment substantially different from that of the Board of Managing Directors".

The Schaeffler Group has prepared its first combined separate non-financial report, covering the year 2017. KPMG AG

Wirtschaftsprüfungsgesellschaft has performed a limited assurance engagement on the non-financial report and found that, based on the limited review procedures performed, nothing has come to its attention that causes it to believe that the combined separate non-financial report has not been prepared, in all material respects, in accordance with legal requirements.

The audit committee discussed the financial statement documents, the combined separate non-financial report, the dependency report, the long-form audit reports, and the report on the limited assurance engagement with the Board of Managing Directors and the auditors on March 01, 2018. The audit committee scrutinized the development of earnings for 2017, the financial position and net assets as at the reporting date, and, particularly, provisions for risks. The financial statement documents, the combined separate non-financial report, the dependency report, the long-form audit reports, and the recommendations of the audit committee were also dealt with in the Supervisory Board meeting convened to approve the financial statements on March 02, 2018. The required documents had been distributed to all members of the audit committee and the Supervisory Board in due time before these meetings to give members sufficient opportunity to examine them. The auditor was present during the discussion. He reported on significant findings of the financial statement audit and the limited assurance engagement and was available to provide additional information to the audit committee and the Supervisory Board. Based on its own examinations of the separate financial statements, the dependency report (including the closing statement of the Board of Managing Directors), the combined separate non-financial report, and the consolidated financial statements together with the combined management report, and based on recommendations made by the audit committee, the Supervisory Board concurs with the result of the auditors' audits. There was no cause for objection, including objection to the closing statement on the dependency report prepared by the Board of Managing Directors. The Supervisory Board has approved the separate financial statements and the consolidated financial statements. The separate financial statements have thus been adopted.

The Supervisory Board has reviewed the appropriation of retained earnings proposed by the Board of Managing Directors and will, together with the Board of Managing Directors, propose to the annual general meeting the payment of a dividend of EUR 0.54 per common share and EUR 0.55 per common non-voting share in respect of 2017.

On behalf of the Supervisory Board, I would like to express my sincere gratitude to the members of the Board of Managing Directors, to management, and to all other employees of Schaeffler AG and the group companies for their great commitment and dedication and their constructive teamwork in 2017.

For the Supervisory Board

Georg F. W. Schaeffler
Chairman

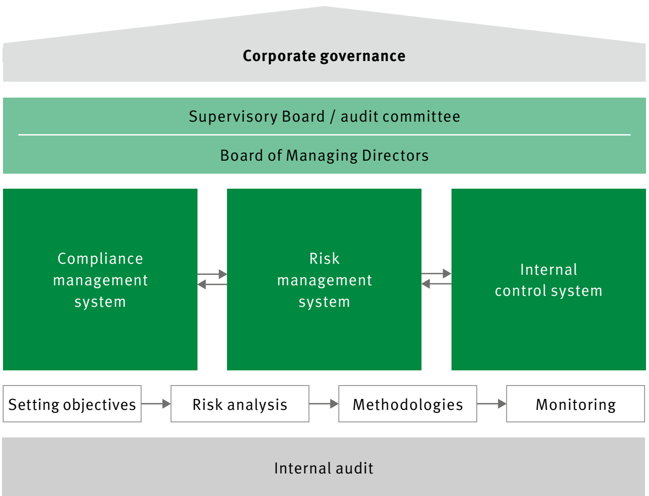
Herzogenaurach, March 02, 2018

3. Governance structure

The Schaeffler Group considers maintaining the corporate culture of a global family business essential and intends to play a leading role as a listed family business. In doing so, its focus is on customer relationships and acting with integrity. Its corporate values drive the nature of its transactions. Transactions and business relationships inconsistent with the group's corporate values are rejected. The governance structure promotes transparency and supports the values "Sustainable", "Innovative", "Excellent", and "Passionate".

The components of the **governance structure** support the operating business units in effectively identifying and managing risk.

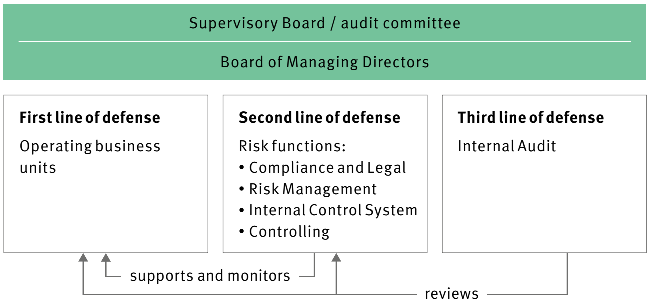
Schaeffler Group governance structure No. 069



The Schaeffler Group has continued to improve the processes within its governance structure with a view to meeting the needs of its customers while at the same time protecting the company. The governance structure is aimed at promoting the coordinated operation of the subsystems and, hence, the early identification of risks to the continued existence and development of the Schaeffler Group. Clearly assigned responsibilities and a robust internal control system are in place to manage significant risks.

The Group Compliance and Risk Committee (GCRC) represents a key governance component in this regard, increasing transparency in internal structures, the organization, and in responsibilities. The GCRC is chaired by the Schaeffler Group's Group Chief Compliance Officer. It consists of the heads of the relevant governance functions (including Compliance, Legal, Internal Control System, and Controlling). The GCRC is responsible for assisting the Board of Managing Directors with its organizational responsibilities with respect to compliance and risk management. Among the key objectives of the GCRC are defining and delineating responsibilities and interfaces and preventing redundancies in the process. In addition, it is expected to create a consistent and complete view of the risk situation in the divisions, functions, and regions based on a uniform measurement and prioritization methodology. A further objective is developing and monitoring risk mitigation activities. The Compliance & Risk Working Group consisting of staff representatives from the functions represented on the GCRC provides operational support to the GCRC.

Three lines of defense model No. 070



The activities of the subsystems within the governance structure are coordinated based on the internationally recognized **three lines of defense model**. It assigns clear responsibility for dealing with risks to the company's continued existence and development and is based on the principle that primary responsibility for a risk lies with its originator.

First line of defense: At the first tier, operating business units are responsible for performing controls within all business processes to prevent risk. If prevention is not feasible, risks have to be identified and reduced to an appropriate level. Hence, the Schaeffler Group's employees represent the first line of defense against potential risks. The Schaeffler Code of Conduct encourages them to turn to their supervisor or the corresponding control function with any questions or concerns they might have regarding dealing with risks and inappropriate business practices. If needed, they can use an anonymous whistleblowing system for reporting severe violations of the Schaeffler Code of Conduct, especially regarding illegal business practices, that is available for this purpose.

Second line of defense: At the second tier, risk functions (including Internal Control System, Controlling, Risk Management, Compliance, and Legal) define global standards and controls, regularly monitor compliance with them, and report on their effectiveness. The Risk Management function is also responsible for regular and independent risk assessment.

Third line of defense: The third tier is the audit by Internal Audit. Independent and objective audits are designed to ensure process efficiency in risk management, internal controls, and corporate governance.

With its corporate governance structure and its "three lines of defense model", the Schaeffler Group fulfils its obligation to manage the company responsibly and to maintain effective controls.

3.1 Compliance management system

Integrity is one of the mainstays of the Schaeffler Group's manner of conducting business. Under the Schaeffler Code of Conduct, the Board of Managing Directors and all employees are required to comply with all applicable local, national, and international laws and regulations, wherever the Schaeffler Group does business. A compliance organization covering the entire Schaeffler Group provides them with support in doing so.

The Schaeffler Group's Board of Managing Directors emphatically supports the underlying compliance management system (CMS) and the necessity of consistently complying with legal requirements and internal regulations.

The CMS is based on the three pillars of prevention, detection, and reaction and is part of the second line of defense within the Schaeffler Group's governance structure. The CMS in its current state is the result of a comprehensive revision initiated by the Board of Managing Directors as part of the "Compliance Fit & Proper" program. Following the successful completion of a review of the underlying conceptual design in accordance with the Principles for the Proper Performance of Reasonable Assurance Engagements Relating to Compliance Management Systems IDW AsS 980 by an independent audit firm, an independent audit firm has started to review the implementation of the CMS. The review is scheduled to be completed by mid-2018.

The CMS comprises, in particular, managing and monitoring the activities necessary to prevent, or detect early on, violations of law in the area of corruption, money-laundering, competition and antitrust law, and economic criminal activity. It also serves to actively manage risk and protect the company and its employees. The CMS consists of seven core components: compliance culture, compliance objectives, vulnerability analysis, compliance program, compliance organization, communication, and monitoring and improvement.

The compliance organization derives its arrangements for preventing violations of antitrust and competition legislation, corruption, economic crime, and money-laundering from a regular groupwide risk analysis using a risk-based approach. The risk analysis provides information on the current situation with respect to risks arising from operations and on the effectiveness of the preventive arrangements in place. The analysis is primarily based on interviews with management and employees of all divisions and regions with the objective of obtaining information that is required to estimate the probability of occurrence and the size of the potential amount of damage and that is as close to the business processes as possible. These estimates are supplemented with sector and expert knowledge, experience with actual compliance violations, results of controls and audits, as well as by using operations-, market-, and country-specific risk criteria ranging from publicly available risk indicators, such as the Corruption Perception Index compiled by Transparency International, through to issues regarding the location-specific design of Schaeffler's business model.

The Schaeffler Group's Group Chief Compliance Officer heads up the compliance organization and reports directly to the Chief Executive Officer. The Group Chief Compliance Officer also has a reporting line to the Chairman of the Supervisory Board and reports to the chairman of the audit committee on a regular basis.

The compliance department provides the Group Chief Compliance Officer with the support of a network of experienced compliance specialists spanning all of the Schaeffler Group's Europe, Americas, Greater China, and Asia/Pacific regions. He also utilizes a centralized team of experts located at the corporate head office in Herzogenaurach that consists of the "Advisory", "Risk Analysis & Solutions", and "Forensics & Investigations" departments. The responsibilities of this team of experts include defining and monitoring appropriate groupwide compliance standards and activities, consulting on compliance, and improving processes and controls. The team is also responsible for independently investigating alleged violations and following up on the necessary consequences. It analyzes the causes of misconduct, derives suggestions for remedial measures, and follows up on their implementation. Violations of laws and regulations or of internal rules on compliance with these are not tolerated and result in disciplinary action.

Measures designed to prevent compliance violations include the Schaeffler Group's Code of Conduct, guidelines on behavior in compliance with antitrust and competition legislation, fighting corruption, and protecting confidential information, web-based and classroom training sessions, and a compliance helpdesk available for consultation on specific compliance issues. In addition to requirements relating to general conduct, the principles and practices described in the Schaeffler Code of Conduct also cover conduct vis-à-vis business partners and third parties, dealing with sensitive information, employees and co-workers, and requirements regarding the environment, health, and safety. In accordance with the corporate values, bribery or any form of corruption are not tolerated. All Schaeffler Group employees are expressly prohibited from engaging in corruption in any way. The same applies to conduct violating competition or antitrust laws. The Schaeffler Group stays away from any transactions that cannot be effected or continued without unacceptable conduct.

Training sessions are continually refined and updated and adapted to the employees' areas of responsibility. In 2017, the compliance training program included training on risk awareness, the Schaeffler Code of Conduct, security of information including classification of information, protection against cybercrime, and CEO fraud. In addition, the company has also put in place arrangements for detecting possible compliance violations; these arrangements include audits and controls as well as a whistleblowing system which can be used to report violations on an anonymous basis. All such reports received are reviewed independently. Reprisals against employees reporting concerns about misconduct within the company in good faith are prohibited.

The Schaeffler Group has further expanded its arrangements and measures for complying with legal requirements and internal rules in 2017. The company continued to expand its register of contacts with competitors. The register was introduced at a number of pilot locations worldwide. It contributes to transparency and supports the process for approving contacts with competitors in advance. The company also developed a new business partner due diligence process that can in future be used to further minimize any business partner-related risks groupwide using an IT tool integrated into the business processes as much as possible. Both underline the standard the Schaeffler Group expects of its business partners with respect to acting with integrity and abiding by rules.

The company maintains an insider list in order to comply with capital markets regulations. As soon as an individual is added to the insider list (whether event-driven or as a permanent insider), the individual is notified and separately informed of the legal obligations and sanctions related to his or her access to insider information. In addition, there is an insider committee whose activities include deciding on how to deal with potential insider information and ensuring compliance with the requirements of capital markets laws.

3.2 Risk management system

Like the compliance management system, the risk management system is part of the second line of defense in the Schaeffler Group's governance structure. It comprises all activities and arrangements made to identify, assess, manage, and monitor risk. A risk is defined as the danger that events or actions will prevent a company from achieving its plan or successfully implementing its strategies. For all identified risks, the probability of occurrence and possible impact on achieving objectives are continually identified, assessed, appropriate action initiated and followed-up on.

More on the company's risk management system on pp. 71 et seq.

3.3 Internal control system

The second line of defense also comprises the Schaeffler Group's internal control system (ICS). The ICS consists of technological and organizational arrangements and controls that have been systematically designed to ensure compliance with guidelines and to prevent loss or damage that may be caused by the company's employees or by third parties. Controls can be performed both process-dependent or independently of the process. The Schaeffler Group's internal control system is based on the COSO model and consists of the following components: control environment, risk assessment, control activities, information and communication, and monitoring. It is focused on financial reporting and represents the arrangements and controls ensuring that the consolidated financial statements are prepared in accordance with financial reporting standards and ensuring accurate external financial reporting.

More on the company's internal control system on pp. 73 et seq.

3.4 Internal Audit

Internal Audit represents the third line of defense of the Schaeffler Group's governance structure. Internal Audit provides independent and objective audit and consulting services focused on adding value and improving business processes. The internal audit function contributes to meeting the corporate objectives the Schaeffler Group has communicated by assessing and helping to improve the effectiveness of the compliance management system, risk management, controls, and management and supervisory processes using a systematic and goal-oriented approach. Responsibility for establishing the internal audit function and for its effectiveness rests with the Board of Managing Directors and cannot be delegated. Hence, Internal Audit reports to the entire Board of Managing Directors. The head of Internal Audit reports directly to the Chief Executive Officer of Schaeffler AG and also reports to the chairman of the audit committee on a regular basis.

The Schaeffler Group has made the following arrangements to ensure the independence and objectivity of Internal Audit:

- direct organizational link to the Chief Executive Officer to ensure there are no gaps in audit coverage
- neither the head of Internal Audit nor audit staff have any operational responsibilities
- reports annually on potential impairment of independence to the Chief Executive Officer/Board of Managing Directors/audit committee
- The Board of Managing Directors has to approve and appropriately document the approval of the audit planning and significant changes therein.

Internal Audit consists of the functions "Methods, Reporting and Quality Assurance", "Corporate Audits" and "IT and Special Audits". It also has locations in each of the Schaeffler Group's four regions.

The responsibilities of Internal Audit specifically include, but are not limited to, the following activities:

- audit and assessment of the appropriateness, efficiency, and effectiveness of the internal control system
- audit and assessment of the appropriateness, efficiency, and effectiveness of the management and supervisory processes
- audit and assessment of the finance and accounting systems, the information system, and the reporting system
- audit and assessment of the effectiveness of risk and compliance management
- audit and assessment of the effectiveness of arrangements for preventing and detecting fraud
- audit of arrangements for safeguarding assets
- audit and assessment of the implementation of and compliance with legal requirements and the company's internal rules ("orderliness")
- performance of special investigations with respect to fraud, conflicts of interest, and other irregularities

In a risk analysis done in preparation for audit assignments, Internal Audit exchanges information with other departments (e.g. Compliance and Corporate Security, Controlling, Legal, Quality, Risk Management).

In order to obtain sufficient reliable, relevant, and constructive information to achieve its audit objectives, Internal Audit regularly performs its audit assignments on location.

In its audit reports, Internal Audit communicates its findings, identifies the individuals responsible for implementation, and agrees remediation measures, including a time frame for their implementation. In a monitoring and follow-up process, Internal Audit monitors implementation of the remediation measures addressing identified deficiencies.

In accordance with the International Standards for the Professional Practice of Internal Auditing 2016 of the Institute of Internal Auditors (IIA), the head of Internal Audit has established a quality assurance and improvement program covering all of Internal Audit's responsibilities.

4. Remuneration report

This remuneration report describes the main features of the remuneration system for the Board of Managing Directors, i.e. the remuneration structure and amount. In addition, the remuneration report provides disclosures about benefits the company has promised to provide to the members of the Board of Managing Directors upon termination of their employment as well as disclosures on the remuneration of the Supervisory Board.

The remuneration report is in accordance with the requirements of the German Commercial Code (HGB) and International Financial Reporting Standards (IFRS) and is part of the group management report. It also reflects the recommendations of the German Corporate Governance Code.

4.1 Main features of the remuneration system for the Board of Managing Directors

As stipulated in the German Corporate Governance Code (GCGC) and section 87 AktG, the Supervisory Board sets the total remuneration and regularly reviews the remuneration scheme.
To ensure that the total remuneration is appropriate, the Supervisory Board takes into account customary levels of remuneration both in other companies of comparable size within the same industry and country (horizontal comparison) and the wage and salary structure within the enterprise itself (vertical comparison of remuneration of Board of Managing Directors to the company's workforce).

The total remuneration of the Board of Managing Directors is performance- and success-based and supports the Schaeffler Group's operational and strategic objectives in a dynamic and international environment. The remuneration of each member of the Board of Managing Directors consists of a fixed amount as well as short- and long-term variable components. The variable component is largely long-term in nature. In addition, the members of the Board of Managing Directors receive the customary fringe benefits, pension commitments, a company car, and insurance benefits.

Remuneration of Board of Managing Directors – system and components No. 071

Components	Performance metric	Range of remuneration	Conditions for payment	Payment cycle
Non-performance-based components				
Fixed remuneration	Function and responsibility	None	Contractually agreed	Monthly
Fringe benefits	Function and responsibility	None	Contractually agreed	Payment not applicable
Performance-based components				
Short-term bonus	For the CEO and the Chief Officers of the functions: Free cash flow (FCF Group) and Schaeffler Value Added (SVA Group) at group level (weighted equally). For the divisional CEOs: Free cash flow (FCF Group) and Schaeffler Value Added (SVA Group) at group level as well as Schaeffler Value Added (SVA Division) and cash flow (CF Division) at division level (weighted equally)	0% –150%	Meeting annual performance targets	Annually
Long-term bonus	Share price trend of Schaeffler common non-voting shares and meeting targets consisting of:	Maximum is the number of PSUs granted, minimum number is nil		
Performance Share Unit Plan (PSUP)	50% service condition and 25% relative Total-Shareholder-Return-(TSR)-based performance target and 25% cumulative FCF-based performance target	Share price cap: double the share price at grant date	Meeting service condition and/or performance targets	4 years after grant date
Retirement benefits			Retirement or triggering event	Generally monthly

Non-performance-based components

Fixed remuneration

Each ordinary member of the Board of Managing Directors receives an identical amount of fixed remuneration; the Chief Executive Officer receives twice this amount. Fixed remuneration is paid in twelve equal installments each month.

Fringe benefits

Fringe benefits include the use of a company car, including for private purposes, and customary insurance benefits such as directors' and officers' liability insurance (D&O insurance). This D&O insurance policy includes a deductible provision that is in accordance with section 93 (2) (3) AktG. Tax on the pecuniary advantage related to fringe benefits granted is paid individually by each member of the Board of Managing Directors. No loans were granted to members of the Board of Managing Directors in 2017.

Performance-based components

Short-term variable component – short-term bonus

All members of the Board of Managing Directors receive an annual short-term bonus if the relevant targets are met. The employment contracts of the members of the Board of Managing Directors set out the individual target-based bonus based on achievement of 100% of the performance targets.

The Supervisory Board determines the performance target tiers including the minimum and maximum targets on an annual basis. The performance targets underlying the remuneration reflect the strategic direction of the Schaeffler Group. The amount of the short-term bonus payable to the CEO and the Chief Officers of the functions is determined based on the extent to which the performance targets have been met. The performance targets are weighted equally and consist of free cash flow (FCF Group) of the Schaeffler Group and Schaeffler Value Added (SVA Group) of the Schaeffler Group. For the divisional CEOs, the performance targets used to determine the extent to which performance targets have been met consist of free cash flow of the Schaeffler Group (FCF Group) and Schaeffler Value Added of the Schaeffler Group (SVA Group) and of Schaeffler Value Added of the division (SVA Division) as well as cash flow of the division (CF Division), again weighted equally.

FCF Group is generally calculated based on the Schaeffler Group's cash flows from operating activities and from investing activities for the relevant year. SVA Group is generally based on the Schaeffler Group's EBIT less its cost of capital. SVA Division is determined in the same manner based on measures segmented in accordance with IFRS 8. The CF Division performance target is calculated as the sum of EBIT plus depreciation, amortization, and impairment losses plus change in working capital less additions to property, plant and equipment and intangible assets.

The Supervisory Board can set other strategic targets in addition to the FCF, SVA, and CF performance targets. Furthermore, the Supervisory Board can establish a multiplier ranging from 0.8 to 1.2 to reflect a Managing Director's individual performance. The short-term bonus may lapse in its entirety if the minimum targets are not met. In the event that maximum targets are exceeded, payment of all short-term bonuses is limited to 150% of the individual target-based bonus, regardless of whether an additional strategic target is set or a multiplier reflecting a Managing Director's individual performance is applied. The short-term bonus earned during a year is paid in a lump sum once the extent to which targets have been met has been determined.

Long-term variable component – long-term bonus (Performance Share Unit Plan, PSUP)

The Supervisory Board has implemented a share-based remuneration instrument in the form of a PSUP in order to align the interests of the Board of Managing Directors with those of the shareholders and to promote the sustainable development of the Schaeffler Group.

One performance share unit (PSU) conveys the right to a cash payment amounting to the average share price of the last 60 trading days of the performance period provided the previously defined target amounts are achieved. The PSUP is granted in annual tranches. Each tranche has a performance period of four years beginning on January 01 of the year it is granted. The target amount per tranche is stipulated in the employment contracts of the members of the Board of Managing Directors and is designed to create a remuneration structure that is largely oriented toward the long term. The target amount of the variable long-term remuneration exceeds the target bonus under the variable short-term remuneration. In addition, the number of PSUs granted to each individual member of the Board of Managing Directors is based on that member's duties and responsibilities. The number of PSUs granted at any one date as part of a tranche remains constant.

Vesting of PSUs is linked to the following three conditions:

- 50% of PSUs (base number) are granted subject to a service condition. The base number is only paid out if the member of the Board of Managing Directors remains employed as a member of a governing body of Schaeffler AG and is not under notice of termination at the end of the performance period.[3]
- 25% of the PSUs are granted subject to a long-term FCF-based performance target which involves a comparison of cumulative FCF for the performance period to the target FCF.
- 25% of the PSUs are granted subject to a relative performance target based on total shareholder return (TSR) (share price performance including dividends). To determine to what extent these PSUs have vested, TSR for Schaeffler AG's common non-voting shares is compared to the TSR of companies in the benchmark group (MDAX) over the vesting period.

The Supervisory Board sets the FCF- and TSR-based target amounts for each tranche when PSUs are granted.

[3] Taking into account the rules applicable to leavers.

The 2015, 2016, and 2017 tranches of PSUs subject to FCF- and TSR-based performance targets vest based on the following target tiers.

PSUP performance targets (1) No. 072

Cumulative FCF for the performance period	Number of FCF PSUs vested in %
Cumulative FCF compared to target-FCF > ~ 6.01%	100%
2.01% < cumulative FCF compared to target-FCF < ~ 6.00%	75%
-2.00% < cumulative FCF compared to target-FCF < ~ 2.00%	50%
-6.00% < cumulative FCF compared to target-FCF < ~ -2.01%	25%
Cumulative FCF compared to target-FCF < ~ -6.01%	0%

PSUP performance targets (2) No. 073

TSR outperformance over the performance period	Number of TSR PSUs vested in %
> 25%	100%
5% < TSR outperformance ≤ 25%	75%
-5% < TSR outperformance ≤ 5%	50%
-25% < TSR outperformance ≤ -5%	25%
≤ -25%	0%

The target amounts for the FCF-based performance target are derived from the Schaeffler Group's medium-term plan. The payment under a PSU is capped at double the underlying share price at the grant date.

The underlying share price of the 2017 tranche is EUR 13.18. The PSUs granted to each individual and the related fair values in 2017 are as follows:

PSUs granted in 2017 [1] No. 074

	Target amount (in € thousands)	Number of PSUs outstanding on December 31, 2017 [1]	Grant date fair value per PSU (in €)	Grant date fair value (in € thousands)
Klaus Rosenfeld (CEO)	1,300			
Base number of PSUs		49,316	11.84	584
FCF PSUs		24,659	11.84	292
TSR PSUs		24,659	6.99	172
Prof. Dr. Peter Gutzmer	950			
Base number of PSUs		36,039	11.84	427
FCF PSUs		18,020	11.84	213
TSR PSUs		18,020	6.99	126
Dietmar Heinrich [2]	271			
Base number of PSUs		10,275	10.67	110
FCF PSUs		5,137	10.67	55
TSR PSUs		5,137	4.58	24
Oliver Jung	950			
Base number of PSUs		36,039	11.84	427
FCF PSUs		18,020	11.84	213
TSR PSUs		18,020	6.99	126
Prof. Dr. Peter Pleus	950			
Base number of PSUs		36,039	11.84	427
FCF PSUs		18,020	11.84	213
TSR PSUs		18,020	6.99	126
Corinna Schittenhelm	650			
Base number of PSUs		24,659	11.84	292
FCF PSUs		12,329	11.84	146
TSR PSUs		12,329	6.99	86
Dr. Stefan Spindler	800			
Base number of PSUs		30,348	11.84	359
FCF PSUs		15,175	11.84	180
TSR PSUs		15,175	6.99	106
Matthias Zink	650			
Base number of PSUs		24,659	11.84	292
FCF PSUs		12,329	11.84	146
TSR PSUs		12,329	6.99	86
Managing Directors who left the company in 2017				
Dr. Ulrich Hauck [3]	800			
Base number of PSUs		30,348	11.84	359
FCF PSUs		15,175	11.84	180
TSR PSUs		15,175	6.99	106
Total	**7,321**	**555,450**	**-**	**5,873**

[1] Equals the number of PSUs granted on January 01, 2017 (on July 17, 2017 for Dietmar Heinrich).
[2] Dietmar Heinrich has been a member of the Board of Managing Directors of Schaeffler AG since August 01, 2017.
[3] Dr. Ulrich Hauck left the Board of Managing Directors of Schaeffler AG as at July 31, 2017. His employment agreement remains in effect until March 31, 2018.

The underlying share price of the 2016 tranche is EUR 14.58. The PSUs granted to each individual and the related fair values in 2016 are as follows:

PSUs granted in 2016 [1]

No. 075

	Target amount (in € thousands)	Number of PSUs outstanding on December 31, 2016 [1]	Grant date fair value per PSU (in €)	Grant date fair value (in € thousands)
Klaus Rosenfeld (CEO)	1,300			
Base number of PSUs		44,581	13.82	616
FCF PSUs		22,291	13.82	308
TSR PSUs		22,291	9.13	204
Prof. Dr. Peter Gutzmer	950			
Base number of PSUs		32,578	13.82	450
FCF PSUs		16,290	13.82	225
TSR PSUs		16,290	9.13	149
Dr. Ulrich Hauck	800			
Base number of PSUs		27,434	13.82	379
FCF PSUs		13,718	13.82	190
TSR PSUs		13,718	9.13	125
Oliver Jung	950			
Base number of PSUs		32,578	13.82	450
FCF PSUs		16,290	13.82	225
TSR PSUs		16,290	9.13	149
Prof. Dr. Peter Pleus	950			
Base number of PSUs		32,578	13.82	450
FCF PSUs		16,290	13.82	225
TSR PSUs		16,290	9.13	149
Corinna Schittenhelm	650			
Base number of PSUs		22,290	13.82	308
FCF PSUs		11,146	13.82	154
TSR PSUs		11,146	9.13	102
Dr. Stefan Spindler	800			
Base number of PSUs		27,434	13.82	379
FCF PSUs		13,718	13.82	190
TSR PSUs		13,718	9.13	125
Managing Directors who left the company in 2016				
Norbert Indlekofer [2]	950			
Base number of PSUs		32,578	13.82	450
FCF PSUs		16,290	13.82	225
TSR PSUs		16,290	9.13	149
Total	**7,350**	**504,117**	**-**	**6,376**

[1] Equals the number of PSUs granted on January 01, 2016.
[2] Norbert Indlekofer left the Board of Managing Directors of Schaeffler AG as at December 31, 2016.

The PSUs granted are classified and measured as cash-settled share-based compensation. The fair value for PSUs subject to the TSR-based performance target was determined using a binomial model. The fair value of the base number and of the PSUs subject to the FCF-based performance target was determined based on the price of the company's common non-voting shares as at the measurement date. The valuation model takes into account the terms of the contract under which the PSUs were granted (including payment floors and caps, target tiers, expected dividend payments, as well as the volatility of the company's common non-voting shares and of the benchmark index).

The valuation as at the grant date of the 2017 tranche (prior year: 2016 tranche) reflects the following input parameters:

- risk-free interest rate for the remaining performance period of -0.16% (prior year: 0.15%) for a January 01, 2017 grant date, -0.04% for a July 17, 2017 grant date;
- expected dividend yield of Schaeffler AG common non-voting shares over the performance period of 2.49% (prior year: 2.15%) for a January 01, 2017 grant date, 4.01% for a July 17, 2017 grant date,
- expected volatility of Schaeffler AG common non-voting shares of 34.27% (prior year: 33.02%) for a January 01, 2017 grant date, 28.78% for a July 17, 2017 grant date,
- expected volatility of the benchmark index of 18.75% (prior year: 19.56%) for a January 01, 2017 grant date, 10.62% for a July 17, 2017 grant date,
- expected correlation coefficient between the benchmark index and Schaeffler AG common non-voting shares of 0.61 (prior year: 0.43) for a January 01, 2017 grant date, 0.48 for a July 17, 2017 grant date.

Retirement benefits

All current members of the Board of Managing Directors hold retirement benefit commitments. The pension resulting from the various individual retirement benefit commitments is generally calculated as a percentage of pensionable remuneration based on the duration of the individual's service on the Board of Managing Directors. Individual percentages vary between 1.5% and 3.0% per year of membership on the Board of Managing Directors. Pension commitments for each member of the Board of Managing Directors are tailored individually. The pension received by a member of the Board of Managing Directors is based on their last pensionable employment income before retirement. Individual maximum pensions range from 40% to 60% of pensionable employment income.

Pension payments commence in the form of retirement benefits if employment ends at or after attainment of the age of 65, and in the form of disability benefits if employment ends due to disability. Beneficiaries are entitled to claim a reduced pension early as a retirement benefit beginning at age 60. Upon the death of the member of the Board of Managing Directors, the spouse is entitled to between 50% and 60% of the pension as a surviving dependants' pension. Surviving dependent children are entitled to 10% or 20% of the pension as a half- or full-orphan's pension, respectively.

The pension increases by 1.0% each year beginning at retirement. The pension of one member of the Board of Managing Directors is subject to annual increases by the same percentage as the consumer price index in Germany. This also applies to disability, widows', and orphans' pensions.

The following tables summarize the service cost and defined benefit obligation of pension benefits earned up to December 31, 2017, calculated in accordance with IAS 19 and based on the beneficiary's current age and years of service.

Service cost for 2017 and defined benefit obligations as at December 31, 2017 in accordance with IAS 19 No. 076

in € thousands	Year	Service cost	Defined benefit obligation
Klaus Rosenfeld (CEO)	2017	1,331	10,952
Prof. Dr. Peter Gutzmer	2017	0	4,569
Dietmar Heinrich [1]	2017	114	546
Oliver Jung	2017	307	2,891
Prof. Dr. Peter Pleus	2017	383	6,097
Corinna Schittenhelm	2017	326	651
Dr. Stefan Spindler	2017	308	680
Matthias Zink	2017	317	799
Managing Directors who left the company in 2017			
Dr. Ulrich Hauck [2]	2017	-949	0
Total		**2,137**	**27,185**

[1] Dietmar Heinrich has been a member of the Board of Managing Directors of Schaeffler AG since August 01, 2017.
[2] Dr. Ulrich Hauck left the Board of Managing Directors of Schaeffler AG as at July 31, 2017. His employment agreement remains in effect until March 31, 2018.

Service cost for 2016 and defined benefit obligations as at December 31, 2016 in accordance with IAS 19 No. 077

in Tsd. EUR	Year	Service cost	Defined benefit obligation
Klaus Rosenfeld (CEO)	2016	1,158	10,387
Prof. Dr. Peter Gutzmer	2016	287	4,840
Dr. Ulrich Hauck	2016	458	949
Oliver Jung	2016	272	2,750
Prof. Dr. Peter Pleus	2016	357	6,092
Corinna Schittenhelm	2016	319	326
Dr. Stefan Spindler	2016	250	517
Managing Directors who left the company in 2016			
Norbert Indlekofer [1]	2016	194	5,049
Total		**3,295**	**30,910**

[1] Norbert Indlekofer left the Board of Managing Directors of Schaeffler AG as at December 31, 2016.

Change in remuneration system

When the new remuneration system for the Board of Managing Directors went into effect in 2015, any members of the Board of Managing Directors already in office in 2015 and whose term in office extended beyond December 31, 2015 were granted a one-time sign-on bonus to offset the shortfall in liquidity caused by the change. The sign-on bonuses were paid in equal installments in October 2015 and October 2016.

In addition, the company has committed to pay two Managing Directors advances of EUR 300 thousand each for 2017 and payments of EUR 300 thousand and EUR 225 thousand, respectively, for 2018, and has also committed to pay EUR 300 thousand to one of these Managing Directors for 2019; these payments will be offset against payment of the long-term bonuses granted in 2017, 2018, and 2019.

Benefits granted in connection with the termination of membership on the Board of Managing Directors

Payments made to a member of the Board of Managing Directors upon early termination of their employment agreement without due cause are limited to two years' remuneration (severance cap) and must not represent compensation for more than the remaining term of the employment agreement. The severance cap is generally calculated based on the total remuneration for the last full financial year and also on the expected total remuneration for the current year where applicable.

Members of the Board of Managing Directors whose employment has terminated are generally subject to a non-competition clause for a period of 2 years following termination of their employment agreement. In return, they are entitled to compensation in the amount of 50% of the average contractual remuneration granted to the member of the Board of Managing Directors for the last 12 months before the end of their employment. Such contractual remuneration includes both performance-based and non-performance-based remuneration components. Income from other employment is deducted from the compensation payment in accordance with section 74c HGB.

The employment agreements of Dietmar Heinrich and Matthias Zink, who were appointed to the Board of Managing Directors in 2017, and Corinna Schittenhelm, appointed to the Board of Managing Directors in 2016, include post-contract non-competition clauses calling for corresponding compensation.

Dr. Ulrich Hauck left Schaeffler AG's Board of Managing Directors early effective July 31, 2017. His employment agreement remains in effect until March 31, 2018. The post-contract non-competition clause was waived. The fixed remuneration including fringe benefits he will continue to receive amounts to a total of EUR 403 thousand and his proportionate short-term bonus for 2017 is EUR 291 thousand. In addition, the company agreed to pay Dr. Hauck the proportionate short-term bonus for 2018 (target bonus EUR 188 thousand) and a proportionate long-term bonus for 2018 (target bonus EUR 200 thousand). In connection with the waiver of the post-contract non-competition clause, the company will make payments for the period of approx. 4 months, in the amount of 50% of the average monthly contractual remuneration granted for the last 12 months before the end of Dr. Hauck's employment.

External activities of members of the Board of Managing Directors

The members of the Board of Managing Directors have agreed to work exclusively for the company. External activities, whether paid or unpaid, require prior approval by the executive committee of the Supervisory Board. This ensures that neither the time commitment involved nor the related remuneration conflict with the individual's responsibilities toward Schaeffler AG. External activities representing a position on legally required supervisory boards or similar supervisory bodies of commercial enterprises are listed in section 5 "Governing bodies of the company".

Appropriateness of the remuneration of the Board of Managing Directors

In accordance with section 87 AktG, the Supervisory Board of Schaeffler AG ensures that the remuneration of individual members of the Board of Managing Directors bears a reasonable relationship to the duties and performance of such member as well as the condition of the company. The Supervisory Board engaged Ernst & Young GmbH Wirtschaftsprüfungsgesellschaft to review the appropriateness of the Managing Directors' remuneration, most recently in 2016. Ernst & Young concluded that the total remuneration of the members of the Board of Managing Directors is customary and appropriate in comparison to that of other companies of comparable size within the same industry and country in terms of the amount, structure, and features of remuneration instruments.

4.2 Amounts of remuneration of the Board of Managing Directors

The fixed and variable components of remuneration are disclosed below. The following tables show the benefits granted and received for 2017 and 2016.

Benefits granted for 2017

	Klaus Rosenfeld				Prof. Dr. Peter Gutzmer				Dietmar Heinrich			
	Chief Executive Officer				Deputy Chief Executive Officer and Chief Technology Officer				Chief Financial Officer			
	since October 24, 2014				since October 24, 2014				since August 01, 2017			
in € thousands	**2016**	**2017**	**2017 (Min)**	**2017 (Max)**	**2016**	**2017**	**2017 (Min)**	**2017 (Max)**	**2016**	**2017**	**2017 (Min)**	**2017 (Max)**
Fixed remuneration	1,200	1,200	1,200	1,200	600	600	600	600	-	250	250	250
Fringe benefits	27	28	28	28	28	29	29	29	-	9	9	9
Total	**1,227**	**1,228**	**1,228**	**1,228**	**628**	**629**	**629**	**629**	**-**	**259**	**259**	**259**
One-year variable remuneration	1,200	1,200	0	1,800	900	900	0	1,350	-	250	0	375
Multi-year variable remuneration												
• Long-term bonus: PSUP (4 years) - 2015 tranche	-	-	-	-	-	-	-	-	-	-	-	-
• Long-term bonus: PSUP (4 years) - 2016 tranche	1,128	-	-	-	824	-	-	-	-	-	-	-
• Long-term bonus: PSUP (4 years) - 2017 tranche	-	1,048	0	2,600	-	766	0	1,900	-	189	0	542
Total	**3,555**	**3,476**	**1,228**	**5,628**	**2,352**	**2,295**	**629**	**3,879**	**-**	**698**	**259**	**1,176**
Pension expense	1,158	1,331	1,331	1,331	287	0	0	0	-	114	114	114
Total remuneration	**4,713**	**4,807**	**2,559**	**6,959**	**2,639**	**2,295**	**629**	**3,879**	**-**	**812**	**373**	**1,290**

Benefits received for 2017

	Klaus Rosenfeld		Prof. Dr. Peter Gutzmer		Dietmar Heinrich	
	Chief Executive Officer		Deputy Chief Executive Officer and Chief Technology Officer		Chief Financial Officer	
	since October 24, 2014		since October 24, 2014		since August 01, 2017	
in € thousands	**2017**	**2016**	**2017**	**2016**	**2017**	**2016**
Fixed remuneration	1,200	1,200	600	600	250	-
Sign-on bonus	-	600	-	300	-	-
Fringe benefits	28	27	29	28	9	-
Total	**1,228**	**1,827**	**629**	**928**	**259**	**-**
One-year variable remuneration	1,116	1,199	837	899	233	-
Multi-year variable remuneration						
• Long-term bonus: PSUP (4 years) - 2015 tranche	0	0	0	0	0	-
• Long-term bonus: PSUP (4 years) - 2016 tranche	0	0	0	0	0	-
• Long-term bonus: PSUP (4 years) - 2017 tranche	0	0	0	0	0	-
Total	**2,344**	**3,026**	**1,466**	**1,827**	**492**	**-**
Pension expense	1,331	1,158	0	287	114	-
Total remuneration	**3,675**	**4,184**	**1,466**	**2,114**	**606**	**-**

No. 078

Oliver Jung				Prof. Dr. Peter Pleus				Corinna Schittenhelm				Dr. Stefan Spindler				Matthias Zink			
Chief Operating Officer				CEO Automotive				Chief Human Resources Officer				CEO Industrial				CEO Automotive			
since October 24, 2014				since October 24, 2014				since January 01, 2016				since May 01, 2015				since January 01, 2017			
2016	**2017**	**2017 (Min)**	**2017 (Max)**	**2016**	**2017**	**2017 (Min)**	**2017 (Max)**	**2016**	**2017**	**2017 (Min)**	**2017 (Max)**	**2016**	**2017**	**2017 (Min)**	**2017 (Max)**	**2016**	**2017**	**2017 (Min)**	**2017 (Max)**
600	600	600	600	600	600	600	600	600	600	600	600	600	600	600	600	-	600	600	600
28	28	28	28	41	42	42	42	23	25	25	25	23	24	24	24	-	24	24	24
628	**628**	**628**	**628**	**641**	**642**	**642**	**642**	**623**	**625**	**625**	**625**	**623**	**624**	**624**	**624**	**-**	**624**	**624**	**624**
900	900	0	1,350	900	900	0	1,350	600	600	0	900	750	750	0	1,125	-	600	0	900
-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
824	-	-	-	824	-	-	-	564	-	-	-	694	-	-	-	-	-	-	-
-	766	0	1,900	-	766	0	1,900	-	524	0	1,300	-	645	0	1,600	-	524	0	1,300
2,352	**2,294**	**628**	**3,878**	**2,365**	**2,308**	**642**	**3,892**	**1,787**	**1,749**	**625**	**2,825**	**2,067**	**2,019**	**624**	**3,349**	**-**	**1,748**	**624**	**2,824**
272	307	307	307	357	383	383	383	319	326	326	326	250	308	308	308	-	317	317	317
2,624	**2,601**	**935**	**4,185**	**2,722**	**2,691**	**1,025**	**4,275**	**2,106**	**2,075**	**951**	**3,151**	**2,317**	**2,327**	**932**	**3,657**	**-**	**2,065**	**941**	**3,141**

No. 079

Oliver Jung		Prof. Dr. Peter Pleus		Corinna Schittenhelm		Dr. Stefan Spindler		Matthias Zink	
Chief Operating Officer		CEO Automotive		Chief Human Resources Officer		CEO Industrial		CEO Automotive	
since October 24, 2014		since October 24, 2014		since January 01, 2016		since May 01, 2015		since January 01, 2017	
2017	**2016**	**2017**	**2016**	**2017**	**2016**	**2017**	**2016**	**2017**	**2016**
600	600	600	600	600	600	600	600	600	-
-	300	-	300	-	-	-	300	-	-
28	28	42	41	25	23	24	23	24	-
628	**928**	**642**	**941**	**625**	**623**	**624**	**923**	**624**	**-**
837	899	778	862	558	599	608	522	518	-
0	0	0	0	0	0	0	0	0	-
0	0	0	0	0	0	0	0	0	-
0	0	0	0	0	0	0	0	0	-
1,465	**1,827**	**1,420**	**1,803**	**1,183**	**1,222**	**1,232**	**1,445**	**1,142**	**-**
307	272	383	357	326	319	308	250	317	-
1,772	**2,099**	**1,803**	**2,160**	**1,509**	**1,541**	**1,540**	**1,695**	**1,459**	**-**

Benefits granted for 2017 – Managing Directors who left the company

No. 080

	Dr. Ulrich Hauck Chief Financial Officer from April 01, 2015 to July 31, 2017			
in € thousands	2016	2017	2017 (Min)	2017 (Max)
Fixed remuneration	600	350	350	350
Fringe benefits	28	16	16	16
Total	**628**	**366**	**366**	**366**
One-year variable remuneration	750	438	0	656
Multi-year variable remuneration				
• Long-term bonus: PSUP (4 years) - 2015 tranche	-	-	-	-
• Long-term bonus: PSUP (4 years) - 2016 tranche	694	-	-	-
• Long-term bonus: PSUP (4 years) - 2017 tranche	-	645	0	1,600
Total	**2,072**	**1,449**	**366**	**2,622**
Pension expense	458	-949	-949	-949
Total remuneration	**2,530**	**500**	**-583**	**1,673**

Benefits received for 2017 – Managing Directors who left the company

No. 081

	Dr. Ulrich Hauck Chief Financial Officer from April 01, 2015 to July 31, 2017	
in € thousands	2017	2016
Fixed remuneration	350	600
Sign-on bonus	-	300
Fringe benefits	16	28
Total	**366**	**928**
One-year variable remuneration	407	749
Multi-year variable remuneration		
• Long-term bonus: PSUP (4 years) - 2015 tranche	0	0
• Long-term bonus: PSUP (4 years) - 2016 tranche	0	0
• Long-term bonus: PSUP (4 years) - 2017 tranche	0	0
Total	**773**	**1,677**
Pension expense	-949	458
Total remuneration	**- 176**	**2,135**

The total remuneration for 2017 and 2016 is broken down by individual and by its various components in accordance with section 285 (9a) HGB and section 314 (1) (6a) HGB below.

Total remuneration (HGB) for 2017 by individual

No. 082

	Remuneration components			
in € thousands	fixed	variable, short-term	variable, long-term [1]	Total remuneration
Klaus Rosenfeld (CEO)	1,228	1,116	1,048	3,392
Prof. Dr. Peter Gutzmer	629	837	766	2,232
Dietmar Heinrich [2]	259	233	189	681
Oliver Jung	628	837	766	2,231
Prof. Dr. Peter Pleus	642	778	766	2,186
Corinna Schittenhelm	625	558	524	1,707
Dr. Stefan Spindler	624	608	645	1,877
Matthias Zink	624	518	524	1,666
Managing Directors who left the company in 2017				
Dr. Ulrich Hauck [3]	366	407	645	1,418
Total	**5,625**	**5,892**	**5,873**	**17,390**

[1] Share-based payment in the form of the PSUP.
[2] Dietmar Heinrich has been a member of the Board of Managing Directors of Schaeffler AG since August 01, 2017.
[3] Dr. Ulrich Hauck left the Board of Managing Directors of Schaeffler AG as at July 31, 2017. His employment agreement remains in effect until March 31, 2018.

Total remuneration (HGB) for 2016 by individual

No. 083

	Remuneration components			
in € thousands	fixed	variable, short-term	variable, long-term [1]	Total remuneration
Klaus Rosenfeld (CEO)	1,227	1,199	1,128	3,554
Prof. Dr. Peter Gutzmer	628	899	824	2,351
Dr. Ulrich Hauck	628	749	694	2,071
Oliver Jung	628	899	824	2,351
Prof. Dr. Peter Pleus	641	862	824	2,327
Corinna Schittenhelm	623	599	564	1,786
Dr. Stefan Spindler	623	522	694	1,839
Managing Directors who left the company in 2016				
Norbert Indlekofer [2]	625	862	824	2,311
Total	**5,623**	**6,591**	**6,376**	**18,590**

[1] Share-based payment in the form of the PSUP.
[2] Norbert Indlekofer left the Board of Managing Directors of Schaeffler AG as at December 31, 2016.

The total expenses resulting from the PSUP for 2017 are broken down by individual in accordance with section 314 (1) (6a) (8) HGB in connection with IFRS 2.51a below.

PSUP expenses in 2017

No. 084

in € thousands	Expenses (IFRS)
Klaus Rosenfeld (CEO)	669
Prof. Dr. Peter Gutzmer	489
Dietmar Heinrich [1]	21
Oliver Jung	837
Prof. Dr. Peter Pleus	489
Corinna Schittenhelm	196
Dr. Stefan Spindler	355
Matthias Zink	101
Managing Directors who left the company	
Dr. Ulrich Hauck [2]	1,090
Total	**4,247**

[1] Dietmar Heinrich has been a member of the Board of Managing Directors of Schaeffler AG since August 01, 2017.
[2] Dr. Ulrich Hauck left the Board of Managing Directors of Schaeffler AG as at July 31, 2017. His employment agreement remains in effect until March 31, 2018.

The total expenses resulting from the PSUP for 2017 are broken down by individual in accordance with section 314 (1) (6a) (8) HGB in connection with IFRS 2.51a below.

PSUP expenses in 2016

No. 085

in € thousands	Aufwendungen (IFRS)
Klaus Rosenfeld (CEO)	402
Prof. Dr. Peter Gutzmer	293
Dr. Ulrich Hauck	213
Oliver Jung	293
Prof. Dr. Peter Pleus	184
Corinna Schittenhelm	88
Dr. Stefan Spindler	201
Managing Directors who left the company	
Norbert Indlekofer [1]	948
Total	**2,622**

[1] Norbert Indlekofer left the Board of Managing Directors of Schaeffler AG as at December 31, 2016.

4.3 Remuneration of the Supervisory Board

The description of the remuneration of the Supervisory Board includes the disclosures required by German commercial law and is consistent with the recommendations of the GCGC. The remuneration of the Supervisory Board was set by a resolution passed by the general meeting on December 01, 2014.

The members of the Supervisory Board of Schaeffler AG receive fixed remuneration of EUR 50,000 per year. The Chairman of the Supervisory Board receives twice this amount, his Deputies 1.5 times this amount. In addition, membership on committees is compensated as follows:

- Executive committee; committee remuneration of EUR 20,000 for each ordinary member, twice this amount for the chairman.
- Audit committee; committee remuneration for each ordinary member of EUR 20,000, twice this amount for the chairman.

Where a member of the Supervisory Board chairs several committees or chairs both the Supervisory Board and one or more committees, no remuneration is paid for the additional chairmanship. Where the term of office of a member of the Supervisory Board or the position entitling the Supervisory Board member to increased remuneration begins or ends during the year, the remuneration or increased remuneration paid to the Supervisory Board member is prorated.

In addition, each member of the Supervisory Board receives an attendance fee of EUR 1,500 for each meeting of the Supervisory Board or its committees he or she attends in person. No attendance fees are paid where meetings of the Supervisory Board or its committees are attended via telephone.

Members of the Supervisory Board are reimbursed for expenses incurred in connection with the performance of their duties and for any value-added tax on their remuneration and expenses.

The company has obtained director's and officers' liability insurance (D&O insurance) for all members of the Supervisory Board; the features of the policy's deductible provision are in accordance with section 93 (3) (3) AktG.

No advances or loans were granted to members of the Supervisory Board in 2017 or 2016. The following tables summarize the amount of remuneration of each member of the Supervisory Board.

Supervisory Board remuneration for 2017 [1)] No. 086

in € thousands	Fixed remuneration	Remuneration for committee membership	Attendance fees [2)]	Total remuneration
Bullinger, Prof. Dr. Hans-Jörg	50		8	58
Engelmann, Dr. Holger	50		6	56
Gottschalk, Prof. Dr. Bernd	50		6	56
Grimm, Andrea (since April 08, 2017) [3)]	36		6	42
Lenhard, Norbert [3)]	50	20	12	82
Luther, Dr. Siegfried	50	40	14	104
Mittag, Dr. Reinold [3)]	50	20	14	84
Münch, Yvonne (until March 07, 2017) [3)]	9		2	11
Resch, Barbara [3)]	50	20	12	82
Schaeffler, Georg F. W.	100	40	15	155
Schaeffler-Thumann, Maria-Elisabeth	75	20	3	98
Schmidt, Stefanie [3)]	50		8	58
Spindler, Dirk	50		8	58
Stalker, Robin	50	20	14	84
Stolz, Jürgen [3)]	50		8	58
Vicari, Salvatore [3)]	50	20	14	84
Wechsler, Jürgen [3)]	75	20	11	106
Wiesheu, Dr. Otto	50		8	58
Wolf, Prof. KR Ing. Siegfried	50	20	11	81
Worrich, Jürgen [3)]	50	20	14	84
Zhang, Prof. Dr.-Ing. Tong	50		6	56
Total	**1,095**	**260**	**200**	**1,555**

1) All amounts shown exclude any value-added tax applicable on remuneration. The positions held by the Supervisory Board members are listed in section 5 "Governing bodies of the company".
2) No attendance fees are paid where meetings of the Supervisory Board or its committees are attended via telephone.
3) These employee representatives have declared that their board remuneration is transferred to the Hans Böckler Foundation in accordance with the guidelines issued by the German Federation of Trade Unions.

Supervisory Board remuneration for 2016 [1)] No. 087

in € thousands	Fixed remune-ration	Remune-ration for committee member-ship	Attendance fees [2)]	Total remune-ration
Bullinger, Prof. Dr. Hans-Jörg	50		6	56
Engelmann, Dr. Holger	50		6	56
Gottschalk, Prof. Dr. Bernd	50		6	56
Lenhard, Norbert [3)]	50	20	11	81
Luther, Dr. Siegfried	50	40	14	104
Mittag, Dr. Reinold [3)]	50	20	14	84
Münch, Yvonne [3)]	50		8	58
Resch, Barbara [3)]	50	20	12	82
Schaeffler, Georg F. W.	100	40	12	152
Schaeffler-Thumann, Maria-Elisabeth	75	20	6	101
Schmidt, Stefanie [3)]	50		6	56
Spindler, Dirk	50		8	58
Stalker, Robin	50	20	12	82
Stolz, Jürgen [3)]	50		8	58
Vicari, Salvatore [3)]	50	20	12	82
Wechsler, Jürgen [3)]	75	20	11	106
Wiesheu, Dr. Otto	50		6	56
Wolf, Prof. KR Ing. Siegfried	50	20	8	78
Worrich, Jürgen [3)]	50	20	14	84
Zhang, Prof. Dr.-Ing. Tong	50		8	58
Total	**1,100**	**260**	**188**	**1,548**

1) All amounts shown exclude any value-added tax applicable on remuneration. The positions held by the Supervisory Board members are listed in section 5 “Governing bodies of the company”.
2) No attendance fees are paid where meetings of the Supervisory Board or its committees are attended via telephone.
3) These employee representatives have declared that their board remuneration is transferred to the Hans Böckler Foundation in accordance with the guidelines issued by the German Federation of Trade Unions.

Members of the Supervisory Board have not received any compensation for personal services, especially consulting and agency services, in 2017 or 2016.

5. Governing bodies of the company

5.1 Supervisory Board

The Supervisory Board consists of twenty members. Ten of these members are appointed by a resolution of the annual general meeting, and ten members are elected by the employees in accordance with the requirements of the German Co-Determination Act. The term of office of the shareholder representatives on the Supervisory Board ends at the conclusion of the annual general meeting 2019. The term of office of the employee representatives ends at the conclusion of the annual general meeting 2020.

Georg F. W. Schaeffler

Shareholder of INA-Holding Schaeffler GmbH & Co. KG
Chairman of the Supervisory Board of Schaeffler AG

Appointed: December 01, 2014
Committee memberships: chairman of the mediation, executive, and nomination committees and member of the audit committee
Seats on supervisory and similar boards: member of the supervisory board of Continental AG, Hanover

Maria-Elisabeth Schaeffler-Thumann

Shareholder of INA-Holding Schaeffler GmbH & Co. KG
Deputy Chairperson of the Supervisory Board of Schaeffler AG

Appointed: December 01, 2014
Committee memberships: member of the mediation, executive, and nomination committees
Seats on supervisory and similar boards: member of the supervisory board of Continental AG, Hanover

Jürgen Wechsler*

Regional Director of IG Metall Bavaria
Deputy Chairman of the Supervisory Board of Schaeffler AG

Appointed: November 19, 2015
Committee memberships: member of the mediation and executive committees
Seats on supervisory and similar boards: member of the supervisory board of BMW AG, Munich; deputy chairman of the supervisory board of Siemens Healthcare GmbH, Munich

Prof. Dr. Hans-Jörg Bullinger

Senator of Fraunhofer-Gesellschaft zur Förderung angew. Forschung e.V.

Appointed: December 01, 2014
Seats on supervisory and similar boards: chairman of the supervisory board of ARRI AG, Munich; member of the supervisory board of Bauerfeind AG, Zeulenroda-Triebes; chairman of the supervisory board of TÜVSÜD AG, Munich; deputy chairman of the supervisory board of WILO SE, Dortmund; member of the board of directors of Kärcher GmbH & Co. KG, Winnenden

Dr. Holger Engelmann

Chairman of the Management Board of Webasto SE

Appointed: December 01, 2014
Committee memberships: member of the nomination committee
Seats on supervisory and similar boards: chairman of the supervisory board of Webasto Thermo & Comfort SE, Gilching

* Employee representative on the Supervisory Board.

Prof. Dr. Bernd Gottschalk
Owner and Managing Partner of AutoValue GmbH

Appointed: December 01, 2014
Committee memberships: member of the nomination committee
Seats on supervisory and similar boards: deputy chairman of the supervisory board of JOST-Werke Deutschland GmbH, Neu-Isenburg; member of the supervisory board of Plastic Omnium SA, Levallois-Perret, France; chairman of the advisory board of Woco Industrietechnik GmbH, Bad Soden-Salmünster

Andrea Grimm* (since April 08, 2017)
Controller

Appointed: April 08, 2017

Norbert Lenhard*
Chairman of the central Works Council of Schaeffler Technologies AG & Co. KG; Chairman of the Works Council at the Schweinfurt plant

Appointed: November 19, 2015
Committee memberships: member of the mediation and executive committees

Dr. Siegfried Luther
Management Consultant

Appointed: December 01, 2014
Committee memberships: chairman of the audit committee
Seats on supervisory and similar boards: chairman of the audit committee of Evonik Industries AG, Essen; member of the board of directors of Sparkasse Gütersloh-Riethberg, Gütersloh

Dr. Reinold Mittag*
Trade Union Secretary of IG Metall

Appointed: November 19, 2015
Committee memberships: member of the audit committee

Barbara Resch*
Wage coordinator

Appointed: November 19, 2015
Committee memberships: member of the executive committee

Stefanie Schmidt*
Chairperson of the Works Council at the Wuppertal plant

Appointed: November 19, 2015

Dirk Spindler*
Senior Vice President R&D Processes, Methods and Tools of Schaeffler AG

Appointed: November 19, 2015

Robin Stalker
Chartered Accountant

Appointed: December 01, 2014
Committee memberships: member of the audit committee
Seats on supervisory and similar boards: deputy chairman of the supervisory board of Schmitz Cargobull AG, Horstmar (since November 30, 2017)

Jürgen Stolz*
Deputy Chairman of the Group Works Council;
member of the Works Council at the Buehl plant

Appointed: November 19, 2015

Salvatore Vicari*
Chairman of the Works Council at the Homburg/Saar plant

Appointed: November 19, 2015
Committee memberships: member of the audit committee
Seats on supervisory and similar boards: member of the supervisory board of GEW-Management GmbH, Homburg (since June 01, 2017)

Dr. Otto Wiesheu
Lawyer

Appointed: December 01, 2014

Prof. KR Ing. Siegfried Wolf
Chairman of the Board of Directors of Russian Machines LLC

Appointed: December 01, 2014
Committee memberships: member of the executive committee
Seats on supervisory and similar boards: member of the supervisory board of Banque Eric Sturdza SA, Geneva, Switzerland; member of the supervisory board of Continental AG, Hanover; chairman of the supervisory board of GAZ Group, Nizhny Novgorod, Russia; member of the supervisory board of Miba AG, Mitterbauer Beteiligungs AG, Laakirchen, Austria; chairman of the supervisory board of SBERBANK Europe AG, Vienna, Austria; member of the supervisory board of UC RUSAL Plc, Nicosia, Cyprus

* Employee representative on the Supervisory Board.

Jürgen Worrich*

Chairman of the European Schaeffler Works Council; member of the Works Council at the Herzogenaurach plant

Appointed: November 19, 2015
Committee memberships: member of the audit committee

Prof. Dr.-Ing. Tong Zhang

Director Clean Energy Automotive Engineering Center at Tongji University in Shanghai, China

Appointed: December 01, 2014

The following member left the Supervisory Board in 2017

Yvonne Münch* (until March 07, 2017)

Manager Plant Purchase and Logistics

Appointed: November 19, 2015
Term of office ended: March 07, 2017

5.2 Supervisory Board committees

Mediation committee

Georg F. W. Schaeffler (Chairman), Norbert Lenhard, Maria-Elisabeth Schaeffler-Thumann, and Jürgen Wechsler

Executive committee

Georg F. W. Schaeffler (Chairman), Norbert Lenhard, Barbara Resch, Maria-Elisabeth Schaeffler-Thumann, Jürgen Wechsler, and Prof. KR Ing. Siegfried Wolf

Audit committee

Dr. Siegfried Luther (Chairman), Dr. Reinold Mittag, Georg F. W. Schaeffler, Robin Stalker, Salvatore Vicari, and Jürgen Worrich

Nomination committee

Georg F. W. Schaeffler (Chairman), Dr. Holger Engelmann, Prof. Dr. Bernd Gottschalk, and Maria-Elisabeth Schaeffler-Thumann

5.3 Board of Managing Directors

The Schaeffler Group is managed by the Board of Managing Directors of Schaeffler AG. The Board of Managing Directors currently has nine members: the Chief Executive Officer (CEO), the CEOs of the Automotive OEM, Automotive Aftermarket, and Industrial divisions, and the Managing Directors responsible for the functions (1) Technology , (2) Operations, (3) Finance, and (4) Human Resources. Together, the Board of Managing Directors and the Regional CEOs represent the Schaeffler Group's Executive Board.

Klaus Rosenfeld

Chief Executive Officer

Responsible for: Quality; Schaeffler Consulting; Communications & Branding; Investor Relations; Legal; Internal Audit; Business Development & Strategy; Compliance & Corporate Security; Corporate Real Estate
Appointed: October 24, 2014
Term of office ends: June 30, 2019
Seats on supervisory and similar boards: member of the supervisory board of Continental AG, Hanover; member of the board of directors of Schaeffler Holding (China) Co. Ltd., Shanghai, China; member of the board of directors of Schaeffler India Ltd., Vadodara, India; member of the board of directors of Siemens Gamesa Renewable Energy S.A., Zamudio, Spain (since April 03, 2017)

Prof. Dr.-Ing. Peter Gutzmer

Deputy CEO and Chief Technology Officer

Responsible for: Corporate R&D Management; Technology Strategy & Innovation; R&D Processes, Methods & Tools; R&D Competence & Services; Intellectual Property Rights; Surface Technology; Information Technology; Strategic IT; Coordination Office Digitalization
Appointed: October 24, 2014
Term of office ends: December 31, 2019
Seats on supervisory and similar boards: member of the supervisory board of Continental AG, Hanover

* Employee representative on the Supervisory Board.

Dietmar Heinrich (since August 01, 2017)

Chief Financial Officer

Responsible for: Finance Strategy, Processes & Infrastructure; Corporate Accounting; Corporate Controlling; Corporate Treasury; Corporate Taxes; Corporate Insurance; Divisional Controlling Automotive OEM, AAM, and Industrial divisions;
Appointed: August 01, 2017
Term of office ends: July 31, 2020
Seats on supervisory and similar boards: member of the supervisory board of FAG Magyarorszag Ipari Kft., Debrecen, Hungary (until November 30, 2017); member of the supervisory board of LuK Savaria Kft., Szombathely, Hungary (until January 08, 2018); member of the supervisory board of Schaeffler Austria GmbH, Berndorf-St. Veit, Austria; member of the board of directors of Schaeffler India Ltd., Vadodara, India; member of the supervisory board of Schaeffler Kysuce, spol. s r.o., Kysucké Nové Mesto, Slovakia (until December 12, 2017); member of the supervisory board of Schaeffler Skalica, spol. s r.o., Skalica, Slovakia (until December 12, 2017))

Oliver Jung

Chief Operating Officer

Responsible for: Operations Strategy & Processes; Production Technology; Special Machinery; Tool Management & Prototyping; Industrial Engineering; Bearing & Components Technologies; Logistics; Purchasing; MOVE
Appointed: October 24, 2014
Term of office ends: September 30, 2018
Seats on supervisory and similar boards: member of the supervisory board of FAG Magyarorszag Ipari Kft., Debrecen, Hungary; member of the supervisory board of Heidelberger Druckmaschinen AG, Heidelberg (since May 23, 2017); chairman of the supervisory board of Schaeffler Austria GmbH, Berndorf-St. Veit, Austria; member of the supervisory board of SupplyOn AG, Munich

Prof. Dr. Peter Pleus

CEO Automotive OEM

Responsible for: Strategy & Business Development Automotive OEM; Global Key Account Management Automotive OEM; Engine Systems and Chassis Systems business divisions
Appointed: October 24, 2014
Term of office ends: December 31, 2018
Seats on supervisory and similar boards: member of the supervisory board of IAV GmbH, Berlin

Corinna Schittenhelm

Chief Human Resources Officer

Responsible for: HR Strategy; HR Policies & Standards; Leadership, Recruiting & Talent Management; Schaeffler Academy; HR Systems, Processes & Reporting; Environment, Health & Safety; Human Resources Functions; Human Resources Automotive OEM; Human Resources AAM; Human Resources Industrial
Appointed: January 01, 2016
Term of office ends: December 31, 2018

Michael Söding (since January 01, 2018)

CEO Automotive Aftermarket

Responsible for: Strategy & Business Development AAM; Sales & Marketing AAM; Product Management/R&D AAM; Operations & Supply Chain Management AAM
Appointed: January 01, 2018
Term of office ends: December 31, 2020

Dr. Stefan Spindler

CEO Industrial

Responsible for: Strategy & Business Development Industrial; Global Key Account Management Industrial; Sales & Marketing Industrial; Industry 4.0; R&D Industrial; Operations and Supply Chain Management Industrial
Appointed: May 01, 2015
Term of office ends: April 30, 2023
Seats on supervisory and similar boards: deputy chairman of the supervisory board of Schaeffler Austria GmbH, Berndorf-St. Veit, Austria

Matthias Zink

CEO Automotive OEM

Responsible for: Transmission Systems and E-Mobility business divisions; R&D Automotive OEM; Operations & Supply Chain Management Automotive OEM
Appointed: January 01, 2017
Term of office ends: December 31, 2019
Seats on supervisory and similar boards: member of the supervisory board of LuK Savaria Kft., Szombathely, Hungary (since March 30, 2017); member of the board of directors of Schaeffler (China) Co. Ltd., Shanghai, China

The following member left the Board of Managing Directors in 2017

Dr. Ulrich Hauck (since July 31, 2017)

Chief Financial Officer

Responsible for: Finance Strategy, Processes & Infrastructure; Corporate Accounting; Corporate Controlling; Corporate Treasury; Corporate Taxes; Divisional Controlling Automotive and Industrial divisions; Corporate Insurance
Appointed: April 01, 2015
Term of office ended: July 31, 2017
Seats on supervisory and similar boards: member of the supervisory board of mutares AG, Munich

Consolidated financial statements

1. Consolidated income statement

No. 088

in € millions	Note	2017	2016	Change in %
Revenue	3.1	14,021	13,338	5.1
Cost of sales		-10,175	-9,552	6.5
Gross profit		**3,846**	**3,786**	**1.6**
Research and development expenses		-846	-751	12.6
Selling expenses		-970	-915	6.0
Administrative expenses		-443	-428	3.5
Other income	3.2	82	41	100
Other expenses	3.3	-141	-177	-20.3
Earnings before financial result and income taxes (EBIT)		**1,528**	**1,556**	**-1.8**
Financial income	3.5	108	220	-50.9
Financial expenses	3.5	-300	-561	-46.5
Financial result	**3.5**	**-192**	**-341**	**-43.7**
Earnings before income taxes		**1,336**	**1,215**	**10.0**
Income taxes	3.6	-339	-343	-1.2
Net income		**997**	**872**	**14.3**
Attributable to shareholders of the parent company		980	859	14.1
Attributable to non-controlling interests		17	13	30.8
Earnings per common share (basic/diluted, in €)	3.7	1.47	1.29	14.0
Earnings per common non-voting share (basic/diluted, in €)	3.7	1.48	1.30	13.8

2. Consolidated statement of comprehensive income

No. 089

				2017			2016
in € millions	Note	before taxes	taxes	after taxes	before taxes	taxes	after taxes
Net income		**1,336**	**-339**	**997**	**1,215**	**-343**	**872**
Foreign currency translation differences for foreign operations		-270	0	-270	59	0	59
Net change from hedges of net investments in foreign operations	4.14	33	-10	23	-10	3	-7
Effective portion of changes in fair value of cash flow hedges [1)]	4.14	71	-21	50	-9	3	-6
Total other comprehensive income (loss) that may be reclassified subsequently to profit or loss		**-166**	**-31**	**-197**	**40**	**6**	**46**
Remeasurement of net defined benefit liability	4.11	120	-39	81	-223	63	-160
Total other comprehensive income (loss) that will not be reclassified to profit or loss		**120**	**-39**	**81**	**-223**	**63**	**-160**
Total other comprehensive income (loss)		**-46**	**-70**	**-116**	**-183**	**69**	**-114**
Total comprehensive income (loss)		**1,290**	**-409**	**881**	**1,032**	**-274**	**758**
Total comprehensive income (loss) attributable to shareholders of the parent company		1,271	-400	871	1,012	-267	745
Total comprehensive income (loss) attributable to non-controlling interests		19	-9	10	20	-7	13

[1)] Incl. losses of EUR 58 m (prior year: EUR 54 m) reclassified to profit and loss.

3. Consolidated statement of financial position

No. 090

in € millions	Note	12/31/2017	12/31/2016	Change in %
ASSETS				
Intangible assets	4.1	636	632	0.6
Property, plant and equipment	4.2	4,865	4,507	7.9
Other financial assets	4.6	114	217	-47.5
Other assets	4.6	71	51	39.2
Deferred tax assets	4.3	492	572	-14.0
Total non-current assets		**6,178**	**5,979**	**3.3**
Inventories	4.4	2,017	1,905	5.9
Trade receivables	4.5	2,192	2,218	-1.2
Other financial assets	4.6	111	55	> 100
Other assets	4.6	236	218	8.3
Income tax receivables	4.3	102	93	9.7
Cash and cash equivalents	4.7	698	1,071	-34.8
Assets held for sale	4.8	3	25	-88.0
Total current assets		**5,359**	**5,585**	**-4.0**
Total assets		**11,537**	**11,564**	**-0.2**
SHAREHOLDERS' EQUITY AND LIABILITIES				
Share capital		666	666	0.0
Capital reserves		2,348	2,348	0.0
Other reserves		249	-404	-
Accumulated other comprehensive income (loss)		-822	-713	15.3
Equity attributable to shareholders of the parent company		**2,441**	**1,897**	**28.7**
Non-controlling interests		107	100	7.0
Total shareholders' equity	**4.9**	**2,548**	**1,997**	**27.6**
Provisions for pensions and similar obligations	4.11	2,124	2,182	-2.7
Provisions	4.12	173	96	80.2
Financial debt	4.10	3,066	3,704	-17.2
Income tax payables	4.3	153	163	-6.1
Other financial liabilities	4.13	24	86	-72.1
Other liabilities	4.13	7	6	16.7
Deferred tax liabilities	4.3	129	124	4.0
Total non-current liabilities		**5,676**	**6,361**	**-10.8**
Provisions	4.12	233	354	-34.2
Financial debt	4.10	2	3	-33.3
Trade payables	4.14	1,867	1,625	14.9
Income tax payables	4.3	162	176	-8.0
Other financial liabilities	4.13	682	696	-2.0
Other liabilities	4.13	367	344	6.7
Liabilities held for sale	4.8	0	8	-
Total current liabilities		**3,313**	**3,206**	**3.3**
Total shareholders' equity and liabilities		**11,537**	**11,564**	**-0.2**

4. Consolidated statement of cash flow

No. 091

in € millions	Note	2017	2016	Change in %
Operating activities				
EBIT		1,528	1,556	-1.8
Interest paid		-121	-279	-56.6
Interest received		10	98	-89.8
Income taxes paid		-345	-327	5.5
Depreciation, amortization, and impairment losses		767	737	4.1
(Gains) losses on disposal of assets		2	4	-50.0
Changes in:				
• Inventories		-206	-88	› 100
• Trade receivables	5.2	-86	-205	-58.0
• Trade payables		261	271	-3.7
• Provisions for pensions and similar obligations		31	-29	-
• Other assets, liabilities, and provisions	4.13	-63	138	-
Cash flows from operating activities		**1,778**	**1,876**	**-5.2**
Investing activities				
Proceeds from disposals of property, plant and equipment		9	4	› 100
Capital expenditures on intangible assets		-32	-29	10.3
Capital expenditures on property, plant and equipment		-1,241	-1,117	11.1
Acquisition of subsidiaries	5.1	-47	0	-
Proceeds from disposal of subsidiaries		20	0	-
Other investing activities		1	1	0.0
Cash used in investing activities		**-1,290**	**-1,141**	**13.1**
Financing activities				
Dividends paid to shareholders and non-controlling interests		-330	-329	0.3
Receipts from loans		440	1,000	-56.0
Repayments of loans	5.1	-940	-2,910	-67.7
Other financing activities		0	1,773	- 100
Cash used in financing activities		**-830**	**-466**	**78.1**
Net increase (decrease) in cash and cash equivalents		**-342**	**269**	**-**
Effects of foreign exchange rate changes on cash and cash equivalents		-31	3	-
Cash and cash equivalents as at beginning of period		1,071	799	34.0
Cash and cash equivalents as at December 31		**698**	**1,071**	**-34.8**

5. Consolidated statement of changes in equity

No. 092

in € millions	Share capital	Capital reserves	Other reserves	Accumulated other comprehensive income (loss): Translation reserve	Hedging reserve	Defined benefit plan remeasurement reserve	Total	Equity attributable to shareholders [1]	Non-controlling interests	Total
Balance as at January 01, 2016	**666**	**2,348**	**-935**	**-79**	**-29**	**-491**	**-599**	**1,480**	**88**	**1,568**
Net income			859					859	13	872
Other comprehensive income (loss)				52	-6	-160	-114	-114	0	-114
Total comprehensive income (loss)			**859**	**52**	**-6**	**-160**	**-114**	**745**	**13**	**758**
Dividends			-328					-328	-1	-329
Total amount of transactions with shareholders			**-328**					**-328**	**-1**	**-329**
Balance as at December 31, 2016	**666**	**2,348**	**-404**	**-27**	**-35**	**-651**	**-713**	**1,897**	**100**	**1,997**
Balance as at January 01, 2017	**666**	**2,348**	**-404**	**-27**	**-35**	**-651**	**-713**	**1,897**	**100**	**1,997**
Net income			980					980	17	997
Other comprehensive income (loss)				-240	50	81	-109	-109	-7	-116
Total comprehensive income (loss)			**980**	**-240**	**50**	**81**	**-109**	**871**	**10**	**881**
Dividends			-328					-328	-2	-330
Transactions with non-controlling interests			1					1	-1	0
Total amount of transactions with shareholders			**-327**					**-327**	**-3**	**-330**
Balance as at December 31, 2017	**666**	**2,348**	**249**	**-267**	**15**	**-570**	**-822**	**2,441**	**107**	**2,548**

[1] Equity attributable to shareholders of the parent company.

See Note 4.9 to the consolidated financial statements for further details

6. Consolidated segment information

(Part of the notes to the consolidated financial statements)

No. 093

	2017	2016	2017	2016	2017	2016
in € millions		Automotive		Industrial		Total
Revenue	10,869	10,338	3,152	3,000	14,021	13,338
Cost of sales	-7,915	-7,389	-2,260	-2,163	-10,175	-9,552
Gross profit	2,954	2,949	892	837	3,846	3,786
EBIT	1,283	1,373	245	183	1,528	1,556
• in % of revenue	11.8	13.3	7.8	6.1	10.9	11.7
Depreciation, amortization, and impairment losses	-585	-543	-182	-194	-767	-737
Inventories [1)]	1,287	1,231	730	674	2,017	1,905
Trade receivables [1)]	1,736	1,730	456	488	2,192	2,218
Property, plant and equipment [1)]	3,779	3,421	1,086	1,086	4,865	4,507
Additions to intangible assets and property, plant and equipment	1,039	904	248	211	1,287	1,115

Prior year information presented based on 2017 segment structure.
[1)] Amounts as at December 31.

See Note 5.5 to the consolidated financial statements for further details

Notes to the consolidated financial statements

1. General information

1.1 Reporting entity

Schaeffler AG, Herzogenaurach, is a publicly listed corporation domiciled in Germany with its registered office located at Industriestraße 1-3, 91074 Herzogenaurach. The company was founded on April 19, 1982 and is registered in the Commercial Register of the Fürth Local Court (HRB No. 14738). The consolidated financial statements of Schaeffler AG as at December 31, 2017, comprise Schaeffler AG and its subsidiaries, investments in associated companies, and joint ventures (together referred to as the "Schaeffler Group"). The Schaeffler Group is a global automotive and industrial supplier.

The company is consolidated in the consolidated financial statements of INA-Holding Schaeffler GmbH & Co. KG, Herzogenaurach, which are filed with the operator of the Federal Gazette (Bundesanzeiger Verlag GmbH, Cologne) and published in the Federal Gazette.

1.2 Basis of preparation

In accordance with section 315e (1) HGB, the consolidated financial statements of the Schaeffler Group for the year ended December 31, 2017, have been compiled in accordance with International Financial Reporting Standards as adopted in the European Union (EU) by Regulation (EC) No. 1606/2002 of the European Parliament and of the Council on the application of international accounting standards as well as with the additional requirements of German commercial law. The term IFRS includes all International Financial Reporting Standards (IFRS) and International Accounting Standards (IAS) in effect as well as all interpretations and amendments issued by the IFRS Interpretations Committee (IFRIC) and the former Standing Interpretations Committee (SIC). Comparative figures for the prior year were also determined based on these standards.

General presentation

These consolidated financial statements are presented in euros (EUR), the functional and presentation currency of the Schaeffler Group's parent company. Unless stated otherwise, all amounts are in millions of euros (EUR m). The consolidated statement of financial position is classified using the current/non-current distinction.

The financial statements of all entities included in these consolidated financial statements have been prepared as of the same date as these consolidated financial statements.

As amounts (in EUR m) and percentages have been rounded, rounding differences may occur.

Estimation uncertainty and management judgment

In compiling financial statements, management exercises judgment in making appropriate estimates and assumptions affecting the application of accounting policies and the reported amounts of assets and liabilities, income and expenses. Actual amounts may differ from these estimates.

Estimates and the basis on which assumptions are made are reviewed regularly. Changes in estimates are recognized in the period in which the changes are made as well as in all subsequent periods affected by the changes.

The following significant issues are subject to estimation uncertainty with respect to the application of accounting policies and management judgment:

- determination of the useful life of property, plant and equipment
- identification of cash-generating units and determination of recoverable amounts for purposes of impairment tests of goodwill and non-current assets
- determination of valuation allowances on inventories
- assessment of the recoverability of deferred tax assets
- evaluation of control over structured entities
- accounting for post employment employee benefits, especially selecting actuarial assumptions
- recognition and measurement of provisions
- share-based payment and
- determination of fair values of financial debt and derivatives

Except for the measurement of defined benefit pension obligations, changes in assumptions made in the past and the resolution of previously-existing uncertainties related to the above items did not have a significant impact in 2017. The discount rate used to measure defined benefit pension obligations was increased to reflect higher interest rate levels, affecting the recognized amounts of the provision and shareholders' equity (see Note 4.11). In addition, the provisions for restructuring and for antitrust proceedings (see Note 4.12) were updated to reflect current information.

1.3 Summary of significant accounting policies

The accounting policies set out below have been applied consistently by all Schaeffler Group entities for all periods presented in these consolidated financial statements.

Consolidation principles

All significant domestic and foreign subsidiaries of the Schaeffler Group that are directly or indirectly controlled by Schaeffler AG have been consolidated in the company's consolidated financial statements. Subsidiaries are consolidated in the consolidated financial statements from the date the Schaeffler Group obtains control until the date control ceases.

Subsidiaries are consolidated using the acquisition method as at the acquisition date. Non-controlling interests are measured at the non-controlling interests' proportionate share of the fair value of assets acquired and liabilities assumed (partial goodwill method).

Balances and transactions with consolidated subsidiaries and any related income and expenses are eliminated in full in compiling the consolidated financial statements. Intercompany profits or losses on intra-group transactions are also eliminated in full. Deferred taxes on temporary differences related to the elimination of such balances and transactions are measured at the tax rate of the acquiring entity.

Foreign currency translation

The exchange rates between the group's most significant currencies and the euro are as follows:

Selected foreign exchange rates No. 094

Currencies		12/31/2017	12/31/2016	2017	2016
1 € in		Closing rates		Average rates	
CNY	China	7.80	7.32	7.63	7.35
INR	India	76.61	71.45	73.51	74.38
KRW	South Korea	1,279.61	1,270.57	1,275.98	1,284.51
MXN	Mexico	23.66	21.79	21.33	20.66
USD	U.S.	1.20	1.05	1.13	1.11

Foreign currency transactions

Transactions denominated in a currency other than the entity's functional currency are translated at the exchange rate applicable on the date they are first recognized. Since receivables and payables denominated in foreign currencies are monetary items, they are translated into the functional currency of the applicable group company at the exchange rate as at the end of the reporting period and when they are realized. Non-monetary items are translated at historical rates.

Exchange gains and losses on operating receivables and payables and on derivatives used to hedge the related currency risk are presented within earnings before financial result and income taxes (EBIT). Exchange gains and losses on the translation of financial assets and liabilities and on derivatives obtained to hedge the related currency risk are reflected in the financial result.

Foreign entities

Assets, including goodwill, and liabilities of subsidiaries whose functional currency is not the euro are translated at the spot rate at the end of the reporting period. The components of equity are translated at historical rates, and items in the consolidated income statement are translated at the weighted average rate for each reporting period. The resulting translation differences are recognized in other comprehensive income and reported in accumulated other comprehensive income. The impact of currency translation recognized in shareholders' equity is reversed to profit or loss when consolidation of the subsidiary ceases.

Items in the consolidated statement of cash flows are translated at the weighted average exchange rate for the period except for cash and cash equivalents, which are translated at the spot rate at the end of the reporting period.

Revenue recognition

Revenue is recognized when, based on the contract with the customer,

- the significant rewards and risks of ownership of the goods have been transferred to the buyer,
- it is sufficiently probable that the economic benefits associated with the sale will flow to the Schaeffler Group,
- the costs associated with the transaction can be measured reliably,
- the Schaeffler Group does not retain continuing managerial involvement with the goods, and
- the amount of revenue can be measured reliably.

Revenue is recognized at the fair value of the consideration received or receivable, net of trade discounts and volume rebates.

Depending on specific customer contracts and purchase orders, revenue is normally recognized at the date of delivery, provided that the conditions listed above are met.

Functional costs

Income and expenses are allocated to the various functional areas. Depreciation, amortization, and impairment losses on intangible assets and property, plant and equipment are allocated to the functional area in which the asset is utilized.

Research and development expenses

Expenses incurred for research activities, advance development, and to produce customer-specific applications are expensed immediately.

Development costs are only recognized as intangible assets once the capitalization criteria of IAS 38 are met.

Capitalized development costs are measured at cost less accumulated amortization and impairment losses. Amortization is recognized in profit or loss on a straight-line basis over a period of six years beginning when the intangible asset is ready for use. Amortization expense is reported in cost of sales.

Financial result

Interest income and expense are recognized in the period to which they relate.

Earnings per share

Earnings per share are calculated by dividing net income attributable to Schaeffler AG's shareholders by the weighted average number of common and common non-voting shares outstanding during the reporting period.

Goodwill

Goodwill is not amortized, but is tested for impairment annually and when there is an indication ("triggering event"). Goodwill is measured at cost less accumulated impairment losses.

The impairment test is performed by comparing the carrying amount of the cash-generating unit to which the goodwill has been allocated with its recoverable amount. A cash-generating unit is the smallest unit with largely independent cash flows. The recoverable amount is the higher of fair value less costs of disposal and value in use of the cash-generating unit. Value in use is determined using the discounted cash flow method. If circumstances giving rise to an impairment loss subsequently cease to exist, impairment losses on goodwill are not reversed.

Expected cash flows are based on a detailed three-year-forecast and on a perpetuity for the period beyond that timeframe. This detailed forecast is based on specific assumptions regarding macroeconomic trends (currency, interest, and commodity price trends), external sales forecasts and internal assessments of demand and projects, sales prices and the volume of investment. Please refer to the report on expected developments in the group management report for further details. Past trends and historic experience are also used in developing the forecast. The discount rate reflects current market expectations and specific risks.

Other intangible assets and property, plant and equipment

Other intangible assets and property, plant and equipment are recognized at acquisition or production cost plus incidental acquisition costs and, where applicable, subsequent acquisition cost and are amortized or depreciated over their expected useful life on a straight-line basis, provided they have a determinable useful life. The expected useful lives of software and capitalized development costs are three and six years, respectively, and range from 15 to 25 years for buildings, from two to ten years for technical equipment and machinery, and from three to eight years for other equipment. Impairment losses are recognized for impairments.

Leases

Lease payments classified as operating leases are expensed on a straight-line basis over the lease term. The Schaeffler Group's finance leases are immaterial.

Impairments of other intangible assets and property, plant and equipment

The Schaeffler Group tests other intangible assets and property, plant and equipment for impairment when there is an indication that these assets may be impaired ("triggering event").

The Schaeffler Group initially determines the recoverable amount under the value in use concept using the discounted cash flow method. If the value in use does not exceed the carrying amount of the cash-generating unit, the recoverable amount is then determined using fair value less costs of disposal.

Financial instruments

Regular-way sales and purchases of financial assets are accounted for using settlement date accounting.

Primary financial instruments

Primary financial instruments are initially measured at fair value. Transaction costs directly attributable to the acquisition or issue of a financial instrument are only included in the carrying amount if the financial instrument is not measured at fair value through profit or loss. Subsequent measurement depends on how the financial instrument is categorized.

The Schaeffler Group classifies its financial instruments into the following categories:

Available-for-sale financial assets

These are measured at fair value. Changes in fair value are recognized in other comprehensive income (including the related deferred taxes). Fair values are largely derived from market prices unless no quoted prices are available or there is no active market; in these cases, fair value is determined using recognized valuation techniques such as the discounted cash flow method. When the fair value of investments in equity instruments cannot be measured reliably using recognized valuation techniques, these investments are measured at cost.

Loans and receivables

Loans and receivables are measured at amortized cost less any impairment losses. These assets are tested for impairment at the end of each reporting period and when there is objective evidence of impairment, such as default or payment delays on the part of the borrower or evidence of insolvency. Impairment losses on trade receivables and miscellaneous other financial assets are recognized in profit or loss unless the receivable is covered by credit insurance. Impairments are initially recognized in an allowance account unless it is clear at the time the impairment loss occurs that the receivable will be either partially or entirely uncollectible.

Trade receivables sold under receivable sale programs as well as the related liabilities are recognized to the extent of the default risks retained (continuing involvement) (see Note 5.2).

Cash and cash equivalents are accounted for at cost.

Financial liabilities

Except for derivative financial instruments, the Schaeffler Group measures its financial liabilities at amortized cost using the effective interest method.

Derivative financial instruments

Derivative financial instruments are classified as trading and measured at fair value unless they are subject to hedge accounting.

Embedded derivatives are separated from the host instrument when the economic characteristics and risks of the embedded derivative are considered not closely related to the economic characteristics and risks of the host instrument.

Hedge accounting

Hedging relationships are accounted for using the cash flow and net investment hedge models. The effective portion of changes in the fair value of the hedging instrument is reported directly in accumulated other comprehensive income until the hedged item occurs. These gains and losses are reclassified to profit or loss in the same period in which the hedged item affects profit or loss. The ineffective portion is recognized in profit or loss.

Inventories

Inventories are measured at the lower of cost and net realizable value. The acquisition cost of raw materials, supplies and purchased merchandise is determined using the moving average cost method. Work in progress and manufactured finished goods are valued at production cost and written down to net realizable value if lower.

Income taxes

Deferred income taxes are accounted for using the asset and liability method.

Except where the recognition of deferred taxes is not permitted, deferred taxes are recognized on temporary differences between carrying amounts in the consolidated IFRS statement of financial position and the company's tax balance sheets, on loss and interest carryforwards, and on tax credits. Deferred tax assets are recognized only to the extent that it is probable that taxable profit will be available against which temporary differences and unused tax loss and interest carryforwards can be utilized. Group entities are assessed individually with respect to whether it is probable that profits will be generated in the future.

Deferred taxes are measured using the future tax rate. Future tax rate changes are reflected in this tax rate when they have been substantively enacted.

Management regularly reviews tax returns, mainly with respect to issues subject to interpretation, and reflects these in income tax payables as appropriate, based on amounts expected to be payable to taxation authorities. Potential risks arising from tax audits are covered by a provision.

Assets and liabilities held for sale

Non-current assets or groups of non-current assets (including the associated liabilities) are classified as held for sale if their carrying amount will be recovered principally through a sale transaction rather than through continuing use. Classification as held for sale requires a commitment to a plan to sell the asset or group of assets and the sale must be highly probable within twelve months. Such assets and liabilities are presented separately in the statement of financial position. Non-current assets held for sale are measured at the lower of their carrying amount and fair value less costs to sell.

Provisions for pensions and similar obligations

The Schaeffler Group provides post employment benefits to its employees in the form of defined benefit plans and defined contribution plans as part of its company pension model.

The Schaeffler Group's obligations under defined benefit plans are calculated annually using the projected unit credit method separately for each plan based on an estimate of the amount of future benefits that employees have earned in return for their service in current and prior periods. Estimating the obligations and costs related to pensions and accrued vested rights involves the use of assumptions based on market expectations, including those related to anticipated future compensation increases. The present value of the defined benefit obligation is determined by discounting estimated future cash outflows using the market rate of return for high-quality corporate bonds. The provisions for pensions and similar obligations recognized in the consolidated statement of financial position represent the present value of the defined benefit obligation at the end of the reporting period, net of the related plan assets measured at fair value, where applicable. In addition to the pension funds maintained to fund the obligation, plan assets include all assets and rights under reimbursement insurance policies if the proceeds of the policy can be used only to make payments to employees entitled to pension benefits and are not available to satisfy claims of the company's other creditors. If plan assets exceed the related pension obligation, the net pension asset is presented under other assets to the extent the Schaeffler Group is entitled to a refund or reduction of future contributions to the fund.

Actuarial gains and losses arising from defined benefit plans are recognized in other comprehensive income, while interest expense on provisions for pensions and similar obligations and the return on plan assets are considered separately for each plan and presented in the financial result on a net basis.

For defined contribution plans, the Schaeffler Group pays fixed contributions to an independent third party. As the Schaeffler Group does not in any way guarantee a return on the assets, neither up to the date pension payments commence nor beyond, the group's obligation is limited to the contributions it makes during the year. The contributions are recognized in personnel expense.

Provisions

Provisions are recognized at present value calculated by discounting expected future cash flows using a pre-tax rate that reflects current market assessments of the time value of money. Interest expense and the impact of any changes in discount rates are presented within the financial result.

Share-based payment

The Schaeffler Group's Performance Share Unit Plan (PSUP) is accounted for as a cash-settled share-based payment plan. The company recognizes a provision in the amount of the fair value of the payment obligation attributable to the period up to the reporting date. The liability is remeasured at the end of each reporting period from the grant date until settlement. The fair value per Performance Share Unit (PSU) is determined using a binomial option pricing model. The fair value is recognized as personnel expense over the period between the grant date and settlement date.

1.4 New accounting pronouncements

Certain amendments to IAS 7 Statement of Cash Flows and IAS 12 Income Taxes are effective starting in 2017. A new reconciliation of changes in liabilities arising from financing activities has been disclosed to meet the requirements of IAS 7. The amendments to IAS 12 have not had any impact on these financial statements.

The Schaeffler Group is not yet required to apply the following amendments to standards issued by the International Accounting Standards Board (IASB) in its financial statements for the financial year 2017, and none were adopted early.

IFRS 9

In July 2014, the IASB issued its standard IFRS 9 Financial Instruments which replaces the requirements of IAS 39. The standard is effective for annual reporting periods beginning on or after January 01, 2018. The company will use the modified retrospective approach to transition to IFRS 9, i.e. the standard will only be applied to the most recent reporting period presented in the financial statements (the year 2018). The cumulative effect of applying the standard retrospectively will be recognized as an adjustment to the opening balance of shareholders' equity at January 01, 2018, the date of initial application.

The Schaeffler Group has examined the impact of applying IFRS 9 in a dedicated project.

IFRS 9 introduces a new approach to the classification and measurement of financial assets. The classification criteria are the cash flow criterion and the business model for managing the financial assets. The Schaeffler Group has reviewed all of its financial assets with respect to whether they meet the cash flow criterion and assigned them to the relevant business models. Classification and measurement of the part of the portfolio of trade receivables that is available for sale under the ABCP program (asset-backed commercial paper) (see Note 5.2) will change from the current measurement base, amortized cost (AC), to measurement at fair value through profit or loss (FVTPL). This will not result in any significant measurement differences. Investments and marketable securities currently classified as available for sale (AfS) will be classified as at fair value through other comprehensive income (FVTOCI). This will not result in any measurement differences. Investments currently measured at amortized cost under the exception allowed by IAS 39 because their fair value was not reliably determinable will be accounted for at fair value, which is expected to increase other reserves by approx. EUR 24 m upon initial application.

IFRS 9 largely carries forward the classification and measurement requirements of IAS 39 for financial liabilities. Although the Schaeffler Group has one modified financial liability, the analysis performed to date indicates that this is not expected to affect the amount recognized under IFRS 9.

IFRS 9 also introduces a new impairment model for financial assets accounted for at amortized cost or at fair value through other comprehensive income. The standard replaces the current incurred loss model with an expected loss model. Credit loss allowances recognized for trade receivables are based on credit losses expected over the entire life of the receivable, determined using customer-specific probabilities of default and taking into account information about future conditions. Credit loss allowances for other financial assets, primarily cash and cash equivalents, should be measured and recognized at the amount of credit losses resulting from default events expected to occur during the next twelve months, unless credit risk has increased significantly since initial recognition. If credit risk has increased significantly, the credit loss allowance recognized has to reflect lifetime expected credit losses. The Schaeffler Group expects initial application to increase other reserves by up approx. EUR 4 m.

The hedge accounting requirements were also revised under IFRS 9 to allow financial statements to better reflect the company's risk management strategy. The standard requires extensive additional quantitative and qualitative note disclosures as well. In accordance with the option provided for hedge accounting in the transition requirements of IFRS 9, the Schaeffler Group will continue to apply the hedge accounting requirements of IAS 39 and intends to initially apply the hedge accounting requirements of IFRS 9 at a later date, i.e. after January 01, 2018.

IFRS 15

The new IFRS 15 Revenue from Contracts with Customers replaces existing revenue recognition guidance previously contained in several standards (IAS 18 Revenue and IAS 11 Construction Contracts) and interpretations (IFRIC 13, IFRIC 15, IFRIC 18, and SIC 31). The standard is effective for annual reporting periods beginning on or after January 01, 2018. The Schaeffler Group will initially apply the standard for the year beginning on January 01, 2018. The company will use the modified retrospective approach to transition to IFRS 15, i.e. the standard will only be applied to the most recent reporting period presented in the financial statements (the year 2018). The cumulative effect of initially applying the standard will be recognized as an adjustment to the opening balance of shareholders' equity at January 01, 2018, the date of initial application.

The Schaeffler Group has examined the impact of applying IFRS 15 in a dedicated project. Areas where initial application is currently expected to result in a significant impact are discussed below.

The Schaeffler Group expects initial application to increase other reserves by approx. EUR 4 m.

Customer tools

The new requirements regarding customers obtaining control of goods or services will result in changes regarding tools for initial series production. The Schaeffler Group has concluded that it has a distinct performance obligation vis-à-vis the customer for tools for initial series production with forecasted revenue of approx. EUR 4 m and is, therefore, required to recognize revenue when the customer obtains control. Consequently, tools for initial series production currently capitalized as assets under construction will be classified as unfinished goods in the opening statement of financial position as at January 01, 2018. This will result in the recognition of revenue and cost of sales when the customer obtains control of the completed tools for initial series production in future periods.

Initial application of this accounting treatment will not result in a significant change in other reserves.

Development services

IFRS 15 will require revenue to be recognized for development services that represent a distinct, separately identifiable performance obligation vis-à-vis the customer and for which the Schaeffler Group is entitled to consideration under the contract. Revenue is recognized when the customer obtains control of the completed development services (revenue recognition at a point in time). Therefore, any costs incurred for these development projects will be accounted for in cost of sales and the reimbursements received from customers as revenues.

Due to these changes, the Schaeffler Group will recognize development services in progress as inventories of EUR 22 m as well as contract liabilities for consideration received from customers of EUR 25 m in its opening statement of financial position as at January 01, 2018. These balances will lead to the recognition of revenue and cost of sales when the customer obtains control of the completed development services in future periods.

The Schaeffler Group expects initial application of this accounting treatment to decrease other reserves by EUR 3 m.

Customer-specific products

IFRS 15 will require revenue to be recognized over time for customer-specific products that have no alternative use due to their specifications, provided the Schaeffler Group has an enforceable right to payment from the customer for these products amounting to at least any costs of performance completed to date plus a reasonable profit margin.

Products are customer-specific if the Schaeffler Group can sell them to only one customer. This will result in revenue being recognized earlier than under the company's current accounting policies. EUR 29 m in contract assets for revenue recognized over time for customer-specific products will be capitalized in the opening statement of financial position as at January 01, 2018. Inventories will decrease by EUR 22 m.

The Schaeffler Group expects initial application of this accounting treatment to increase other reserves by EUR 7 m.

IFRS 16

In January 2016, the IASB issued IFRS 16 Leases which replaces the requirements of IAS 17. The standard is effective for annual reporting periods beginning on or after January 01, 2019. Earlier application is permitted, but the Schaeffler Group does not plan to apply the standard early.

IFRS 16 introduces a uniform lessee accounting model requiring lessees to capitalize leases in their statement of financial position. Under this model, lessees are required to recognize assets (for the right of use) and lease liabilities for any lease agreements with a term of more than 12 months. The Schaeffler Group will initially apply the standard for the year beginning on January 01, 2019. The company will use the modified retrospective approach to transition to IFRS 16, i.e. the standard will only be applied to the most recent reporting period presented in the financial statements (the year 2019). The impact of initial application is expected to relate largely to leased real estate. The Schaeffler Group is currently assessing the impact on the consolidated financial statements of applying IFRS 16.

New accounting pronouncements not endorsed by the EU

In addition, the IASB has issued the following new standards and amendments to existing standards which had not yet been adopted by the EU as at the date these consolidated financial statements were authorized for issue. The company has not applied any of them early, and is currently not planning to apply any of them early.

New accounting pronouncements – not yet endorsed by the EU No. 095

Standard/Interpretation		Effective date	Subject of Standard/Interpretation or amendment	Expected impact on the Schaeffler Group
Annual improvements 2014–2016		01/01/2018	Various improvements to IFRS 1, IFRS 12, and IAS 28	none
Amendments to IFRS 2	Classification of Share-based Payment Transactions	01/01/2018	Changes regarding arrangements with a net settlement feature and modifications that may change classification	Under examination [1]
Amendments to IAS 40	Transfers of Investment Property	01/01/2018	Clarifications regarding the requirements for the transfer of investment property	none
IFRIC 22	Foreign Currency Transactions and Advance Consideration	01/01/2018	Clarifications regarding the date of the transaction for the purpose of determining the exchange rate for foreign currency transactions involving the recognition of non-monetary assets or liabilities for advance consideration paid or received before the related assets, income, or expenses are recognized.	Under examination [1]
Amendments to IFRS 9	Financial Instruments	01/01/2019	Amendments regarding whether instruments with prepayment features with negative compensation meet the cash flow condition, clarification regarding modification of financial liabilities	none
Amendments to IAS 28	Long-term Interests in Associates and Joint Ventures	01/01/2019	Amendments clarifying that long-term interests that are considered part of the net investment in an associate or joint venture are accounted for under IFRS 9 unless they are accounted for under the equity method.	none
IFRIC 23	Uncertainty over Income Tax Treatments	01/01/2019	Clarification regarding various aspects of uncertainty over income tax treatment	Under examination [1]
IFRS 17	Insurance Contracts	01/01/2021	Principles for recognition, measurement, and presentation of as well as disclosures about insurance contracts	Under examination [1]
Amendments to IFRS 10, IAS 28		undefined	Clarification of accounting for gains and losses on the sale or contribution of assets between an investor and its associate or joint venture	Under examination [1]

[1] Detailed statements regarding the extent of the impact are not yet possible.

2. Principles of consolidation

2.1 Scope of consolidation

In 2017, the consolidated financial statements of Schaeffler AG cover, in addition to Schaeffler AG, 151 (prior year: 152) subsidiaries; 50 (prior year: 51) entities are domiciled in Germany and 101 (prior year: 101) in other countries.

The scope of consolidation of Schaeffler AG did not change significantly compared to the consolidated financial statements of the Schaeffler Group as at December 31, 2016.

In the consolidated financial statements as at December 31, 2017, five (prior year: five) investments (including two joint ventures; prior year: two) are accounted for at equity.

A further five (prior year: one) companies were not consolidated as at December 31, 2017, since they were insignificant to the results of operations, financial position, and net assets of the Schaeffler Group.

More on the Schaeffler Group's companies in Note 5.10

3. Notes to the consolidated income statement

3.1 Revenue

Revenue No. 096

in € millions	2017	2016
Revenue from the sale of goods	13,828	13,167
Other revenue	193	171
Total	**14,021**	**13,338**

Other revenue primarily includes EUR 116 m (prior year: EUR 96 m) in revenue from the sale of tools and machines constructed by the company as well as EUR 59 m (prior year: EUR 64 m) from services.

3.2 Other income

Other income No. 097

in € millions	2017	2016
Gains on reversal of provisions	38	13
Miscellaneous income	44	28
Total	**82**	**41**

3.3 Other expenses

Other expenses No. 098

in € millions	2017	2016
Exchange losses	35	9
Miscellaneous expenses	106	168
Total	**141**	**177**

Foreign exchange losses consisted largely of exchange losses from operations and exchange losses related to forward exchange contracts. In 2017, netting foreign exchange gains and losses resulted in a net exchange loss of EUR 35 m (prior year: EUR 9 m).

Miscellaneous other expenses include EUR 39 m (prior year: EUR 0 m) in restructuring expenses incurred to set up a shared service center in Europe. In addition, EUR 16 m (prior year: EUR 86 m) in expenses were attributable to potential third-party claims in connection with antitrust proceedings and other compliance cases. The prior year contained EUR 45 m in expenses related to the stepped-up efficiency measures aimed at revitalizing the Industrial division under the second wave of the program “CORE”.

3.4 Personnel expense and headcount

Average number of employees by region No. 099

	2017	2016
Europe	60,954	59,609
Americas	12,826	12,563
Greater China	11,981	10,778
Asia/Pacific	2,936	2,783
Total	**88,697**	**85,733**

The number of employees at December 31, 2017, was 90,151, 4.0% above the prior year level of 86,662.

The Schaeffler Group's personnel expense consisted of the following:

Personnel expense No. 100

in € millions	2017	2016
Wages and salaries	3,606	3,388
Social security contributions	700	665
Other personnel expense	131	114
Total	**4,437**	**4,167**

The increase in personnel expense in 2017 is mainly attributable to pay increases arising from local collective agreements and to the targeted expansion of capacity, mainly in production and production-related areas in the Greater China and Europe regions. In order to further strengthen its innovative ability, the company focused on recruiting new personnel in its research and development departments, especially in Germany.

Other personnel expense includes EUR 128 m (prior year: EUR 110 m) in retirement benefit expenses.

3.5 Financial result

Schaeffler Group financial result No. 101

in € millions	2017	2016
Interest expense on financial debt [1]	-123	-286
Interest income on shareholder loans	0	49
Gains and losses on derivatives and foreign exchanges	-17	-33
Fair value changes on embedded derivatives	-14	-30
Interest income and expense on pensions and partial retirement obligations	-38	-45
Other	0	4
Total	**-192**	**-341**

[1] Incl. amortization of transaction costs and prepayment penalties.

Interest expense on financial debt amounted to EUR 123 m in 2017 (prior year: EUR 286 m) and included prepayment penalties of EUR 13 m (prior year: EUR 48 m) and EUR 5 m (prior year: EUR 31 m) for the early amortization of transaction costs.

In 2016, IHO Verwaltungs GmbH prepaid its loans payable to Schaeffler AG in full. As a result, the Schaeffler Group no longer earned any **interest income on loans to shareholders** in 2017 (prior year: EUR 49 m).

Net **foreign exchange** losses on financial assets and liabilities and net losses on **derivatives** amounted to EUR 17 m (prior year: EUR 33 m). These include the impact of translating the financing instruments denominated in U.S. dollars to euros and hedges of these instruments using cross-currency swaps.

Fair value changes on embedded derivatives, primarily prepayment options for external financing instruments, resulted in net losses of EUR 14 m (prior year: EUR 30 m), comprising EUR 8 m (prior year: EUR 79 m) in losses related to prepayment options written off as part of the cost of refinancing transactions in 2017 and EUR 6 m (prior year: EUR 49 m in gains) resulting from changes in the fair value of the remaining prepayment options.

3.6 Income taxes

Income taxes No. 102

in € millions	2017	2016
Current income taxes	329	345
Deferred income taxes	10	-2
Total	**339**	**343**

As a corporation, Schaeffler AG was subject to German corporation and trade taxes during the reporting period 2017.

The average domestic tax rate was 28.6% in 2017 (prior year: 28.6%). This tax rate consisted of corporation tax, including the solidarity surcharge, of 15.9% (prior year: 15.9%) as well as the average trade tax rate of 12.7% (prior year: 12.7%).

The current income tax benefit related to prior years amounted to EUR 13 m (prior year: EUR 13 m) in 2017. The Schaeffler Group had a deferred tax benefit of EUR 16 m related to prior years (prior year: deferred tax expense of EUR 6 m) in 2017.

The following tax rate reconciliation shows the tax effects required to reconcile expected income tax expense to income tax expense as reported in the consolidated income statement. The calculation for 2017 is based on the Schaeffler Group's 28.6% (prior year: 28.6%) effective combined trade and corporation tax rate including solidarity surcharge.

Tax rate reconciliation No. 103

in € millions	2017	2016
Earnings before income taxes	1,336	1,215
Expected tax expense	**382**	**348**
Addition/reduction due to deviating local tax bases	5	5
Foreign/domestic tax rate differences	-22	-19
Change in tax rate and law	-8	-2
Non-recognition of deferred tax assets	7	4
Tax credits and other tax benefits	-16	-11
Non-deductible expenses and non-taxable income	24	32
Taxes for previous years	-29	-7
Other	-4	-7
Reported tax expense	**339**	**343**

Foreign/domestic tax rate differences primarily represent the impact of differences in country-specific tax rates applicable to German and foreign entities.

Non-deductible expenses and non-taxable income includes non-deductible operating expenses and deferred tax liabilities on dividends expected to be paid by subsidiaries.

Taxes for previous years mainly contain income tax benefits from reassessments of tax issues from prior years.

3.7 Earnings per share

Earnings per share No. 104

in € millions	2017	2016
Net income	997	872
Net income attributable to shareholders of the parent company	980	859
Earnings attributable to common shares (basic/diluted)	734	644
Earnings attributable to common non-voting shares (basic/diluted)	246	215
Average number of common shares issued in millions	500	500
Average number of common non-voting shares issued in millions	166	166
Earnings per common share (basic/diluted, in €)	**1.47**	**1.29**
Earnings per common non-voting share (basic/diluted, in €)	**1.48**	**1.30**

There were no dilutive items at December 31, 2017, or in the prior year. Diluted earnings per share equal basic earnings per share.

4. Notes to the consolidated statement of financial position

4.1 Intangible assets

The carrying amounts of **goodwill** allocated to cash-generating units were unchanged at EUR 319 m (prior year: EUR 319 m) for the Automotive segment and EUR 208 m (prior year: EUR 208 m) for the Industrial segment.

For purposes of determining value in use, cash flows beyond the detailed forecasting horizon of 2020 are based on an annual growth rate of 1.0% (prior year: 1.0%) for each segment. Depending on the underlying business and its country of operation, the Schaeffler Group used an assumed pre-tax interest rate of 12.6% (prior year: 12.6%) as the weighted average cost of capital for the Automotive segment and 12.4% (prior year: 12.6%) for the Industrial segment. This corresponds to a post-tax interest rate of 9.1% for the Automotive segment (prior year: 8.9%) and 9.0% for the Industrial segment (prior year: 8.9%).

As the value in use of each of the cash-generating units exceeded their carrying amount both for 2017 and the prior year, they were not impaired.

Internally generated intangible assets consisted largely of development costs of EUR 55 m (prior year: EUR 47 m), including EUR 35 m (prior year: EUR 22 m) in assets not yet available for use that were not yet subject to amortization.

Amortization of intangible assets totaled EUR 28 m (prior year: EUR 31 m) and was recognized in the following line items in the consolidated income statement: cost of sales EUR 6 m (prior year: EUR 8 m), research and development expenses EUR 5 m (prior year: EUR 5 m), and administrative expenses EUR 17 m (prior year: EUR 18 m).

Intangible assets No. 105

in € millions	Goodwill	Purchased intangible assets	Internally generated intangible assets	Total
Historical cost				
Balance as at January 01, 2016	**483**	**1,072**	**293**	**1,848**
Additions from initial consolidation of subsidiaries	44	1	0	45
Additions	0	12	17	29
Disposals	0	-4	0	-4
Transfers	0	0	0	0
Foreign currency translation	0	1	0	1
Balance as at December 31, 2016	**527**	**1,082**	**310**	**1,919**
Balance as at January 01, 2017	**527**	**1,082**	**310**	**1,919**
Additions from initial consolidation of subsidiaries	0	0	0	0
Additions	0	19	13	32
Disposals	0	-7	0	-7
Transfers	0	-1	1	0
Foreign currency translation	0	-4	-2	-6
Balance as at December 31, 2017	**527**	**1,089**	**322**	**1,938**
Accumulated amortization and impairment losses				
Balance as at January 01, 2016	**0**	**1,013**	**246**	**1,259**
Additions from initial consolidation of subsidiaries	0	0	0	0
Amortization	0	18	13	31
Disposals	0	-3	0	-3
Transfers	0	0	0	0
Foreign currency translation	0	0	0	0
Balance as at December 31, 2016	**0**	**1,028**	**259**	**1,287**
Balance as at January 01, 2017	**0**	**1,028**	**259**	**1,287**
Additions from initial consolidation of subsidiaries	0	0	0	0
Amortization	0	19	9	28
Disposals	0	-7	0	-7
Transfers	0	0	0	0
Foreign currency translation	0	-4	-2	-6
Balance as at December 31, 2017	**0**	**1,036**	**266**	**1,302**
Net carrying amounts				
As at January 01, 2016	**483**	**59**	**47**	**589**
As at December 31, 2016	**527**	**54**	**51**	**632**
As at January 01, 2017	**527**	**54**	**51**	**632**
As at December 31, 2017	**527**	**53**	**56**	**636**

4.2 Property, plant and equipment

Property, plant and equipment No. 106

in € millions	Land, land rights, and buildings	Technical equipment and machinery	Other equipment	Assets under construction	Total
Historical cost					
Balance as at January 01, 2016	**2,448**	**7,836**	**1,050**	**663**	**11,997**
Additions from initial consolidation of subsidiaries	0	1	0	0	1
Disposals of subsidiaries	-4	-51	-2	0	-57
Additions	44	379	83	580	1,086
Disposals	-3	-176	-45	-3	-227
Transfers	61	419	-3	-477	0
Reclassification to IFRS 5	-18	-36	-2	0	-56
Foreign currency translation	2	38	1	-7	34
Balance as at December 31, 2016	**2,530**	**8,410**	**1,082**	**756**	**12,778**
Balance as at January 01, 2017	**2,530**	**8,410**	**1,082**	**756**	**12,778**
Additions from initial consolidation of subsidiaries	0	0	0	0	0
Disposals of subsidiaries	0	0	0	0	0
Additions	39	372	109	735	1,255
Disposals	-2	-190	-71	-1	-264
Transfers	69	401	28	-498	0
Reclassification to IFRS 5	-3	0	0	0	-3
Foreign currency translation	-66	-269	-22	-22	-379
Balance as at December 31, 2017	**2,567**	**8,724**	**1,126**	**970**	**13,387**
Accumulated depreciation and impairment losses					
Balance as at January 01, 2016	**1,290**	**5,719**	**805**	**3**	**7,817**
Additions from initial consolidation of subsidiaries	0	0	0	0	0
Disposals of subsidiaries	-2	-41	-2	0	-45
Depreciation	78	540	80	0	698
Impairment losses	2	4	1	1	8
Disposals	-3	-173	-42	0	-218
Transfers	0	24	-24	0	0
Reclassification to IFRS 5	-12	-28	-2	0	-42
Foreign currency translation	5	46	1	1	53
Balance as at December 31, 2016	**1,358**	**6,091**	**817**	**5**	**8,271**
Balance as at January 01, 2017	**1,358**	**6,091**	**817**	**5**	**8,271**
Additions from initial consolidation of subsidiaries	0	0	0	0	0
Disposals of subsidiaries	0	0	0	0	0
Depreciation	78	556	105	0	739
Impairment losses	0	0	0	0	0
Disposals	-1	-186	-70	0	-257
Transfers	0	0	0	0	0
Reclassification to IFRS 5	0	0	0	0	0
Foreign currency translation	-31	-184	-15	-1	-231
Balance as at December 31, 2017	**1,404**	**6,277**	**837**	**4**	**8,522**
Net carrying amounts					
As at January 01, 2016	**1,158**	**2,117**	**245**	**660**	**4,180**
As at December 31, 2016	**1,172**	**2,319**	**265**	**751**	**4,507**
As at January 01, 2017	**1,172**	**2,319**	**265**	**751**	**4,507**
As at December 31, 2017	**1,163**	**2,447**	**289**	**966**	**4,865**

At December 31, 2017, the Schaeffler Group had open commitments under fixed contracts to purchase property, plant and equipment to the amount of EUR 451 m (prior year: EUR 320 m).

4.3 Deferred tax assets and liabilities and income tax receivables and payables

Deferred tax assets and liabilities

The following items gave rise to recognized deferred tax assets and liabilities:

Deferred tax assets and liabilities No. 107

in € millions	12/31/2017 Deferred tax assets	12/31/2017 Deferred tax liabilities	12/31/2016 Deferred tax assets	12/31/2016 Deferred tax liabilities
Intangible assets	2	-28	3	-22
Property, plant and equipment	104	-147	98	-175
Financial assets	2	-4	2	-13
Inventories	101	-5	110	-4
Trade receivables and other assets	65	-108	64	-108
Provisions for pensions and similar obligations	375	-44	406	-35
Other provisions and other liabilities	142	-113	189	-82
Interest- and loss carryforwards	21	0	15	0
Deferred taxes (gross)	**812**	**-449**	**887**	**-439**
Netting	-320	320	-315	315
Deferred taxes (net)	**492**	**-129**	**572**	**-124**

The group had gross carryforwards under the interest deduction cap of EUR 32 m (prior year: EUR 10 m) at the end of the reporting period. The company has recognized deferred tax assets on all interest carryforwards.

At December 31, 2017, the Schaeffler Group had gross loss carryforwards of EUR 99 m (prior year: EUR 115 m) for corporation tax and EUR 9 m (prior year: EUR 9 m) for trade tax, including EUR 72 m (prior year: EUR 92 m) in corporation tax losses and EUR 9 m (prior year: EUR 9 m) in trade tax losses for which no deferred taxes have been recognized.

EUR 22 m (prior year: EUR 51 m) of the corporation tax loss carryforwards on which no deferred tax assets were recognized can be carried forward for a limited period. The interest carryforwards can be utilized indefinitely.

No deferred tax assets were recognized on EUR 31 m (prior year: EUR 7 m) in temporary differences, as it is not considered probable that they will be utilized in the future.

No deferred taxes have been recognized on EUR 2,006 m (prior year: EUR 1,694 m) in undistributed profits of certain subsidiaries, as the company intends to continually reinvest these profits rather than distributing them.

As at the end of the reporting period, certain subsidiaries and tax groups that have suffered losses have recognized net deferred tax assets of EUR 5 m (prior year: EUR 1 m). Recovery of these deferred tax assets is considered probable since sufficient taxable profits are expected in the future.

At December 31, 2017, the amount of deferred taxes recognized in accumulated other comprehensive income was EUR 260 m (prior year: EUR 328 m) and mainly related to hedges of net investments in foreign operations, changes in the fair value of derivatives designated as hedging instruments, as well as remeasurements of pensions and similar obligations.

Income tax receivables and payables

At December 31, 2017, income tax receivables amounted to EUR 102 m (prior year: EUR 93 m) and did not include any non-current balances.

At December 31, 2017, income tax payables amounted to EUR 315 m (prior year: EUR 339 m), including non-current balances of EUR 153 m (prior year: EUR 163 m).

Non-current income tax payables included EUR 47 m (prior year: EUR 46 m) in interest on additional tax payments for prior years. Current income tax payables included EUR 30 m (prior year: EUR 27 m) in interest on additional tax payments for prior years.

4.4 Inventories

Inventories No. 108

in € millions	12/31/2017	12/31/2016
Raw materials and supplies	393	358
Work in progress	571	468
Finished goods and merchandise	1,052	1,078
Advance payments	1	1
Total	**2,017**	**1,905**

EUR 10,021 m (prior year: EUR 9,413 m) in inventories used were expensed as cost of sales in the consolidated income statement in 2017.

The impairment allowance on inventories amounted to EUR 271 m (prior year: EUR 260 m) as at December 31, 2017.

4.5 Trade receivables

Trade receivables No. 109

in € millions	12/31/2017	12/31/2016
Trade receivables (gross)	**2,213**	**2,243**
Impairment allowances	-21	-25
Trade receivables (net)	**2,192**	**2,218**

Movements in impairment allowances on these trade receivables can be reconciled as follows:

Impairment allowances on trade receivables No. 110

in € millions	2017	2016
Impairment allowances as at January 01	**-25**	**-28**
Additions	-1	-3
Allowances used to cover write-offs	2	3
Reversals	3	3
Impairment allowances as at December 31	**-21**	**-25**

Trade receivables of EUR 2,033 m (prior year: EUR 2,079 m) were neither past due nor impaired as at December 31, 2017.

Also as at December 31, 2017, trade receivables of EUR 133 m (prior year: EUR 113 m) were past due but not impaired. These balances were mainly up to 60 days overdue.

Trade accounts receivable subject to specific impairment allowances had a gross carrying amount of EUR 46 m (prior year: EUR 51 m), and the related impairment allowance was EUR -21 m (prior year: EUR -25 m).

At December 31, 2017, trade receivables outstanding with a carrying amount of EUR 123 m (prior year: EUR 0 m) net of retained default risks had been sold under the ABCP program (see Note 5.2).

EUR 195 m (prior year: EUR 201 m) in receivables were pledged as security for a line of credit as at December 31, 2017.

More on the Schaeffler Group's exposure to counterparty, currency, and liquidity risk in Note 4.14

4.6 Other financial assets and other assets

Other financial assets (non-current/current) No. 111

			12/31/2017			12/31/2016
in € millions	Non-current	Current	Total	Non-current	Current	Total
Loans receivable and financial receivables	2	0	2	3	0	3
Derivative financial assets	69	74	143	175	29	204
Miscellaneous other financial assets	43	37	80	39	26	65
Total	**114**	**111**	**225**	**217**	**55**	**272**

At December 31, 2017, **non-current derivative financial assets** consisted mainly of derivatives used to hedge currency risk and prepayment options on financial debt. The current portion of derivative financial assets represented fair values of derivatives the Schaeffler Group uses to hedge currency risk.

More on the Schaeffler Group's exposure to currency and liquidity risk in Note 4.14

Other assets (non-current/current) No. 112

			12/31/2017			12/31/2016
in € millions	Non-current	Current	Total	Non-current	Current	Total
Pension asset	46	0	46	21	0	21
Tax receivables	1	202	203	1	171	172
Miscellaneous other assets	24	34	58	29	47	76
Total	**71**	**236**	**307**	**51**	**218**	**269**

Tax receivables consisted predominantly of value-added tax refunds receivable.

The majority of **miscellaneous other assets** represented the non-current and current portions of prepaid assets and deferred charges.

4.7 Cash and cash equivalents

At December 31, 2017, cash and cash equivalents consisted primarily of bank balances.

At the end of the reporting period, cash and cash equivalents include EUR 293 m (prior year: EUR 325 m) held by subsidiaries in Argentina, Brazil, Chile, China, Colombia, India, Peru, the Philippines, South Korea, South Africa, Taiwan, Thailand, Venezuela, Vietnam and other countries. These subsidiaries are subject to exchange restrictions or other legal restrictions. As a result, the availability of these funds to Schaeffler AG as the parent entity is restricted.

4.8 Assets held for sale and liabilities associated with assets held for sale

Assets held for sale of EUR 3 m relate to the planned sale of land scheduled to close in the first quarter of 2018.

The decrease in assets and liabilities held for sale compared to the prior year is due to the complete disposal of the fine blanking activities of Schaeffler Schweiz GmbH, which had been classified as a disposal group as at December 31, 2016, in the second quarter of 2017.

4.9 Shareholders' equity

Shareholders' equity No. 113

in € millions	12/31/2017	12/31/2016
Share capital	666	666
Capital reserves	2,348	2,348
Other reserves	249	-404
Accumulated other comprehensive income (loss)	-822	-713
Equity attributable to shareholders of the parent company	**2,441**	**1,897**
Non-controlling interests	107	100
Total shareholders' equity	**2,548**	**1,997**

Schaeffler AG's **share capital** of EUR 666 m remains unchanged.

It is divided into 666 million no-par-value bearer shares, each representing an interest in share capital of EUR 1.00. The no-par-value shares are divided into 500 million common shares and 166 million common non-voting shares. The common non-voting shares carry a preferential right to profits consisting of a preferred dividend of EUR 0.01 per common non-voting share.

The common shares are held by IHO Verwaltungs GmbH. The common non-voting shares are widely held. Share capital is fully paid up and Schaeffler AG had no authorized or contingent capital or any resolutions with respect to these types of capital as at December 31, 2017.

Capital reserves remained unchanged at EUR 2,348 m as at December 31, 2017.

The change in **other reserves** in 2017 was largely attributable to consolidated net income and the dividends.

Distributions to shareholders are limited to Schaeffler AG's retained earnings, as determined in accordance with German commercial law. For 2017, a dividend of EUR 361 m will be proposed to the Schaeffler AG annual general meeting. EUR 91 m of these dividends relate to the common non-voting shares. This represents a total dividend of EUR 0.55 (prior year: EUR 0.50) per common non-voting share and EUR 0.54 (prior year: EUR 0.49) per common share. As the proposed dividend is subject to shareholder approval at the annual general meeting, it has not been recognized as a liability in these consolidated financial statements.

Accumulated other comprehensive income consisted of the impact of currency translation, changes in the fair value of financial instruments designated as hedging instruments, and remeasurements of pensions and similar obligations.

At December 31, 2017, **non-controlling interests** represented third-party interests in the equity of Schaeffler India Ltd. (previously FAG Bearings India Ltd.), India. The remaining interests in the two Thai companies Schaeffler (Thailand) Co., Ltd. and Schaeffler Holding (Thailand) Co., Ltd. were acquired during the year.

4.10 Current and non-current financial debt

Financial debt (current/non-current) No. 114

			12/31/2017			12/31/2016
in € millions	Due in up to 1 year	Due in more than 1 year	Total	Due in up to 1 year	Due in more than 1 year	Total
Bonds	0	1,994	1,994	0	2,719	2,719
Facilities Agreement	0	983	983	0	982	982
Capital investment loans	0	89	89	0	0	0
Other financial debt	2	0	2	3	3	6
Total	**2**	**3,066**	**3,068**	**3**	**3,704**	**3,707**

The decrease in financial debt compared to December 31, 2016, resulted primarily from the early redemption of the USD bond with a principal of USD 700 m, a coupon of 4.25%, and an original maturity of May 2021 in full on May 24, 2017. The redemption was funded using available liquidity and by utilizing EUR 350 m of the revolving credit facility. On November 23, 2017, the Schaeffler Group reduced the amount drawn under the revolving credit facility to a remaining balance of EUR 150 m by repaying EUR 200 m from available liquidity. On December 27, 2017, the Schaeffler Group repaid the remaining balance of EUR 150 m outstanding under the revolving credit facility in full.

On December 15, 2017, Schaeffler AG signed a loan agreement to finance long-term logistics projects. These logistics projects, which form part of the "European Distribution Center" (EDC) project, are the central distribution center "EDC Central" (Kitzingen) and the European assembly and packaging center known as the "Aftermarket Kitting Operation" (AKO). The total amount of the loan is EUR 250 m, of which EUR 90 m (prior year: EUR 0 m) were drawn as at December 31, 2017. The loan has a term until 2022 plus certain renewal options.

At December 31, 2017, the group's debt consisted of a loan tranche with a principal of EUR 1.0 bn, four bond series totaling the equivalent of approx. EUR 2.0 bn, a revolving line of credit (revolving credit facility, RCF) with a principal of EUR 1.3 bn, and a capital investment loan with a principal of EUR 250 m.

The Schaeffler Group had the following loans outstanding at December 31, 2017:

Schaeffler Group loans No. 115

Tranche	Currency	Principal in millions 12/31/2017	Principal in millions 12/31/2016	Carrying amount in € millions 12/31/2017	Carrying amount in € millions 12/31/2016	Coupon 12/31/2017	Coupon 12/31/2016	Maturity
Term Loan	EUR	1,000	1,000	991	992	Euribor [1] + 1.20%	Euribor [1] + 1.20%	07/18/2021
Revolving Credit Facility [2]	EUR	1,300	1,300	-8	-10	Euribor [1] + 0.80%	Libor [1] + 0.80%	07/18/2021
Capital investment loan [3]	EUR	250	0	89	0	Euribor [1] + 1.00%	n/a	12/15/2022
Total				**1,072**	**982**			

[1] Euribor Floor of 0.00%.
[2] EUR 12 m (December 31, 2016: EUR 13 m) were drawn down as at December 31, 2017, primarily in the form of letters of credit.
[3] EUR 90 m (December 31, 2016: EUR 0 m) were drawn down as at December 31, 2017.

In addition, the Schaeffler Group had further committed lines of credit in the equivalent of approx. EUR 154 m (prior year: approx. EUR 160 m), primarily for the U.S. and China. Approx. EUR 111 m (prior year: approx. EUR 160 m) of these committed facilities were unutilized at December 31, 2017.

The following bonds issued by Schaeffler Finance B.V., Barneveld, Netherlands, were outstanding as at the end of the reporting period:

Schaeffler Group bonds No. 116

ISIN	Currency	Principal in millions 12/31/2017	Principal in millions 12/31/2016	Carrying amount in € millions 12/31/2017	Carrying amount in € millions 12/31/2016	Coupon	Maturity
XS1212469966	EUR	400	400	398	397	2.50%	05/15/2020
US806261AJ29 [1]	USD	0	700	0	658	4.25%	05/15/2021
XS1067864022	EUR	500	500	498	498	3.50%	05/15/2022
US806261AM57	USD	600	600	502	571	4.75%	05/15/2023
XS1212470972	EUR	600	600	596	595	3.25%	05/15/2025
Total				**1,994**	**2,719**		

[1] Redeemed in full on May 24, 2017.

The differences between principal and carrying amount are the result of accounting for these instruments at amortized cost calculated using the effective interest method. The carrying value of the Revolving Credit Facility consisted entirely of unamortized transaction costs.

An additional EUR 22 m (prior year: EUR 27 m) in interest accrued on the bonds up to December 31, 2017, were reported in other financial liabilities (see Note 4.13).

Under its existing debt financing agreements, the Schaeffler Group is subject to certain constraints including a requirement to meet a leverage covenant. The creditors are entitled to call the debt prior to maturity under certain circumstances, including if the leverage covenant is not met, which would result in the debt becoming due immediately. As in prior years, the company has complied with the leverage covenant throughout 2017 as stipulated in the debt agreements.

The shares in two subsidiaries as well as intra-group loan receivables were pledged as collateral under the loan and bond agreements.

4.11 Provisions for pensions and similar obligations

The post-employment benefits the Schaeffler Group provides to its employees include both defined benefit plans and and defined contribution plans. While defined contribution plans generally entail no further obligation beyond the regular contributions included in personnel expense, defined benefit plans are recognized in the consolidated statement of financial position. The provisions also include a minor amount of obligations similar to pensions.

Defined benefit plans

The Schaeffler Group's defined benefit plans include pension plans, termination payments mandatorily payable upon retirement regardless of the reason employment is terminated, and other post employment benefits. The company's pension obligations essentially relate to Germany, the U.S., and the United Kingdom, with the majority of the obligations attributable to Germany.

Germany

In Germany, the company grants pension benefits largely in the form of pension commitments based on pension units as well as under deferred compensation arrangements.

For the significant pension plans, pension commitments based on pension units largely result from the Schaeffler Company Pension Scheme ("Schaeffler Versorgungsordnung") and similar schemes that base the amount of the pension units on eligible income and also contain a minimum guarantee. When the Schaeffler Company Pension Scheme was introduced in 2006, the other pension schemes in Germany were closed to new entrants. Benefits are always paid on an annuity basis. The pension obligations arising from these pension commitments are financed by provisions. Current pension benefits are paid out of cash flows from operating activities.

In addition, employees have various deferred compensation arrangements to choose from. Some Schaeffler Group subsidiaries offer their staff a company pension model under which the employees contribute a portion of their pre-tax salary in return for a pension commitment. The compensation deferred is invested in equity, fixed-income, and money market funds under a lifecycle model, i.e. plan assets are moved to lower-risk asset classes as the beneficiary's age increases. In addition, the Schaeffler Group guarantees a minimum annual return. As benefits are paid in up to five annual installments starting when the beneficiary reaches retirement age, longevity risk is minimized. Benefit obligations resulting from the deferral of pre-tax compensation are covered by assets held separately under a contractual trust agreement (CTA).

U.S. and United Kingdom

Additional significant defined benefit plans cover employees in the U.S. and in the United Kingdom. The Schaeffler Group finances its pension obligations in these countries using external pension funds with restricted access. At the end of 2017, approx. 76% (prior year: 74%) of pension obligations in the U.S. and approx. 113% (prior year: 104%) of pension obligations in the United Kingdom were covered by plan assets. These pension plans were closed to new entrants in 2006 (U.S.) and 2009 (United Kingdom) and replaced with defined contribution plans. As a result, employees can no longer earn additional defined benefits.

Net defined benefit obligations

The company's obligations under defined benefit plans and the related plan assets are presented as follows in the consolidated statement of financial position as at December 31, 2017:

Amounts recognized in the statement of financial position for pensions and similar obligations No. 117

	12/31/2017					12/31/2016				
in € millions	Germany	U.S.	United Kingdom	Other countries	Total	Germany	U.S.	United Kingdom	Other countries	Total
Provisions for pensions (liabilities net of related plan assets)	-1,990	-51	-1	-82	-2,124	-2,029	-58	-4	-91	-2,182
Pension asset (plan assets net of related liabilities)	13	0	28	5	46	7	0	12	2	21
Net defined benefit liability	**-1,977**	**-51**	**27**	**-77**	**-2,078**	**-2,022**	**-58**	**8**	**-89**	**-2,161**

At the end of the reporting period, the defined benefit obligations and related plan assets amounted to the following:

Analysis of net defined benefit liability No. 118

	12/31/2017					12/31/2016				
in € millions	Germany	U.S.	United Kingdom	Other countries	Total	Germany	U.S.	United Kingdom	Other countries	Total
Present value of defined benefit obligations (active members)	-1,206	-76	0	-201	-1,483	-1,224	-84	0	-204	-1,512
Present value of defined benefit obligations (deferred members)	-154	-24	-159	-4	-341	-141	-27	-166	-4	-338
Present value of defined benefit obligations (pensioners)	-802	-110	-57	-29	-998	-825	-115	-65	-26	-1,031
Present value of defined benefit obligations (total)	**-2,162**	**-210**	**-216**	**-234**	**-2,822**	**-2,190**	**-226**	**-231**	**-234**	**-2,881**
Fair value of plan assets	185	159	243	157	744	168	168	239	145	720
Net defined benefit liability	**-1,977**	**-51**	**27**	**-77**	**-2,078**	**-2,022**	**-58**	**8**	**-89**	**-2,161**

Movements in the net defined pension benefit liability in 2017 can be reconciled as follows:

Reconciliation of net defined benefit liability/asset January 01/December 31 No. 119

					2017					2016
in € millions	Germany	U.S.	United Kingdom	Other countries	Total	Germany	U.S.	United Kingdom	Other countries	Total
Net defined benefit liability (-)/ asset (+) as at January 01	**-2,022**	**-58**	**8**	**-89**	**-2,161**	**-1,771**	**-59**	**25**	**-103**	**-1,908**
Benefits paid	59	1	0	7	67	58	1	0	9	68
Service cost	-70	0	0	-15	-85	-56	0	0	-19	-75
Net interest on net defined benefit liability	-34	-2	0	-2	-38	-42	-2	1	-2	-45
Employer contributions	-2	0	0	16	14	12	0	0	12	24
Employee contributions	0	0	0	0	0	1	0	0	0	1
Transfers in/out	0	-2	0	0	-2	0	-2	0	0	-2
Remeasurement of net defined benefit liability	92	6	19	3	120	-224	6	-15	10	-223
Business combinations/disposals	0	0	0	0	0	0	0	0	2	2
Changes in foreign exchange rates	0	4	0	3	7	0	-2	-3	2	-3
Net defined benefit liability (-)/ asset (+) as at December 31	**-1,977**	**-51**	**27**	**-77**	**-2,078**	**-2,022**	**-58**	**8**	**-89**	**-2,161**

The increase in **service cost** to EUR 85 m (prior year: EUR 75 m) in 2017 was mainly driven by the decrease in the discount rate for Germany as at December 31, 2016, to 1.7% from 2.3% as at the end of 2015. The reason is as follows: The decrease in the discount rate increases the settlement amount of the defined benefit plans, resulting in higher service cost than in the prior year.

Movements in defined benefit obligations

The opening and closing balances of the present value of the defined benefit obligations as at the end of the reporting period can be reconciled as follows:

Reconciliation of present value of defined benefit obligations January 01/December 31 No. 120

					2017					2016
in € millions	Germany	U.S.	United Kingdom	Other Countries	Total	Germany	U.S.	United Kingdom	Other Countries	Total
Present value of defined benefit obligations as at January 01	**-2,190**	**-226**	**-231**	**-234**	**-2,881**	**-1,919**	**-223**	**-204**	**-248**	**-2,594**
Benefits paid	62	10	9	14	95	61	11	10	18	100
Current service cost	-70	0	0	-14	-84	-56	0	0	-18	-74
Past service cost	0	0	0	-1	-1	0	0	0	-1	-1
Interest cost	-37	-9	-6	-6	-58	-45	-9	-7	-6	-67
Employee contributions	-11	-1	0	0	-12	-8	-1	0	-1	-10
Transfers in/out	1	0	0	0	1	0	0	0	0	0
Gains (+) / losses (-) – changes in financial assumptions	85	-11	-7	7	74	-235	0	-58	4	-289
Gains (+) / losses (-) – changes in demographic assumptions	0	2	10	0	12	0	4	0	-1	3
Gains (+) / losses (-) – experience adjustments	-2	-1	0	-6	-9	12	-1	0	2	13
Business combinations/disposals	0	0	0	0	0	0	0	0	20	20
Changes in foreign exchange rates	0	26	9	6	41	0	-7	28	-3	18
Present value of defined benefit obligations as at December 31	**-2,162**	**-210**	**-216**	**-234**	**-2,822**	**-2,190**	**-226**	**-231**	**-234**	**-2,881**

Movements in and types of plan assets

The opening and closing balances of the fair value of plan assets can be reconciled as follows:

Reconciliation of fair value of plan assets January 01/December 31 No. 121

					2017					2016
in € millions	Germany	U.S.	United Kingdom	Other countries	Total	Germany	U.S.	United Kingdom	Other countries	Total
Fair value of plan assets as at January 01	**168**	**168**	**239**	**145**	**720**	**148**	**164**	**229**	**145**	**686**
Benefits paid	-3	-9	-9	-7	-28	-3	-10	-10	-9	-32
Interest income on plan assets	3	7	6	4	20	3	7	8	4	22
Employee contributions	11	1	0	0	12	9	1	0	1	11
Employer contributions	-2	0	0	16	14	12	0	0	12	24
Transfers in/out	-1	-2	0	0	-3	0	-2	0	0	-2
Return on plan assets excluding interest income	9	16	16	2	43	-1	3	43	5	50
Business combinations/disposals	0	0	0	0	0	0	0	0	-18	-18
Changes in foreign exchange rates	0	-22	-9	-3	-34	0	5	-31	5	-21
Fair value of plan assets as at December 31	**185**	**159**	**243**	**157**	**744**	**168**	**168**	**239**	**145**	**720**

The Schaeffler Group plans to contribute EUR 9 m to plan assets in 2018.

Negative employer contributions represent refunds of additional contributions made in the past to cover temporary shortfalls.

Plan assets consisted of the following:

Classes of plan assets No. 122

					12/31/2017					12/31/2016
in € millions	Germany	U.S.	United Kingdom	Other Countries	Total	Germany	U.S.	United Kingdom	Other Countries	Total
Equity instruments	98	61	66	14	239	84	68	64	17	233
Debt instruments	32	100	47	134	313	28	99	47	112	286
Real estate	0	0	24	3	27	0	0	23	8	31
Cash	30	-2	1	0	29	32	1	2	1	36
(Reimbursement) insurance policies	25	0	0	6	31	24	0	0	7	31
Mixed funds	0	0	105	0	105	0	0	103	0	103
Total	**185**	**159**	**243**	**157**	**744**	**168**	**168**	**239**	**145**	**720**

Plan assets do not include real estate used by the Schaeffler Group or any of the Schaeffler Group's own equity instruments. Except for amounts related to real estate and reimbursement insurance policies, all amounts shown above represent market prices quoted in an active market.

Information on changes in the various classes of plan assets in Germany is provided by the fund manager in the form of performance reports and is regularly reviewed by investment committees. The investment strategy follows a lifecycle model: Plan assets are moved to lower-risk asset classes as the beneficiary's age increases.

Asset-liability studies are prepared for the funded defined benefit plans in the United Kingdom and in the U.S. at regular intervals, and the investment policy of each fund is based on the applicable study and any local legal requirements.

Comprehensive income

The following summarizes the various amounts recognized in comprehensive income for defined benefit plans:

Comprehensive income on defined benefit pension plans No. 123

					2017					2016
in € millions	Germany	U.S.	United Kingdom	Other countries	Total	Germany	U.S.	United Kingdom	Other countries	Total
Current service cost	70	0	0	14	84	56	0	0	18	74
Past service cost	0	0	0	1	1	0	0	0	1	1
• plan amendments	0	0	0	1	1	0	0	0	1	1
Gains (-)/losses (+) on settlements	0	0	0	0	0	0	0	0	0	0
Service cost	**70**	**0**	**0**	**15**	**85**	**56**	**0**	**0**	**19**	**75**
Interest cost	37	9	6	6	58	45	9	7	6	67
Interest income	-3	-7	-6	-4	-20	-3	-7	-8	-4	-22
Net interest on net defined benefit liability/asset	**34**	**2**	**0**	**2**	**38**	**42**	**2**	**-1**	**2**	**45**
Gains (-)/losses (+) – changes in financial assumptions	-85	11	7	-7	-74	235	0	58	-4	289
Gains (-)/losses (+) – changes in demographic assumptions	0	-2	-10	0	-12	0	-4	0	1	-3
Gains (-)/losses (+) – experience adjustments	2	1	0	6	9	-12	1	0	-2	-13
Return on plan assets excluding interest income	-9	-16	-16	-2	-43	1	-3	-43	-5	-50
Remeasurements of net defined benefit liability/asset	**-92**	**-6**	**-19**	**-3**	**-120**	**224**	**-6**	**15**	**-10**	**223**
Total comprehensive (income) loss on defined benefit obligations	**12**	**-4**	**-19**	**14**	**3**	**322**	**-4**	**14**	**11**	**343**

Service cost and interest on the net defined benefit liability are included in the following line items of the consolidated income statement:

Net pension expense in the consolidated income statement No. 124

					2017					2016
in € millions	Germany	U.S.	United Kingdom	Other countries	Total	Germany	U.S.	United Kingdom	Other countries	Total
Cost of sales	41	10	1	13	65	33	0	0	12	45
Research and development expenses	13	2	0	1	16	11	0	0	1	12
Selling expenses	5	2	0	6	13	4	0	0	3	7
Administrative expenses	11	1	0	2	14	8	0	0	2	10
Included in EBIT	**70**	**15**	**1**	**22**	**108**	**56**	**0**	**0**	**18**	**74**
Interest expense	37	9	6	6	58	45	9	7	6	67
Interest income on plan assets	-3	-7	-6	-4	-20	-3	-7	-8	-4	-22
Included in financial result	**34**	**2**	**0**	**2**	**38**	**42**	**2**	**-1**	**2**	**45**
Total	**104**	**17**	**1**	**24**	**146**	**98**	**2**	**-1**	**20**	**119**

Maturity profile of defined benefit obligations

The weighted average duration of defined benefit obligations is 18.7 years (prior year: 19.3 years) at year-end. In the most significant countries, Germany, the U.S., and the United Kingdom, the duration averages 19.7 years (prior year: 20.3 years), 11.7 years (prior year: 11.9 years), and 22.8 years (prior year: 24.0 years), respectively.

Over the next ten years, the company expects to make the following payments for the defined benefit obligations it has as at year-end:

Payments expected in coming years No. 125

in € millions	Payments expected
2018	88
2019	92
2020	99
2021	105
2022	111
2023–2027	587

Actuarial assumptions

At each reporting date, defined benefit obligations are measured based on certain actuarial assumptions.

The assumptions used, in particular discount rates, future salary increases, and future pension increases, are determined separately for each country.

The weighted averages of the principal actuarial assumptions for the Schaeffler Group are as follows:

Actuarial assumptions No. 126

	2017					2016				
	Germany	U.S.	United Kingdom	Other countries	Total [1]	Germany	U.S.	United Kingdom	Other countries	Total [1]
Discount rate as at December 31	1.9%	3.7%	2.6%	2.8%	2.2%	1.7%	4.2%	2.8%	2.6%	2.1%
Future salary increases	3.3%	n.a. [2]	n.a. [2]	3.2%	3.2%	3.3%	n.a. [2]	n.a. [2]	3.2%	3.3%
Future pension increases	1.8%	2.5%	3.3%	0.1%	1.9%	1.8%	2.5%	3.3%	0.1%	1.9%

[1] Average discount rate for the Schaeffler Group.
[2] The pension plans in the U.S. and in the United Kingdom have been closed since 2006 and 2009, respectively, and structured such that future salary increases will not affect the amount of the net liability.

Mortality assumptions are based on published statistics and country-specific mortality tables. The "RICHTTAFELN 2005 G" mortality tables developed by Prof. Dr. Klaus Heubeck and published by HEUBECK-RICHTTAFELN-GmbH are used for the German plans. These tables are generation tables, which specifically include appropriate assumptions to take into account future increases in life expectancy.

Sensitivity analysis

Selecting the assumptions discussed above is key to the calculation of the present value of the defined benefit obligation. The following table shows the sensitivity of the present value of the defined benefit obligation to changes in one of the key assumptions.

Sensitivity analysis of present value of defined benefit obligation No. 127

		2017					2016				
in € millions		Germany	U.S.	United Kingdom	Other countries	Total	Germany	U.S.	United Kingdom	Other countries	Total
Discount rate	Plus 1.0%	-352	-22	-42	-24	-440	-382	-25	-46	-25	-478
	Minus 1.0%	490	27	56	29	602	508	30	63	30	631
Future salary increases	Plus 1.0%	47	n.a. [1]	n.a. [1]	18	65	50	n.a. [1]	n.a. [1]	17	67
	Minus 1.0%	-41	n.a. [1]	n.a. [1]	-15	-56	-44	n.a. [1]	n.a. [1]	-15	-59
Future pension increases	Plus 1.0%	217	0	27	3	247	230	0	30	2	262
	Minus 1.0%	-162	0	-23	-2	-187	-190	0	-25	-1	-216

[1] The pension plans in the U.S. and in the United Kingdom have been closed since 2006 and 2009, respectively, and structured such that future salary increases will not affect the amount of the net liability.

Another key parameter in the measurement of the Schaeffler Group's pension obligations is life expectancy. An increase in life expectancy in the most significant countries by one year would lead to an increase in the present value of the corresponding obligation by EUR 102 m (prior year: EUR 106 m) in Germany, EUR 6 m (prior year: EUR 6 m) in the U.S., and EUR 9 m (prior year: EUR 9 m) in the United Kingdom.

As in the prior year, the above sensitivities were calculated using the same method as for the present value of the pension obligations as at the balance sheet date. The sensitivities presented above do not take into account interaction between assumptions; rather, the analysis assumes that each assumption changes separately. In practice, this would be unusual, as assumptions are frequently correlated.

Risk and risk management

The existing defined benefit plans expose the Schaeffler Group to the usual actuarial risks.

The existing plan assets are managed independently on a decentralized basis in the various countries.

Defined contribution plans

In 2017, the Schaeffler Group incurred EUR 22 m (prior year: EUR 20 m) in expenses related to defined contribution plans. At EUR 15 m (prior year: EUR 13 m), the majority of this amount relates to plans in the U.S.

4.12 Provisions

Provisions No. 128

in € millions	Employee benefits	Restructuring	Warranties	Other taxes	Other	Total
Balance as at January 01, 2017	**94**	**58**	**70**	**22**	**206**	**450**
Additions	52	39	66	5	68	230
Utilization	-47	-33	-30	-3	-79	-192
Reversals	-1	-18	-21	-6	-24	-70
Foreign currency translation	-1	0	-2	0	-9	-12
Balance as at December 31, 2017	**97**	**46**	**83**	**18**	**162**	**406**

Provisions consisted of the following non-current and current portions. Non-current provisions are due in one to five years.

Provisions (non-current/current) No. 129

			12/31/2017			12/31/2016
in € millions	Non-current	Current	Total	Non-current	Current	Total
Employee benefits	73	24	97	39	55	94
Restructuring	45	1	46	14	44	58
Warranties	0	83	83	0	70	70
Other taxes	0	18	18	0	22	22
Other	55	107	162	43	163	206
Total	**173**	**233**	**406**	**96**	**354**	**450**

Provisions for employee benefits consisted primarily of EUR 57 m (prior year: EUR 60 m) in provisions for long-time service awards and partial retirement programs primarily classified as non-current.

Restructuring provisions consisted mainly of EUR 39 m in provisions related to setting up a shared service center in Europe. Implementation of these measures will start in 2018 and is expected to be completed by 2022.

Warranty provisions consisted almost entirely of provisions for specific cases for which an outflow of resources within one year is considered probable.

Other provisions include, inter alia, provisions for potential third-party claims in connection with antitrust proceedings and other compliance cases of EUR 55 m (prior year: EUR 103 m). These provisions were classified as both current and non-current. The decrease in other provisions compared to the prior year is primarily attributable to the utilization of the provision for potential third-party claims in connection with the EU antitrust proceedings finalized in March 2014 of EUR 29 m.

Non-current provisions increased by EUR 77 m to EUR 173 m (prior year: EUR 96 m), primarily due to the provisions related to setting up a shared service center in Europe as discussed above.

Current provisions declined by EUR 121 m to EUR 233 m (prior year: EUR 354 m). The reason for this decline was twofold: The provision for potential third-party claims in connection with the EU antitrust proceedings finalized in March 2014 was utilized, and restructuring provisions related to the realignment of the Industrial division (first and second wave program “CORE”) recognized in the last two years were nearly fully utilized and partially reversed.

4.13 Other financial liabilities and other liabilities

Other financial liabilities (non-current/current) No. 130

			12/31/2017			12/31/2016
in € millions	Non-current	Current	Total	Non-current	Current	Total
Amounts payable to staff	2	299	301	0	262	262
Derivative financial liabilities	0	36	36	5	70	75
Miscellaneous other financial liabilities	22	347	369	81	364	445
Total	**24**	**682**	**706**	**86**	**696**	**782**

Amounts payable to staff included primarily profit sharing accruals.

Derivative financial liabilities included forward exchange contracts used to hedge the Schaeffler Group’s currency risk. The change was primarily attributable to a favorable trend in market value.

The decrease in **miscellaneous other financial liabilities** mainly reflects the payment of part of the third-party claims in connection with the EU antitrust proceedings finalized in March 2014. In addition, the consideration payable in connection with the acquisition of Compact Dynamics GmbH was paid in full (see Note 5.1). Payments received from customers for receivables sold under the ABCP program (see Note 5.2) and higher accrued selling costs (customer bonuses, rebates, early-payment discounts) had an offsetting effect.

More on the Schaeffler Group’s exposure to currency and liquidity risk in Note 4.14

Other liabilities (non-current/current) No. 131

			12/31/2017			12/31/2016
in € millions	Non-current	Current	Total	Non-current	Current	Total
Amonts payable to staff	0	152	152	0	138	138
Social security contributions payable	1	41	42	2	40	42
Advance payments received	0	34	34	0	25	25
Other tax payables	0	114	114	0	121	121
Miscellaneous other liabilities	6	26	32	4	20	24
Total	**7**	**367**	**374**	**6**	**344**	**350**

Amounts payable to staff primarily contained accrued vacation and overtime accounts.

Social security contributions payable consisted mainly of unpaid contributions to social security schemes.

Other tax payables included, in particular, value-added taxes payable and payroll withholding taxes payable.

4.14 Financial instruments

The carrying amounts and fair values of financial instruments by class of the consolidated statement of financial position and by category per IFRS 7.8 are summarized below. Investments in associated companies and derivatives subject to hedge accounting are also shown, although they do not fall into any of the IAS 39 measurement categories. No financial instruments were reclassified between categories.

Financial instruments by class and category in accordance with IFRS 7.8 No. 132

		12/31/2017		12/31/2016	
in € millions	Category per IFRS 7.8	Carrying amount	Fair value	Carrying amount	Fair value
Financial assets, by class					
Trade receivables	LaR	2,192	2,192	2,218	2,218
Other financial assets					
• Investments in associates [1]	n.a.	3	-	3	-
• Other investments [2]	AfS	17	-	14	-
• Marketable securities	AfS	16	16	17	17
• Derivatives designated as hedging instruments	n.a.	58	58	63	63
• Derivatives not designated as hedging instruments	HfT	85	85	141	141
• Miscellaneous other financial assets	LaR	46	46	34	34
Cash and cash equivalents	LaR	698	698	1,071	1,071
Financial liabilities, by class					
Financial debt	FLAC	3,068	3,165	3,707	3,820
Trade payables	FLAC	1,867	1,867	1,625	1,625
Other financial liabilities					
• Derivatives designated as hedging instruments	n.a.	11	11	40	40
• Derivatives not designated as hedging instruments	HfT	25	25	35	35
• Miscellaneous other financial liabilities	FLAC	670	670	707	707
Summary by category					
Available-for-sale financial assets (AfS)		33	-	31	-
Financial assets held for trading (HfT)		85	-	141	-
Loans and receivables (LaR)		2,936	-	3,323	-
Financial liabilities at amortized cost (FLAC)		5,605	-	6,039	-
Financial liabilities held for trading (HfT)		25	-	35	-

[1] Equity-accounted investees.
[2] Investments accounted for at cost.

The carrying amounts of trade receivables, miscellaneous other financial assets, cash and cash equivalents, trade payables, as well as miscellaneous other financial liabilities are assumed to equal their fair value due to the short maturities of these instruments.

Other investments include investments (shares in incorporated companies and cooperatives) for which quoted prices in an active market are not available. As a result, the fair value of these instruments cannot be measured reliably. These investments are therefore accounted for at cost. There were no partial disposals of such investments in 2017, and no (partial) disposals are planned in the foreseeable future. Marketable securities consist almost entirely of equity instruments in the form of money market fund units.

Hedge accounting is only applied to derivatives designated as hedges of currency risk in cash flow hedges. The Schaeffler Group uses cross-currency swaps and forward exchange contracts as hedging instruments here.

Please refer to the notes on the various balance sheet line items for the amount of financial assets pledged as collateral. Financial and non-financial assets of the Schaeffler Group have been pledged on the basis of the Facilities Agreement and the bond agreements (see Note 4.10). Collateral has generally been provided for the term of the loan and bond agreements and may be enforced if the creditors are entitled to call the debt, for instance if financial covenants are not met.

The fair values of financial assets and liabilities that are either measured at fair value or for which fair value is disclosed in the notes to the consolidated financial statements were determined using the following valuation methods and inputs:

- Level 1: Exchange-quoted prices as at the reporting date are used for marketable securities as well as bonds payable included in financial debt.
- Level 2: Cross-currency swaps and foreign exchange contracts are measured using discounted cash flow valuation models and the exchange rates in effect at the end of the reporting period as well as risk-adjusted interest and discount rates appropriate to the instruments' terms. These models take into account counterparty credit risk via credit value adjustments. Embedded derivatives are measured using a Hull-White model. Key inputs to this model are interest rates, volatilities, and credit default swap rates (CDS rates).
  The fair value of financial debt (except for the publicly listed bonds payable) is the present value of expected cash in- or outflows discounted using risk-adjusted discount rates that are appropriate to the term of the item being valued and that are in effect at the end of the reporting period.
- Level 3: The Schaeffler Group does not have any financial instruments in this level.

The following table summarizes the fair values and levels of financial assets and liabilities. Financial assets and liabilities whose carrying amount is assumed to represent their fair value have been omitted.

Financial assets and liabilities by fair value hierarchy level No. 133

in € millions	Level 1	Level 2	Total
December 31, 2017			
Marketable securities	16	-	16
Derivatives designated as hedging instruments	-	58	58
Derivatives not designated as hedging instruments	-	85	85
Total financial assets	**16**	**143**	**159**
Financial debt	2,071	1,094	3,165
Derivatives designated as hedging instruments	0	11	11
Derivatives not designated as hedging instruments	0	25	25
Total financial liabilities	**2,071**	**1,130**	**3,201**
December 31, 2016			
Marketable securities	17	-	17
Derivatives designated as hedging instruments	-	63	63
Derivatives not designated as hedging instruments	-	141	141
Total financial assets	**17**	**204**	**221**
Financial debt	2,813	1,007	3,820
Derivatives designated as hedging instruments	-	40	40
Derivatives not designated as hedging instruments	-	35	35
Total financial liabilities	**2,813**	**1,082**	**3,895**

The company reviews its financial instruments at the end of each reporting period for any required transfers between levels. No transfers between levels were made during the period.

Net gains and losses by category of financial instruments in accordance with IFRS 7.20 are as follows:

Net gains and losses by category of financial instruments in accordance with IFRS 7.20 No. 134

					2017	2016
		Subsequent measurement			Net income (loss)	
in € millions	Interest and dividends	at fair value	Impairment loss	Foreign currency translation		
Available-for-sale financial assets	-	1	-	-	1	0
Financial assets and liabilities held for trading	40	-131	-	-	-91	-9
Loans and receivables	11	-	2	-37	-24	44
Financial liabilities at amortized cost	-125	-	-	58	-67	-343
Total	**-74**	**-130**	**2**	**21**	**-181**	**-308**

Interest income and expense on financial assets and liabilities accounted for at amortized cost is included in interest income on financial assets and in interest expense on financial debt, respectively (see Note 3.5).

The net loss on financial assets and liabilities held for trading of EUR 91 m (prior year: EUR 9 m) relates entirely to derivatives. EUR 1 m (prior year: EUR 4 m) of this net loss is included in the financial result. Fair value changes on bifurcated embedded derivatives resulted in losses of EUR 14 m (prior year: EUR 30 m).

Financial risk management

Its financial instruments expose the Schaeffler Group to various risks.

Schaeffler's Board of Managing Directors has the overall responsibility for establishing and overseeing the group's risk management system. The finance department is responsible for developing and monitoring this risk management system and regularly reports to the Schaeffler Group's Chief Financial Officer on its activities in this area.

Group-wide risk management policies are in place to identify and analyze the Schaeffler Group's risks, set appropriate risk limits and controls, monitor risks, and adhere to the limits. Risk management procedures and systems are reviewed on a regular basis to reflect changes in market conditions and Schaeffler Group activities.

The Schaeffler Group has guidelines for the use of hedging instruments, and compliance with these guidelines is reviewed on a regular basis. Internal execution risk is minimized by strict segregation of duties.

Please refer to the "Report on opportunities and risks" in the combined management report for further detail on the group's financial risk management.

The Schaeffler Group distinguishes between liquidity risk, counterparty risk, and market risk (interest rate, currency, and other price risks).

Liquidity risk

The risk that the Schaeffler Group will not be able to meet its payment obligations as they come due is referred to as liquidity risk. The Schaeffler Group's approach to managing liquidity risk is to ensure that there is always sufficient liquidity available to meet liabilities as they come due without incurring unacceptable losses or risking damage to the Schaeffler Group's reputation.

Liquidity risk is monitored and managed using a rolling liquidity budget with a forecasting period of up to twelve months. Both the liquidity status and liquidity forecast are reported regularly to the Chief Financial Officer.

The Schaeffler Group uses equity, cash pooling arrangements, intercompany loans, receivable sale programs, and existing lines of credit based on the relevant legal and tax regulations to ensure it can meet the financing requirements of its operations and financial obligations. To this end, the Schaeffler Group has access to a revolving credit facility (RCF) of EUR 1.3 bn currently bearing interest at Euribor plus 0.80% as well as other bilateral lines of credit.

The Schaeffler Group's contractual payments of interest and principal on financial liabilities and derivative liabilities are summarized as follows:

Cash flows related to non-derivative and derivative financial liabilities No. 135

in € millions	Carrying amount	Contractual cash flows	Up to 1 year	1–5 years	More than 5 years
December 31, 2017					
Non-derivative financial liabilities	**5,605**	**6,007**	**3,662**	**1,164**	**1,181**
• Financial debt	3,068	3,469	1,146	1,142	1,181
• Trade payables	1,867	1,867	1,867	0	0
• Other non-derivative financial liabilities	670	671	649	22	0
Derivative financial liabilities	**36**	**36**	**36**	**0**	**0**
Total	**5,641**	**6,043**	**3,698**	**1,164**	**1,181**
December 31, 2016					
Non-derivative financial liabilities	**6,039**	**6,704**	**2,400**	**2,506**	**1,798**
• Financial debt	3,707	4,363	136	2,429	1,798
• Trade payables	1,625	1,625	1,625	0	0
• Other non-derivative financial liabilities	707	716	639	77	0
Derivative financial liabilities	**75**	**75**	**70**	**5**	**0**
Total	**6,114**	**6,779**	**2,470**	**2,511**	**1,798**

Contractual cash flows for financial debt include expected interest as well as the settlement amount of the loans. Contractual cash flows for derivative financial liabilities consist of the undiscounted expected cash flows translated at closing rates.

Counterparty risk

The risk that the Schaeffler Group will incur a financial loss as a result of a customer or business partner defaulting is called counterparty risk. This risk is primarily inherent in trade receivables and miscellaneous other financial assets.

Counterparty risk arising on trade receivables is managed by constantly monitoring customers' financial status, creditworthiness, and payment history. Additional measures to manage counterparty risk include efficient collection procedures and the use of commercial credit insurance. All relevant rules are outlined in a Schaeffler Group guideline.

Counterparty risk inherent in derivative financial instruments is the risk that counterparties will fail to meet some or all of their payment obligations. To mitigate this risk, such contracts are only entered into with selected banks.

The maximum counterparty risk at the reporting date, excluding collateral, is represented by the carrying amount of the corresponding financial asset.

The Schaeffler Group's Board of Managing Directors does not have any indications that the debtors will not meet their payment obligations with respect to trade receivables that are neither past due nor impaired. Except for amounts recognized in impairment allowances, there are no indications that the counterparties to other financial assets, i.e. marketable securities, derivative financial assets, and miscellaneous other financial assets, will be unable to meet their future contractual obligation.

Trade receivables in the Automotive division are subject to a concentration of risk on several automobile manufacturers (see Note 5.5). Receivables from ten automobile manufacturers make up 39.0% (prior year: 38.4%) of trade receivables.

Interest rate risk

Variable interest features give rise to the risk of rising interest rates on financial liabilities and falling interest rates on financial assets. This risk is measured, assessed and, where necessary, hedged using derivative interest rate hedging instruments. The hedged item is the Schaeffler Group's interest-bearing net financial debt.

The Schaeffler Group's financial debt can be summarized by type of interest as follows:

Variable and fixed interest financial debt No. 136

	12/31/2017	12/31/2016
in € millions	Carrying amount	
Variable interest instruments	**1,072**	**983**
• Financial debt	1,072	983
Fixed interest instruments	**1,996**	**2,724**
• Financial debt	1,996	2,724

IFRS 7 requires the disclosure of the impact of financial instruments on net income and shareholders' equity as a result of changes in interest rates in the form of sensitivity analyses.

The sensitivity calculation assumes that all other variables, particularly exchange rates, remain constant and that contractual arrangements prevent interest rates from falling below 0%. With regard to variable interest instruments, a shift in the yield curve of 100 basis points (Bp) as at December 31, 2017, would affect (increase/decrease) net income and shareholders' equity as follows:

Sensitivity analysis: Shift in yield curve No. 137

	Net income (loss)		Shareholders' equity	
in € millions	Plus 100 Bp	Minus 100 Bp	Plus 100 Bp	Minus 100 Bp
As at December 31, 2017				
Variable interest instruments	-6	0	0	0
Derivatives designated as hedging instruments	0	0	0	0
Derivatives not designated as hedging instruments	-22	82	0	0
Total	**-28**	**82**	**0**	**0**
As at December 31, 2016				
Variable interest instruments	-7	0	0	0
Derivatives designated as hedging instruments	0	0	-2	2
Derivatives not designated as hedging instruments	-22	6	0	0
Total	**-29**	**6**	**-2**	**2**

The impact of variable interest instruments is solely due to an increase or decrease in the interest charge.

Currency risk

The Schaeffler Group is exposed to currency risk on sales, purchases, and loans payable and receivable, as well as financial debt that are denominated in a currency other than the functional currency of the relevant Schaeffler Group entity.

Currency risk from operations

The international nature of the Schaeffler Group's operations involves the flow of goods and cash in a wide range of currencies. This gives rise to currency risk, as the value of assets denominated in a currency with a falling exchange rate declines while the value of liabilities denominated in a currency whose exchange rate is rising will increase.

The Schaeffler Group's significant currency risk exposures from operations by currency based on face values as of the end of each reporting period are as follows:

Currency risk from operations No. 138

in € millions	USD	CNY	RON	PLN
December 31, 2017				
Estimated currency risk from operations	807	573	-201	174
Forward exchange contracts	-606	-470	160	-131
Remaining currency risk from operations	**201**	**103**	**-41**	**43**
December 31, 2016				
Estimated currency risk from operations	730	533	-197	157
Forward exchange contracts	-573	-413	143	-119
Remaining currency risk from operations	**157**	**120**	**-54**	**38**

Estimated currency risk from operations represents the currency risk from operating and investing activities within twelve months after the end of each reporting period. The remaining currency risk from operations reflects the combined exposure of all Schaeffler Group entities not subject to local restrictions on foreign exchange transactions with Schaeffler's finance department. Thus, this exposure represents the difference between hedged items, both recognized and in the form of expected future foreign currency cash flows that have not yet been recognized, on the one hand and hedging instruments that have been recognized in the statement of financial position on the other hand. Currency risk in countries with foreign exchange restrictions (see Note 4.7) is monitored by Schaeffler's finance department. The most significant currency risk exposures in these countries arise on the Chinese renminbi and the Indian rupee and amount to an estimated EUR 58 m (prior year: U.S. dollar of EUR 76 m).

At any point in time the Schaeffler Group hedges a major portion of its estimated currency risk from operations in respect of forecasted sales and purchases over the next twelve months using mainly forward exchange contracts.

IFRS 7 requires entities to disclose the impact of hypothetical changes in exchange rates on net income and shareholders' equity using sensitivity analyses. Exchange rate changes are applied to all of the Schaeffler Group's financial instruments as at the end of the reporting date. The analysis covers foreign currency trade receivables and payables as well as derivative financial instruments used to hedge foreign currency risk.

The sensitivity analysis for currency risk from operations is based on a hypothetical 10% weakening of the euro against each of the significant foreign currencies as of December 31, 2017, assuming all other variables, particularly interest rates, remain constant.

The following table shows the effect on net income and shareholders' equity of translating balances at the closing rate and of measuring instruments at fair value:

Sensitivity analysis: changes in foreign exchange rates – operations No. 139

	12/31/2017		12/31/2016	
in € millions	Net income (loss)	Shareholders' equity	Net income (loss)	Shareholders' equity
USD	9	-59	15	-67
CNY	23	-39	19	-39
HUF	9	11	6	10
PLN	0	-13	0	-12

Conversely, a 10% rise in the euro against the significant foreign currencies as at December 31, 2017, would have had the same but opposite effect, again holding all other variables constant.

Currency risk from financing

Loans and deposits between Schaeffler Group companies denominated in a currency other than the functional currency of the entities are fully hedged on a net basis using forward exchange contracts.

A portion of the company's external financial debt denominated in a currency other than the functional currency is hedged using cross-currency swaps with notional amounts totaling USD 400 m (prior year: USD 800 m). Changes in the fair value of those cross-currency swaps not subject to hedge accounting (notional amount of USD 0 m; prior year: USD 400 m) were recognized directly in profit or loss in 2017.

The sensitivity analysis for currency risk from financing activities is based on a hypothetical 10% weakening of the euro against the U.S. dollar as at December 31, 2017. The analysis covers foreign currency financial debt and derivative financial instruments used to hedge foreign currency risk related to financing and assumes that all other variables, particularly interest rates, remain constant.

Sensitivity analysis: changes in foreign exchange rates – financing activities No. 140

	12/31/2017		12/31/2016	
in € millions	Net income (loss)	Shareholders' equity	Net income (loss)	Shareholders' equity
Foreign exchange gains and losses on financial debt	-33	-16	-76	-47
Foreign exchange gains and losses on derivatives	33	11	80	7
Total	**0**	**-5**	**4**	**-40**

Foreign exchange gains and losses on financial debt affecting shareholders' equity relate to a hedge of a net investment in a foreign operation.

Other price risks

Other price risks normally includes the risk of changes in stock-market prices and stock price indices as well as changes in commodity prices to the extent purchase agreements for commodities are treated as financial instruments due to the requirements of IAS 39, which is not the case for the Schaeffler Group.

Commodity price risk is hedged using long-term supply agreements that include price adjustment clauses.

Risks related to stock-market prices and stock price indices only arise from marketable securities. In light of the size of the Schaeffler Group's holdings of such financial instruments, the price risk related to these items is considered insignificant.

Derivative financial instruments and hedging relationships

Using derivative financial instruments to manage risk is one component of the Schaeffler Group's risk management system. Nominal values and fair values of derivative financial instruments as at the reporting date were as follows:

Summary of derivative financial instruments No. 141

	12/31/2017		12/31/2016	
in € millions	Nominal value	Fair value	Nominal value	Fair value
Financial assets				
Currency hedging				
Forward exchange contracts	2,039	73	1,458	32
• thereof: hedge accounting	983	39	439	6
Cross-currency swaps	384	18	759	108
• thereof: hedge accounting	384	18	380	57
Financial liabilities				
Currency hedging				
Forward exchange contracts	1,698	36	2,106	75
• thereof: hedge accounting	693	11	1,166	40
Cross-currency swaps	0	0	57	0
• thereof: hedge accounting	0	0	57	0

Cash flow hedges

A portion of the Schaeffler Group's forward exchange contracts and cross-currency swaps in certain currencies are accounted for as cash flow hedges with perfect effectiveness. Both the majority of the forecasted transactions and the resulting impact on net income occur within one year of the end of the reporting period.

The portion of the hedging reserve in accumulated other comprehensive income that relates to hedges of currency risk from operations changed as follows:

Reconciliation of hedging reserve related to currency risk – operations No. 142

in € millions	2017	2016
Balance as at January 01	**-34**	**3**
Additions	33	-34
Reclassified to income statement		
• to other income	0	-3
• to other expense	34	0
Balance as at December 31	**33**	**-34**

The Schaeffler Group also applies cash flow hedge accounting to the foreign currency hedge of its bond issued in U.S. dollars using cross-currency swaps with a nominal value of USD 400 m (prior year: USD 400 m). As a result, accumulated gains of EUR 3 m (prior year: gains of EUR 27 m) representing the effective portion of fair value changes on designated financial instruments were recognized in other comprehensive income and reported in accumulated other comprehensive income as at December 31, 2017. There was no ineffectiveness. The foreign exchange effects hedged will be recognized in profit or loss in the years 2018 to 2023.

The portion of the hedging reserve in accumulated other comprehensive income that relates to hedges of currency risk from financing activities changed as follows:

Reconciliation of hedging reserve related to currency risk – financing activities No. 143

in € millions	2017	2016
Balance as at January 01	**-15**	**-42**
Additions	-43	-51
Reclassified to income statement		
• to financial income	0	0
• to financial expense	46	78
Balance as at December 31	**-12**	**-15**

Net investment in a foreign operation

The Schaeffler Group hedges the currency risk of part of its net investments in its U.S. subsidiaries using a portion of its financial debt denominated in U.S. dollars under a net investment hedge (principal of USD 200 m; prior year: USD 500 m). This mitigates the group's translation risk on the U.S. subsidiaries. As a result, foreign exchange gains of EUR 13 m (prior year: losses of EUR 10 m) on designated financial debt were recognized in other comprehensive income in 2017 and reported in accumulated other comprehensive income (translation reserve) as at December 31, 2017. The hedging relationship did not produce any ineffectiveness that would have had to be recognized separately. Investments in the group's other subsidiaries are not hedged.

Offsetting financial assets and financial liabilities

Certain Schaeffler Group companies enter into derivatives based on the German Master Agreement for Financial Forward Transactions ("Deutscher Rahmenvertrag für Finanztermingeschäfte" – DRV) or on the master agreement of the International Swaps and Derivatives Association (ISDA). These agreements permit each counterparty to combine all amounts relating to outstanding transactions due on the same date and in the same currency, arriving at one net amount to be paid by one of the parties to the other. In certain cases, for instance when a credit event such as default occurs, all transactions outstanding under this agreement are terminated, their fair value upon termination is determined, and only a single net amount is payable in settlement of all of these transactions.

The German Master Agreements and ISDA agreements do not meet the criteria for offsetting in the consolidated statement of financial position, as the Schaeffler Group does not currently have a legal right to settle the recognized amounts on a net basis. The right to settle net is only legally enforceable upon the occurrence of future events such as the insolvency of one of the parties to the contract. Hedging transactions entered into directly by Schaeffler Group subsidiaries do not permit net settlement, either.

The carrying amounts of the financial assets and liabilities subject to these agreements, except for the embedded options, are as follows:

Offsetting financial assets and financial liabilities No. 144

in € millions	12/31/2017	12/31/2016
Financial assets		
Gross amount of financial assets	92	139
Amounts offset in accordance with IAS 32.42	0	0
Net amount of financial assets	92	139
Amounts subject to master netting arrangements		
• Derivatives	-36	-62
Net amount of financial assets	56	77
Financial liabilities		
Gross amount of financial liabilities	36	75
Amounts offset in accordance with IAS 32.42	0	0
Net amount of financial liabilities	36	75
Amounts subject to master netting arrangements		
• Derivatives	-36	-62
Net amount of financial liabilities	0	13

4.15 Share-based payment

In connection with the Schaeffler AG listing in October 2015, the company implemented its first share-based payment instrument in the form of a Performance Share Unit Plan (PSUP) for members of Schaeffler AG's Board of Managing Directors. The virtual shares granted (known as Performance Share Units, PSUs) entitle the holder to a cash payment equal to the average share price of Schaeffler AG's common non-voting shares on the vesting date. The PSUs are granted in annual tranches. Each tranche has a performance period of four years beginning on January 01 of the year in which the tranche is granted. Due to the listing, however, the grant date of the 2015 tranche is October 09, 2015. In October 2016, the Board of Managing Directors decided to extend the PSUP to selected members of the Schaeffler Group's senior management. For eligible senior management, the performance period of the 2016 tranche begins retroactively on January 01, 2016. However, the grant date of the 2016 tranche is October 01, 2016. The grant date of the 2017 tranche is January 01, 2017, except for one member of the Board of Managing Directors, whose grant date is July 17, 2017.

Vesting of PSUs is linked to the following three conditions:

- 50% of PSUs are granted subject to a service condition (base number). The base number is only paid out if the beneficiary remains employed with the Schaeffler Group and is not under notice of termination at the end of the performance period.
- 25% of the PSUs are granted subject to a long-term performance target based on free cash flow (FCF), which involves a comparison of accumulated FCF for the performance period to the target FCF.
- 25% of the PSUs are granted subject to a relative performance target based on total shareholder return (TSR) (share price performance including dividends). To determine to what extent these PSUs have vested, TSR for Schaeffler AG's common non-voting shares is compared to the TSR of companies in the benchmark group (MDAX) over the performance period.

The number of PSUs actually payable at the end of the performance period depends on the extent to which the performance targets have been achieved and whether the service condition has been met and can vary between 0% and 100%. The amount payable per PSU is capped at double the underlying price of Schaeffler AG common non-voting shares at the grant date.

Obligations under the PSUP as at December 31, 2017, amounted to EUR 9.8 m (prior year: EUR 3.5 m) and were included in non-current provisions. Net expenses arising from the PSUP for 2017 totaled EUR 6.3 m (prior year: EUR 2.8 m). There were 2,417,229 PSUs (prior year: 1,310,594 PSUs) in total as at December 31, 2017. All PSUs granted were still outstanding as at December 31, 2017.

The average fair value of a PSU granted was EUR 11.71 (prior year: EUR 11.31) as at December 31, 2017. PSUs included in the base number as well as those subject to the FCF-based performance target are measured based on the price of Schaeffler AG common non-voting shares taking into account the present value of dividends, which beneficiaries are not entitled to during the vesting period, as well as the cap.

The fair value of PSUs with a TSR-based performance target is determined using a binomial model. The valuation model used takes into account the terms of the contract under which the PSUs were granted (including payment floors and caps, target range for the TSR-based performance target, dividends expected to be paid on Schaeffler AG common non-voting shares, as well as the volatility of Schaeffler AG common non-voting shares and the benchmark index MDAX). The valuation reflects the following input parameters:

Binomial model – input parameters No. 145

	12/31/2017	12/31/2016
Average risk-free interest rate for the remaining performance period	-0.50%	-0.35%
Expected dividend yield of Schaeffler AG common non-voting shares	3.38%	2.49%
Expected volatility of Schaeffler AG common non-voting shares	28.61%	34.27%
Expected volatility of the benchmark index	10.32%	18.75%
Expected correlation between the benchmark index and Schaeffler AG common non-voting shares	0.46	0.61

Expected future volatilities and the correlation between Schaeffler AG common non-voting shares and the benchmark group (MDAX) were estimated based on the daily closing prices of Schaeffler AG common non-voting shares and the benchmark group (MDAX) in the XETRA trading system of the German Stock Exchange.

4.16 Capital management

The Schaeffler Group has a strategy of pursuing profitable long-term growth. Capital is managed proactively to secure the existence of the company as a going concern for the long term and create financial flexibility for profitable growth in order to add long-term value to the company. A further aim is to ensure that a portion of the company's net income is paid out to shareholders in dividends.

Corporate capital management provides the financial resources required by Schaeffler Group entities, ensures the long-term availability of liquidity, and secures the Schaeffler Group's credit standing. Capital management also administers and continually improves the company's existing financial debt consisting of its external group financing arrangements. Capital management also strives to improve the quality of the Schaeffler Group's balance sheet, measured in terms of the development of the ratio of net financial debt to equity including non-controlling interests (gearing ratio). The gearing ratio was 93.0% at December 31, 2017 (prior year: 132.0%).

The Schaeffler Group has an effective cash management system in place and has diversified its external financing in terms of, for instance, instruments and maturities. The Schaeffler Group can currently utilize cash and cash equivalents, cash flow from operations, various loan facilities, and debt and equity funding via the capital markets to meet its short-, medium-, and long-term financing needs. The next maturity date of bonds or credit facilities is in 2020. Currency risk is continually monitored and reported at corporate level. Currency risk is aggregated across the group and hedged using hedging instruments.

In addition, the Schaeffler Group uses receivable sale programs to a limited extent to manage liquidity and improve its working capital. For this purpose, the company has access to an ABCP program of revolving sales of trade receivables with a committed volume of EUR 150 m (prior year: EUR 0 m) (see Note 5.2). Additionally, the Schaeffler Group has the ability to selectively use a further receivable sale program without a fixed committed volume.

The Schaeffler Group's management will continue to focus on the group's ability to place financial instruments with a broad range of investors and to further improve financing terms. Credit ratings assigned by external rating agencies are key to this ability. In 2017, the Schaeffler Group obtained ratings from rating agencies Standard & Poor's and Moody's and, since April 25, 2017, from Fitch Ratings as well. As a basis for executing its growth strategy, the company intends to maintain the investment grade rating it initially gained in 2016 for the long term.

Under its existing debt financing agreements, the Schaeffler Group is subject to certain constraints including a requirement to meet a leverage covenant. The inputs to the calculation of the leverage covenant are defined in the debt agreements and cannot be derived directly from amounts in the consolidated financial statements. As in prior years, the company has complied with the leverage covenant throughout 2017 as stipulated in the debt agreements. Based on its forecast, the Schaeffler Group also expects to comply with the leverage covenant in subsequent years.

In addition to the leverage covenant contained in the debt agreements, the Schaeffler Group regularly calculates further financial indicators. The gearing ratio discussed above and the net debt to EBITDA ratio are two such further financial indicators. The net debt to EBITDA ratio – the ratio of net financial debt to EBITDA (earnings before financial result, income taxes, depreciation, amortization, and impairment losses) – is calculated as follows:

Net financial debt to EBITDA ratio No. 146

in € millions	12/31/2017	12/31/2016
Current financial debt	2	3
Non-current financial debt	3,066	3,704
Financial debt	**3,068**	**3,707**
Cash and cash equivalents	698	1,071
Net financial debt	**2,370**	**2,636**
Earnings before financial result, income taxes, depreciation, and amortization and impairment losses (EBITDA) [1]	**2,295**	**2,293**
Net financial debt to EBITDA ratio [2]	**1.0**	**1.1**

[1] EBITDA incl. EUR 56 m (prior year: EUR 144 m) in special items.
[2] Net financial debt to EBITDA ratio incl. special items (footnote 1).

5. Other disclosures

5.1 Additional disclosures on the consolidated statement of cash flows

Changes in balance sheet items shown in the consolidated statement of cash flows cannot be derived directly from the consolidated statement of financial position, as they have been adjusted for the impact of foreign currency translation.

In connection with the repayment of the USD bond series, Schaeffler AG also terminated a portion of the cross-currency swaps designed to hedge the currency fluctuations before maturity. The termination resulted in cash inflows of EUR 38 m due to exchange rate changes. These cash inflows from the hedging instrument as well as the cash outflows from the hedged item are presented under repayments of loans.

The purchase price for the acquisition of Compact Dynamics GmbH of EUR 45 m was paid in full in 2017. Further cash outflows of EUR 2 m represented the payment of the 1st tranche of the purchase price for the acquisition of autinity GmbH. A 2nd tranche of EUR 2 m was payable in January 2018. These outflows were partially offset by proceeds of EUR 4 m on the disposal of Schaeffler Motorenelemente AG & Co. KG and EUR 16 m on the sale of the fine blanking activities of Schaeffler Schweiz GmbH. The inflow of the EUR 2 m in cash received as part of the acquisition of Compact Dynamics GmbH was reflected in other investing activities in 2016.

Summary of changes in financial debt No. 147

				Financial debt	Cross-currency swaps held or hedging purposes		Total
in € millions	Bonds	Facilities agreement	Capital investment loan	Other financial debt	Financial assets	Financial liabilities	
Balance as at January 01, 2017	**2,719**	**982**	**0**	**6**	**-108**	**0**	**3,599**
Changes from financing cash flows							
Receipts from loans	0	350	90	0	0	0	440
Repayments of loans	-625	-350	0	-3	38	0	-940
Total changes from cash flows	**-625**	**0**	**90**	**-3**	**38**	**0**	**-500**
Changes arising from obtaining or losing control of subsidiaries or other businesses	**0**	**0**	**0**	**0**	**0**	**0**	**0**
Effect of changes in foreign exchange rates	**-105**	**0**	**0**	**0**	**0**	**0**	**-105**
Changes in fair values	**0**	**0**	**0**	**0**	**57**	**0**	**57**
Other non-cash changes	**5**	**1**	**-1**	**-1**	**0**	**0**	**4**
Balance as at December 31, 2017	**1,994**	**983**	**89**	**2**	**-13**	**0**	**3,055**

5.2 Involvement with unconsolidated structured entities

The Schaeffler Group sells a portion of its trade receivables to a structured entity under an ABCP program (asset-backed commercial paper). The structured entity obtains its funding primarily from the capital markets. The receivables are sold on a revolving basis at their face value less variable reserves and a variable fee discount. The structured entity has engaged the Schaeffler Group to service the receivables in return for an arm's-length fee. The structured entity has the right to remove the Schaeffler Group as the servicer and to engage someone else to service the receivables. The Schaeffler Group has concluded that it does not control the structured entity and, therefore, does not consolidate it.

The sold receivables (see Note 4.5) as well as the related liabilities are recognized to the extent of the company's continuing involvement measured as the amount of the risks retained.

The following balances relate to the Schaeffler Group's involvement with the structured entity as at December 31, 2017:

Balances – involvement with the structured entity No. 148

in € millions	12/31/2017	12/31/2016
Carrying amount of receivables transferred	123	0
Carrying amount of risks and collateral retained in relation to the receivables transferred (recognized as other assets in the statement of financial position)	14	0
Payments received from customers on receivables sold and not yet passed on to the structured entity transferred (recognized as other financial liabilities in the statement of financial position)	42	0
Carrying amount of receivables (classified as trade receivables) and the other liability resulting from the continuing involvement (classified in other financial liabilities in the statement of financial position)	2	0

The ABCP program resulted in a cash inflow of EUR 150 m classified in cash flows from operating activities.

5.3 Leases

Future minimum lease payments under non-cancelable operating rental and lease agreements are due as follows:

Rental and lease agreements No. 149

in € millions	12/31/2017	12/31/2016
Less than one year	57	58
Between one and five years	65	60
More than five years	11	5
Total	**133**	**123**

The obligations consisted primarily of rental agreements for real estate and lease agreements relating to company vehicles and IT and logistics.

In 2017, the Schaeffler Group recognized EUR 89 m (prior year: EUR 85 m) in expenses related to operating rental and lease agreements in profit or loss.

5.4 Contingent liabilities

At December 31, 2017, the Schaeffler Group had contingent liabilities of EUR 74 m (prior year: EUR 46 m). These do not include any items that individually have a material adverse impact on the Schaeffler Group's net assets, financial position, and earnings.

Since 2011, several antitrust authorities have been investigating several manufacturers of rolling bearings and other vendor parts for the automotive sector. The authorities are investigating possible agreements violating antitrust laws. Schaeffler Group companies are among the entities subject to these investigations. In addition, there is a risk that third parties may claim damages in connection with antitrust proceedings that are either ongoing or have been finalized. As at the end of the reporting period, the Schaeffler Group has recognized provisions for a portion of these investigations and potential claims for damages. Additional penalties or claims for damages cannot be ruled out, but can currently not be estimated.

5.5 Segment information

In accordance with IFRS 8, segment information is reported under the management approach, reflecting the internal organizational and management structure including the internal reporting system to the Schaeffler AG Board of Managing Directors. Schaeffler engages in business activities (1) from which it may earn revenues and incur expenses, (2) whose EBIT is regularly reviewed by the Schaeffler Group's Board of Managing Directors and used as a basis for future decisions on how to allocate resources to the segments and to assess their performance, and (3) for which discrete financial information is available.

The Schaeffler Group is divided into the two segments Automotive division and Industrial division as described below. The segments offer different products and services and are managed separately because they require different technology and marketing strategies. Each segment focuses on a specific worldwide group of customers. Consequently, the amounts for revenue, EBIT, assets, additions to intangible assets and property, plant and equipment, as well as amortization, depreciation, and impairment losses are reported based on the current allocation of customers to divisions. The allocation of customers to segments and the allocation of indirect expenses was reviewed and adjusted during the year. To ensure that the information on the Automotive division and Industrial division segments is comparable, prior year information was also presented using the current year's customer structure. Revenue related to transactions between operating segments is not included.

The following summary describes the operations of each of the Schaeffler Group's two reportable segments:

Automotive

Product and service business with customers in the automotive sector. These include primarily manufacturers of passenger cars and commercial vehicles (OEM), automotive suppliers (Tier 1 and Tier 2), as well as companies focusing on the distribution of spare parts for passenger cars and commercial vehicles (aftermarket). The Automotive division is working on a wide range of technologies for the various drive concepts, markets and regions and delivers appropriate solutions for the most varied requirements of the automotive industry. This includes precision components and systems for engines, transmissions, and chassis of vehicles with drivetrains based on the internal combustion engine just as much as applications for hybrid and electric vehicles. The Automotive Aftermarket business division is responsible for the global business with spare parts and provides innovative repair solutions in original-equipment quality, focusing especially on comprehensive services for repair shops.

Industrial

Product and service business with manufacturers of investment goods. Specifically, these customers operate in the production machinery, drive technology, wind power, construction machinery/tractors, consumer goods, heavy industries, rail traffic and power transmission sectors as well as in the industrial aftermarket. The business with customers in the aerospace industry is also included in this segment. The Industrial division's product spectrum includes rolling and plain bearings, linear technology, maintenance products, monitoring systems, and direct drive technology. The Industrial division offers a broad portfolio of bearing solutions, ranging from high-speed and high-precision bearings with small diameters to large-size bearings over three meters in diameter. The focus here is increasingly on smart products and on connecting components.

Information on the operating activities of the two reportable segments is included below. Performance is measured based on EBIT, as the Board of Managing Directors believes that this information is most relevant in evaluating the results of the segments in relation to other entities that operate within these industries.

Reconciliation to earnings before income taxes No. 150

in € millions	2017	2016
EBIT Automotive [1]	1,283	1,373
EBIT Industrial [1]	245	183
EBIT	**1,528**	**1,556**
Financial result	-192	-341
Earnings before income taxes	**1,336**	**1,215**

[1] Prior year information presented based on 2017 segment structure.

In 2017, the Schaeffler Group generated revenue of EUR 1,488 m (prior year: EUR 1,462 m) from one key customer, representing 10.6% (prior year: 11.0%) of total group revenue and 13.7% (prior year: 14.1%) of Automotive segment revenue.

In addition to the divisions and functions, the Schaeffler Group's multidimensional organizational structure is also based on the four regions Europe, Americas, Greater China, and Asia/Pacific. The Automotive division and Industrial division segments are managed on a global basis and operate production and distribution facilities in all four regions. Revenue and non-current assets of the four regions were as follows in 2017:

Information about geographical areas No. 151

	2017	2016	12/31/2017	12/31/2016
in € millions		Revenue [1]		Non-current assets [2]
Europe	7,183	7,077	3,344	3,039
Americas	2,910	2,803	769	818
Greater China	2,456	2,053	1,027	932
Asia/Pacific	1,472	1,405	361	350
Total	**14,021**	**13,338**	**5,501**	**5,139**

[1] Revenue by market (customer locations). Prior year information presented based on 2017 segment structure.
[2] Non-current assets by Schaeffler location. Non-current assets consist of intangible assets and property, plant and equipment.

Germany, China, and the U.S. had revenue of EUR 2,614 m (prior year: EUR 2,818 m), EUR 2,394 m (prior year: EUR 1,992 m), and EUR 1,881 m (prior year: EUR 1,830 m) as well as non-current assets of EUR 2,017 m (prior year: EUR 1,757 m), EUR 1,027 m (prior year: EUR 931 m), and EUR 422 m (prior year: EUR 476 m), respectively.

Effective January 01, 2018, the Automotive Aftermarket was separated from the Automotive division of Schaeffler AG and set up as a third stand-alone division.

5.6 Related parties

Related persons

All common shares in Schaeffler AG are indirectly held by Maria-Elisabeth Schaeffler-Thumann and Georg F. W. Schaeffler. Under the definitions of IAS 24, Maria-Elisabeth Schaeffler-Thumann and Georg F. W. Schaeffler and the close members of their family are related parties of the Schaeffler Group.

The Schaeffler Group does not have any significant direct business relations with Maria-Elisabeth Schaeffler-Thumann and Georg F. W. Schaeffler.

Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the Schaeffler Group, directly or indirectly. For the Schaeffler Group, the members of the Board of Managing Directors and the Supervisory Board of Schaeffler AG represent key management personnel, making them and the close members of their family related parties of Schaeffler AG.

The remuneration of the Board of Managing Directors of Schaeffler AG for 2017 in accordance with IAS 24 totaled EUR 19 m (prior year: EUR 19 m), including EUR 12 m (prior year: EUR 12 m) in short-term benefits. Expenses of EUR 2 m (prior year: EUR 3 m) were recognized for post-employment benefits. Termination benefits amounted to EUR 1 m (prior year: EUR 0 m), and share-based payments totaled EUR 4 m (prior year: EUR 3 m).

Total remuneration of the Board of Managing Directors in accordance with section 314 (1) (6a) (1-3) HGB amounted to EUR 17 m (prior year: EUR 19 m) in 2017.

In addition, the company has committed to pay two Managing Directors advances of EUR 300 thousand each for 2017 and payments of EUR 300 thousand and EUR 225 thousand, respectively, for 2018, and has also committed to pay EUR 300 thousand to one of these Managing Directors for 2019; these payments will be offset against payment of the long-term bonuses granted in 2017, 2018, and 2019.

The following share-based remuneration was granted to members of the Board of Managing Directors in 2017 under the Performance Share Unit Plan (PSUP) implemented in 2015: 277,722 Performance Share Units (PSU) subject to a service condition (fair value per PSU at grant date of EUR 11.84 and EUR 10.67, respectively), 138,864 PSUs subject to an FCF-based performance target (fair value per PSU at grant date of EUR 11.84 and EUR 10.67, respectively), and 138,864 PSUs with a TSR-based performance target (fair value per PSU at grant date of EUR 6.99 and EUR 4.58, respectively).

The following share-based remuneration was granted to members of the Board of Managing Directors in the prior year: 252,051 Performance Share Units (PSU) subject to a service condition (fair value per PSU at grant date of EUR 13.82), 126,033 PSUs subject to an FCF-based performance target (fair value per PSU at grant date of EUR 13.82), and 126,033 PSUs with a TSR-based performance target (fair value per PSU at grant date of EUR 9.13). Please refer to the remuneration report for a detailed discussion of the PSUP.

Short-term benefits paid to members of Schaeffler AG's Supervisory Board, which became operational in early December 2014, amounted to EUR 1.6 m (prior year: EUR 1.6 m).

The company did not pay any other benefits to its key management personnel.

The remuneration system for the Board of Managing Directors and the Supervisory Board of Schaeffler AG is outlined in the remuneration report. The remuneration report also includes information on the remuneration of individual members of the Board of Managing Directors and additional information required by section 314 (1) (6) HGB.

Former members of the Board of Managing Directors (and their surviving dependants) of Schaeffler AG and its legal predecessors received remuneration of EUR 4 m in 2017 (prior year: EUR 3 m).

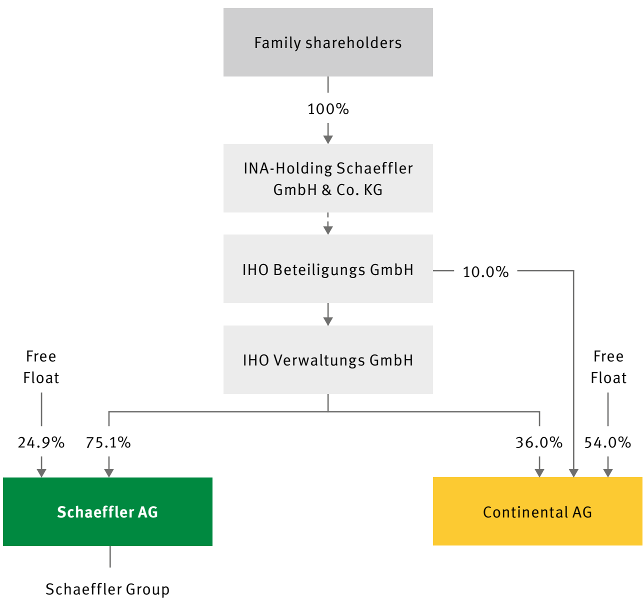
Provisions for pensions and similar obligations for former members of the Board of Managing Directors (and their surviving dependants) of Schaeffler AG and its legal predecessors, before netting of related plan assets, amounted to EUR 13 m at December 31, 2017 (prior year: EUR 11 m).

At December 31, 2017, members of the Board of Managing Directors and the Supervisory Board of Schaeffler AG and close members of their family held bonds issued by Schaeffler Finance B.V. with a principal totaling EUR 0.6 m (prior year: EUR 0.8 m). Key management personnel and close members of their family received interest of EUR 0.0 m (prior year: EUR 0.1 m) on these bonds. Additionally, bonds issued in prior years with a value of EUR 0 m (prior year: EUR 3 m) held by key management personnel and close members of their family were redeemed.

Related entities

Pursuant to IAS 24, the Schaeffler Group's related entities consist of the entities controlled or jointly controlled by Schaeffler AG's ultimate parent company, INA Holding Schaeffler GmbH & Co. KG, or over which INA Holding Schaeffler & Co. KG has significant influence.

Simplified ownership structure No. 152
as at December 31, 2017



As transactions with significant subsidiaries of Schaeffler AG have been eliminated upon consolidation, they need not be discussed here. Transactions with associated companies and joint ventures were insignificant in 2017.

In 2017 and 2016, Schaeffler Group companies had various business relationships with the group's related entities.

On April 26, 2017, the Schaeffler AG annual general meeting declared a total dividend of EUR 328 m in respect of 2016, including EUR 245 m on the common shares held by IHO Verwaltungs GmbH.

In 2016, IHO Verwaltungs GmbH prepaid its loans payable to Schaeffler AG in full. As a result, the Schaeffler Group no longer earned any interest income on loans to shareholders in 2017 (prior year: EUR 49 m).

Business relationships with Continental Group companies existed in the form of supply of vehicle components and tools, rendering of development and other services, and leases of commercial real estate. The transactions with the Continental Group were entered into at arm's-length conditions.

The following table summarizes all income and expenses from transactions with related Schaeffler Group companies recognized in the Schaeffler Group consolidated financial statements. The summary also shows receivables and payables related to such transactions included in the consolidated financial statements as at the end of each reporting period.

Receivables and payables from transactions with related entities No. 153

	12/31/2017	12/31/2016	12/31/2017	12/31/2016
in € millions		Receivables		Payables
Related entities	25	22	17	12

Expenses and income from transactions with related entities No. 154

	2017	2016	2017	2016
in € millions		Expenses		Income
Related entities	85	84	129	168

Receivables from transactions with related entities include EUR 25 m (prior year: EUR 22 m) in trade receivables.

5.7 Auditors' fees

Schaeffler AG incurred the following fees for services rendered by the global network of KPMG and KPMG AG Wirtschaftsprüfungsgesellschaft (KPMG AG):

Auditors' fees No. 155

	2017	2016	2017	2016
in € millions		KPMG		thereof KPMG AG
Financial statement audit services	6.9	6.4	4.0	3.7
Other attestation services	0.3	0.1	0.2	0.1
Tax advisory services	1.7	1.3	1.6	1.0
Other services	0.1	0.5	0.0	0.4
Total	**9.0**	**8.3**	**5.8**	**5.2**

KPMG AG is considered Schaeffler AG's auditor. The fees paid to KPMG AG related to services rendered to Schaeffler AG and its German subsidiaries.

5.8 Declaration of conformity with the German Corporate Governance Code

Schaeffler AG's Board of Managing Directors and the Supervisory Board issued the declaration of conformity with the German Corporate Governance Code pursuant to section 161 of the German Stock Corporations Act ("Aktiengesetz" –AktG) in December 2017 and have made it publicly available on the Schaeffler Group's website (www.schaeffler.com/ir).

5.9 Events after the reporting period

No material events expected to have a significant impact on the net assets, financial position, or results of operations of the Schaeffler Group occurred after December 31, 2017.

5.10 List of shareholdings required by section 313 (2) HGB

The parent company is Schaeffler AG, which is based in Herzogenaurach.

List of shareholdings No. 156

Entity	Location	Country code	Group ownership interest in %
A. Entities fully consolidated			
I. Germany (50)			
AS Auslandsholding GmbH [2]	Buehl	DE	100.00
CBF Europe GmbH	Wuppertal	DE	100.00
Compact Dynamics GmbH	Starnberg	DE	100.00
CVT Beteiligungsverwaltungs GmbH	Buehl	DE	100.00
CVT Verwaltungs GmbH & Co. Patentverwertungs KG [1,4]	Buehl	DE	100.00
Dürkopp Maschinenbau GmbH [2]	Schweinfurt	DE	100.00
Egon von Ruville GmbH [2]	Hamburg	DE	100.00
FAG Aerospace GmbH	Schweinfurt	DE	100.00
FAG Aerospace GmbH & Co. KG [1,4]	Schweinfurt	DE	100.00
FAG Industrial Services GmbH [2]	Herzogenrath	DE	100.00
FAG Kugelfischer GmbH [2]	Schweinfurt	DE	100.00
Gesellschaft für Arbeitsmedizin und Umweltschutz mbH - AMUS [2]	Homburg	DE	100.00
IAB Grundstücks-verwaltungsgesellschaft mbH	Buehl	DE	100.00
IAB Holding GmbH [2]	Herzogenaurach	DE	100.00
IAB Verwaltungs GmbH [2]	Herzogenaurach	DE	100.00
IDAM Beteiligungs GmbH	Herzogenaurach	DE	100.00
INA - Drives & Mechatronics AG & Co. KG [1,4]	Suhl	DE	100.00
INA Automotive GmbH [2]	Herzogenaurach	DE	100.00
INA Beteiligungsverwaltungs GmbH [2]	Herzogenaurach	DE	100.00
Industrieaufbaugesellschaft Bühl mbH [2]	Buehl	DE	100.00
Industriewerk Schaeffler INA-Ingenieurdienst GmbH [2]	Herzogenaurach	DE	100.00
KWK Verwaltungs GmbH	Langen	DE	100.00
LuK Auslandsholding GmbH [2]	Buehl	DE	100.00
LuK Beteiligungsgesellschaft mbH [2]	Buehl	DE	100.00
LuK GmbH & Co. KG [1,4]	Buehl	DE	100.00
LuK Management GmbH	Buehl	DE	100.00
LuK Truckparts GmbH & Co. KG [1,4]	Kaltennordheim	DE	100.00
LuK Unna GmbH & Co. KG [1,4]	Unna	DE	100.00
LuK Vermögens-verwaltungsgesellschaft mbH [2]	Buehl	DE	100.00
MEDUSA Beteiligungsverwaltungs-Gesellschaft Nr. 64 mbH	Buehl	DE	100.00
PD Qualifizierung und Beschäftigung GmbH [2]	Schweinfurt	DE	100.00
Raytech Composites Europe GmbH	Morbach	DE	100.00
Schaeffler Automotive Aftermarket GmbH & Co. KG [1,4]	Langen	DE	100.00
Schaeffler Beteiligungs-gesellschaft mbH	Herzogenaurach	DE	100.00
Schaeffler Beteiligungs-verwaltungs GmbH [2]	Herzogenaurach	DE	100.00
Schaeffler Elfershausen AG & Co. KG [1,4]	Herzogenaurach	DE	100.00
Schaeffler Engineering GmbH [2]	Werdohl	DE	100.00
Schaeffler Europa Logistik GmbH [2]	Herzogenaurach	DE	100.00
Schaeffler Friction Products GmbH	Morbach	DE	100.00
Schaeffler Friction Products Hamm GmbH	Hamm/Sieg	DE	100.00
Schaeffler Immobilien AG & Co. KG [1,4]	Herzogenaurach	DE	100.00
Schaeffler Technologies AG & Co. KG [1,4]	Herzogenaurach	DE	100.00
Schaeffler Versicherungs-Vermittlungs GmbH [2]	Herzogenaurach	DE	100.00
Schaeffler Verwaltungsholding Drei GmbH [2]	Herzogenaurach	DE	100.00
Schaeffler Verwaltungsholding Eins GmbH [2]	Herzogenaurach	DE	100.00
Schaeffler Verwaltungsholding Vier GmbH	Herzogenaurach	DE	100.00
Schaeffler Verwaltungsholding Zwei GmbH [2]	Herzogenaurach	DE	100.00
Unterstützungskasse der FAG Kugelfischer e. V.	Schweinfurt	DE	100.00
WPB Water Pump Bearing Beteiligungsgesellschaft mbH	Herzogenaurach	DE	100.00
WPB Water Pump Bearing GmbH & Co. KG [1,4]	Herzogenaurach	DE	100.00
II. Foreign (101)			
Schaeffler Middle East FZE	Jebel Ali	AE	100.00
Schaeffler Argentina S.R.L.	Buenos Aires	AR	100.00
Schaeffler Austria GmbH	Berndorf-St. Veit	AT	100.00
Schaeffler Australia Pty Ltd.	Frenchs Forest	AU	100.00
Schaeffler Belgium SPRL	Braine L'Alleud	BE	100.00
Schaeffler Bulgaria OOD	Sofia	BG	100.00
LuK do Brasil Embreagens Ltda.	Sorocaba	BR	100.00
Schaeffler Brasil Ltda.	Sorocaba	BR	100.00
Schaeffler Belrus OOO	Minsk	BY	100.00
FAG Aerospace Inc.	Stratford	CA	100.00
Schaeffler Canada Inc.	Oakville	CA	100.00
Schaeffler Schweiz GmbH	Romanshorn	CH	100.00
Schaeffler Chile Rodamientos Ltda.	Santiago	CL	100.00
Schaeffler (China) Co., Ltd.	Taicang	CN	100.00
Schaeffler (Nanjing) Co., Ltd.	Nanjing City	CN	100.00
Schaeffler (Ningxia) Co., Ltd.	Yinchuan	CN	100.00
Schaeffler (Xiangtan) Co., Ltd.	Xiangtan	CN	100.00
Schaeffler Aerospace Bearings (Taicang) Co., Ltd.	Taicang	CN	100.00
Schaeffler Friction Products (Suzhou) Co., Ltd.	Suzhou	CN	100.00
Schaeffler Holding (China) Co., Ltd.	Shanghai	CN	100.00
Schaeffler Trading (Shanghai) Co., Ltd.	Shanghai	CN	100.00
Schaeffler Colombia Ltda.	Bogotá	CO	100.00
Schaeffler CZ s.r.o.	Prague	CZ	100.00
Schaeffler Production CZ s.r.o.	Lanskroun	CZ	100.00
Schaeffler Danmark ApS	Aarhus	DK	100.00
Schaeffler Iberia, S.L.U.	Elgoibar	ES	100.00

Schaeffler Finland Oy	Espoo	FI	100.00
Schaeffler Chain Drive Systems SAS	Calais	FR	100.00
Schaeffler France SAS	Haguenau	FR	100.00
LuK (UK) Limited	Sheffield	GB	100.00
LuK Leamington Limited	Sheffield	GB	100.00
Schaeffler (UK) Limited	Sutton Coldfield	GB	100.00
Schaeffler Automotive Aftermarket (UK) Limited	Sheffield	GB	100.00
Stocklook Limited	Swansea	GB	100.00
The Barden Corporation (UK) Ltd.	Plymouth	GB	100.00
Schaeffler Greece Automotive and Industrial Products and Services M.E.P.E.	Athen	GR	100.00
Schaeffler Hong Kong Company Limited	Hong Kong	HK	100.00
Schaeffler Hrvatska d.o.o.	Zagreb	HR	100.00
FAG Magyarorszag Ipari Kft.	Debrecen	HU	100.00
LuK Savaria Kft.	Szombathely	HU	100.00
Schaeffler Magyarorszag Ipari Kft.	Budapest	HU	100.00
Schaeffler Bearings Indonesia, PT	Jakarta	ID	100.00
Schaeffler Israel Ltd.	Yokneam Illit	IL	100.00
INA Bearings India Private Limited	Pune	IN	100.00
LuK India Private Limited	Hosur	IN	100.00
Schaeffler India Ltd.	Mumbai	IN	51.33
INA Invest S.r.l.	Momo	IT	100.00
Schaeffler Italia S.r.l.	Momo	IT	100.00
Schaeffler Railway Products G.e.i.e.	Milan	IT	75.00
Schaeffler Water Pump Bearing Italia S.r.l.	Momo	IT	100.00
Schaeffler Japan Co., Ltd.	Yokohama	JP	100.00
Schaeffler Ansan Corporation	Ansan-shi	KR	100.00
Schaeffler Korea Corporation	Changwon-si	KR	100.00
SIA "Schaeffler Baltic"	Riga	LV	100.00
LuK Puebla, S. de R.L. de C.V.	Puebla	MX	100.00
Rodamientos FAG S.A. de C.V.	Mexico City	MX	100.00
Schaeffler Automotive Aftermarket Mexico, S. de R.L. de C.V.	Puebla	MX	100.00
Schaeffler Mexico Holding, S. de R.L. de C.V.	Irapuato	MX	100.00
Schaeffler Mexico Servicios, S. de R.L. de C.V.	Guanajuato	MX	100.00
Schaeffler Mexico, S. de R.L. de C.V.	Guanajuato	MX	100.00
Schaeffler Bearings (Malaysia) Sdn. Bhd.	Kuala Lumpur	MY	100.00
Radine B.V.	Barneveld	NL	100.00
Schaeffler Finance B.V.	Barneveld	NL	100.00
Schaeffler Nederland B.V.	Barneveld	NL	100.00
Schaeffler Nederland Holding B.V.	Barneveld	NL	100.00
LuK Norge AS	Kongsberg	NO	100.00
Schaeffler Norge AS	Oslo	NO	100.00
Schaeffler Peru S.A.C.	Lima	PE	100.00
Schaeffler Philippines Inc.	Makati City	PH	100.00
Schaeffler Polska Sp. z.o.o.	Warsaw	PL	100.00
Schaeffler Portugal Unipessoal, Lda.	Caldas da Rainha	PT	100.00
Schaeffler Romania S.R.L.	Brasov	RO	100.00
Schaeffler Manufacturing Rus OOO	Ulyanovsk	RU	100.00
Schaeffler Russland GmbH	Moscow	RU	100.00
Schaeffler Sverige AB	Arlandastad	SE	100.00
FAG Aerospace (Singapore) Pte. Ltd.	Singapore	SG	100.00
Schaeffler (Singapore) Pte. Ltd.	Singapore	SG	100.00
Schaeffler Slovenija d.o.o.	Maribor	SI	100.00
Schaeffler Kysuce, spol. s r.o.	Kysucke Nove Mesto	SK	100.00
Schaeffler Skalica spol. s r.o.	Skalica	SK	100.00
Schaeffler Slovensko spol s.r.o.	Kysucke Nove Mesto	SK	100.00
Schaeffler (Thailand) Co., Ltd.	Bangkok	TH	100.00
Schaeffler Holding (Thailand) Co., Ltd.	Bangkok	TH	100.00
Schaeffler Manufacturing (Thailand) Co., Ltd.	Rayong	TH	100.00
Schaeffler Turkey Endüstri ve Otomotiv Ticaret Limited Sirketi	Istanbul	TR	100.00
Schaeffler Taiwan Co., Ltd.	Taipei	TW	100.00
Schaeffler Ukraine GmbH	Kiev	UA	100.00
FAG Bearings LLC	Danbury	US	100.00
FAG Holding LLC	Danbury	US	100.00
FAG Interamericana A.G.	Miami	US	100.00
LMC Bridgeport, Inc.	Danbury	US	100.00
LuK Clutch Systems, LLC	Wooster	US	100.00
LuK Transmission Systems LLC	Wooster	US	100.00
LuK USA LLC	Wooster	US	100.00
LuK-Aftermarket Services, LLC	Valley City	US	100.00
Schaeffler Group USA, Inc.	Fort Mill	US	100.00
The Barden Corporation	Danbury	US	100.00
Schaeffler Venezuela, C.A.	Caracas	VE	100.00
Schaeffler Vietnam Co., Ltd.	Bien Hoa City	VN	100.00
INA Bearing (Pty) Ltd.	Port Elizabeth	ZA	100.00
Schaeffler South Africa (Pty.) Ltd.	Johannesburg	ZA	100.00

B. Associated companies/Joint ventures I. Germany (3)			
Contitech-INA Beteiligungsgesellschaft mbH	Hanover	DE	50.00
Contitech-INA GmbH & Co. KG [4]	Hanover	DE	50.00
PStec Automation and Service GmbH	Niederwerrn	DE	40.00
II. Foreign (2)			
Eurings Zrt.	Debrecen	HU	37.00
Colinx, LLC	Greenville	US	20.00
C. Unconsolidated entities I. Germany (4)			
autinity systems GmbH [3) 5) 6)]	Chemnitz	DE	33.34
afr-consulting GmbH [3) 5)]	Chemnitz	DE	100.00
Schaeffler Consulting GmbH [3)]	Herzogenaurach	DE	100.00
Schaeffler Bio-Hybrid GmbH [3)]	Herzogenaurach	DE	100.00
II. Foreign (1)			
Schaeffler SR d.o.o. [3)]	Belgrade	RS	100.00

1) Exemption under section 264b HGB.
2) Exemption under section 264 (3) HGB.
3) The company is insignificant to the results of operations, financial position, and net assets of the Schaeffler Group as at the reporting date.
4) Schaeffler AG or another consolidated entity is the general partner.
5) The company was acquired on October 04, 2017.
6) The company holds 66.66% as treasury shares.

5.11 Members of the Supervisory Board and of the Board of Managing Directors

Members of the Supervisory Board

Georg F. W. Schaeffler (Chairman), Maria-Elisabeth Schaeffler-Thumann (Deputy Chairperson), Jürgen Wechsler* (Deputy Chairman), Prof. Dr. Hans-Jörg Bullinger, Dr. Holger Engelmann, Prof. Dr. Bernd Gottschalk, Andrea Grimm* (since April 08, 2017), Norbert Lenhard*, Dr. Siegfried Luther, Dr. Reinold Mittag*, Barbara Resch*, Stefanie Schmidt*, Dirk Spindler*, Robin Stalker, Jürgen Stolz*, Salvatore Vicari*, Dr. Otto Wiesheu, Prof. KR Ing. Siegfried Wolf, Jürgen Worrich*, Prof. Dr.-Ing. Tong Zhang

The following member left the Supervisory Board in 2017

Yvonne Münch* (until March 07, 2017)

Supervisory Board committees

Mediation committee

Georg F. W. Schaeffler (Chairman), Norbert Lenhard, Maria-Elisabeth Schaeffler-Thumann, and Jürgen Wechsler

Executive committee

Georg F. W. Schaeffler (Chairman), Norbert Lenhard, Barbara Resch, Maria-Elisabeth Schaeffler-Thumann, Jürgen Wechsler, and Prof. KR Ing. Siegfried Wolf

Audit committee

Dr. Siegfried Luther (Chairman), Dr. Reinold Mittag, Georg F. W. Schaeffler, Robin Stalker, Salvatore Vicari, and Jürgen Worrich

Nomination committee

Georg F. W. Schaeffler (Chairman), Dr. Holger Engelmann, Prof. Dr. Bernd Gottschalk, and Maria-Elisabeth Schaeffler-Thumann

Members of the Board of Managing Directors

Klaus Rosenfeld (Chief Executive Officer), Prof. Dr.-Ing. Peter Gutzmer (Deputy CEO and Chief Technology Officer), Dietmar Heinrich (Chief Financial Officer; since August 01, 2017), Oliver Jung (Chief Operating Officer), Prof. Dr. Peter Pleus (CEO Automotive OEM), Corinna Schittenhelm (Chief Human Resources Officer), Michael Söding (CEO Automotive Aftermarket; since January 01, 2018), Dr. Stefan Spindler (CEO Industrial), Matthias Zink (CEO Automotive OEM)

The following member left the Board of Managing Directors in 2017

Dr. Ulrich Hauck (Chief Financial Officer; until July 31, 2017)

* Employee representative.

5.12 Preparation of consolidated financial statements

The Board of Managing Directors of Schaeffler AG prepared the consolidated financial statements on February 19, 2018, and released them for submission to the Supervisory Board of Schaeffler AG. The Supervisory Board of Schaeffler AG is responsible for examining and approving the consolidated financial statements.

Herzogenaurach, February 19, 2018

Schaeffler Aktiengesellschaft
The Board of Managing Directors

Klaus Rosenfeld
Chief Executive Officer

Prof. Dr.-Ing. Peter Gutzmer

Dietmar Heinrich

Oliver Jung

Prof. Dr. Peter Pleus

Corinna Schittenhelm

Michael Söding

Dr. Stefan Spindler

Matthias Zink

Independent Auditors' Report

To Schaeffler AG; Herzogenaurach

Report on the Audit of the Consolidated Financial Statements and of the Group Management Report

Opinions

We have audited the consolidated financial statements of Schaeffler AG and its subsidiaries (the Group), which comprise the consolidated statement of financial position as at December 31, 2017 and the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the financial year from January 31, 2017 to December 31, 2017, and notes to the consolidated financial statements, including a summary of significant accounting policies. In addition, we have audited the group management report of Schaeffler AG for the financial year from January 31, 2017 to December 31, 2017. In accordance with the German legal requirements we have not audited the content of the corporate governance statement which are included in the Corporate Governance section of the group management report.

In our opinion, on the basis of the knowledge obtained in the audit,

- the accompanying consolidated financial statements comply, in all material respects, with the IFRSs as adopted by the EU, and the additional requirements of German commercial law pursuant to Section 315e (1) HGB [Handelsgesetzbuch: German Commercial Code] and, in compliance with these requirements, give a true and fair view of the assets, liabilities, and financial position of the Group as at December 31, 2017 and of its financial performance for the financial year from January 1, 2017 to December 31, 2017, and
- the accompanying group management report as a whole provides an appropriate view of the Group's position. In all material respects, this group management report is consistent with the consolidated financial statements, complies with German legal requirements and appropriately presents the opportunities and risks of future development. Our opinion on the group management report does not cover the content of the non-financial statement and the corporate governance statement mentioned above.

Pursuant to Section 322 (3) sentence 1 HGB, we declare that our audit has not led to any reservations relating to the legal compliance of the consolidated financial statements and of the group management report.

Basis for the Opinions

We conducted our audit of the consolidated financial statements and of the group management report in accordance with Section 317 HGB and the EU Audit Regulation No. 537/2014 (referred to subsequently as "EU Audit Regulation") and in compliance with German Generally Accepted Standards for Financial Statement Audits promulgated by the Institut der Wirtschaftsprüfer [Institute of Public Auditors in Germany] (IDW). Our responsibilities under those requirements and principles are further described in the "Auditors' Responsibilities for the Audit of the Consolidated Financial Statements and of the Group Management Report" section of our auditors' report. We are independent of the group entities in accordance with the requirements of European law and German commercial and professional law, and we have fulfilled our other German professional responsibilities in accordance with these requirements. In addition, in accordance with Article 10 (2) point (f) of the EU Audit Regulation, we declare that we have not provided non-audit services prohibited under Article 5 (1) of the EU Audit Regulation. We believe that the evidence we have obtained is sufficient and appropriate to provide a basis for our opinions on the consolidated financial statements and on the group management report.

Key Audit Matters in the Audit of the Consolidated Financial Statements

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated financial statements for the financial year from January 31, 2017 to December 31, 2017. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, we do not provide a separate opinion on these matters.

Recognition and Measurement of Restructuring Provisions

For the Company's accounting and valuation methods used, please refer to Note 1.3. The valuation principles are described in Note 4.12.

The risk to the financial statements Schaeffler AG recognized restructuring provisions of EUR 46 million in its consolidated financial statements as of December 31, 2017.

Restructuring provisions must be recorded if certain criteria for recognition are met under IFRS. The recognition criteria and valuation are largely based on assessments and assumptions from legal representatives. Therefore there exists a risk to the financial statements that the criteria for the recognition of restructuring provisions have not been met or that they are assessed incorrectly.

Our audit approach Our audit procedures included an assessment of whether the criteria for recognition of the restructuring provisions were met as of December 31, 2017. In this respect, we reviewed the restructuring plan of the Executive Board, Group Accounting and the Head of Financial Strategy, Processes and Infrastructure, and also reviewed relevant Executive Board Meetings minutes. In addition, we reviewed corporate communications and the minutes of discussions with the employee representatives, as well as the minutes of each Supervisory Board meeting.

Subsequently, we inquired of the Management Board and Corporate Accounting as to the assumptions underlying the valuation of the restructuring provisions. In doing so, we assessed the restructuring plan in terms of locations, functions, number of employees, as well as expenditures and timing of implementation, and recalculated the provisions based on the documentation provided using the estimates derived from personnel data.

Our conclusions The criteria for recognition of restructuring provisions were met. The assumptions used by management in the valuation of the restructuring provisions are appropriate.

First-time Presentation of Sale of Receivables

For the Company's accounting and valuation methods used, please refer to Note 1.3. The valuation principles are described in Note 4.5.

The risk to the financial statements Schaeffler AG introduced an asset-backed commercial paper program during 2017. As of December 31, 2017, they have sold and partially de-recognized trade receivables with a nominal value of EUR 150 million. In our opinion, this issue is of particular importance since the relevant IFRS regulations are complex and discretionary. Risks to the financial statements relate to the assessment of the de-recognition criteria, as well as the underlying assumptions. There is also the risk that the related disclosures in the notes of the consolidated financial statements are inadequate.

Our audit approach In order to ensure an accurate presentation of the asset-backed commercial paper program, we first assessed the structure of the program itself and then assessed the de-recognition criteria and the underlying assumptions. We involved KPMG financial and treasury management specialists to assist the audit team in these assessments. Finally, we evaluated whether the presentation and related disclosures in the notes are appropriate.

Our conclusions We found the de-recognition criteria and the assumptions used by management to be appropriate. The disclosures related to the asset-backed commercial paper program are also appropriate.

Completeness and Valuation of Provisions for Compliance Investigations

For the Company's accounting and valuation methods used, please refer to Note 1.3. The valuation principles are described in Note 4.12.

The risk to the financial statements As of December 31, 2017, Schaeffler AG recorded provisions of EUR 55 million for potential claims in connection with ongoing investigations into antitrust violations and compliance cases.

A provision for compliance violations should be recognized when the entity has a present obligation as a result of a past event, for which it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and for which a reliable estimate can be made. The amount of the provision to be recognized is determined by using the best estimate. The recognition and valuation of the compliance provisions is therefore based on discretionary assessments of the Executive Board.

There exists a risk for the consolidated financial statements that the provisions are not complete.

Our audit approach In order to assess the appropriateness of the provisions, we obtained explanations for the estimates from the entity's external legal counsel, management, and in-house legal counsel. In particular, we performed the following:

- Assessed the likelihood of the claim by inspecting underlying documents; inquired of legal representatives, corporate accounting, corporate compliance, and in-house legal counsel; as well as obtained legal confirmations from Schaeffler AG's external counsel.
- Examined correspondence from relevant authorities, as well as evaluated underlying documents and protocols; and
- Assessed the reasonableness of the critical assumptions and the methodology of the calculation.

Our conclusions The assessments and assumptions made by management are sufficiently documented and substantiated. The assumptions made by management are appropriate.

Other Information

Management is responsible for the other information. The other information comprises:

- the non-financial statement and the corporate governance statement, and
- the remaining parts of the annual report, with the exception of the audited consolidated financial statements and group management report and our auditors' report.

Our opinions on the consolidated financial statements and on the group management report do not cover the other information, and consequently we do not express an opinion or any other form of assurance conclusion thereon.

In connection with our audit, our responsibility is to read the other information and, in so doing, to consider whether the other information

- is materially inconsistent with the consolidated financial statements, with the group management report or our knowledge obtained in the audit, or
- otherwise appears to be materially misstated.

Responsibilities of Management and the Supervisory Board for the Consolidated Financial Statements and the Group Management Report

Management is responsible for the preparation of the consolidated financial statements that comply, in all material respects, with IFRSs as adopted by the EU and the additional requirements of German commercial law pursuant to Section 315e (1) HGB and that the consolidated financial statements, in compliance with these requirements, give a true and fair view of the assets, liabilities, financial position, and financial performance of the Group. In addition, management is responsible for such internal control as they have determined necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, management is responsible for assessing the Group's ability to continue as a going concern. They also have the responsibility for disclosing, as applicable, matters related to going concern. In addition, they are responsible for financial reporting based on the going concern basis of accounting unless there is an intention to liquidate the Group or to cease operations, or there is no realistic alternative but to do so.

Furthermore, management is responsible for the preparation of the group management report that, as a whole, provides an appropriate view of the Group's position and is, in all material respects, consistent with the consolidated financial statements, complies with German legal requirements, and appropriately presents the opportunities and risks of future development. In addition, management is responsible for such arrangements and measures (systems) as they have considered necessary to enable the preparation of a group management report that is in accordance with the applicable German legal requirements, and to be able to provide sufficient appropriate evidence for the assertions in the group management report.

The supervisory board is responsible for overseeing the Group's financial reporting process for the preparation of the consolidated financial statements and of the group management report.

Auditors' Responsibilities for the Audit of the Consolidated Financial Statements and of the Group Management Report

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and whether the group management report as a whole provides an appropriate view of the Group's position and, in all material respects, is consistent with the consolidated financial statements and the knowledge obtained in the audit, complies with the German legal requirements and appropriately presents the opportunities and risks of future development, as well as to issue an auditors' report that includes our opinions on the consolidated financial statements and on the group management report.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Section 317 HGB and the EU Audit Regulation and in compliance with German Generally Accepted Standards for Financial Statement Audits promulgated by the Institut der Wirtschaftsprüfer (IDW) will always detect a material misstatement. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements and this group management report.

We exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements and of the group management report, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinions. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit of the consolidated financial statements and of arrangements and measures (systems) relevant to the audit of the group management report in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of these systems.
- Evaluate the appropriateness of accounting policies used by management and the reasonableness of estimates made by management and related disclosures.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in the auditors' report to the related disclosures in the consolidated financial statements and in the group management report or, if such disclosures are inadequate, to modify our respective opinions. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Group to cease to be able to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements present the underlying transactions and events in a manner that the consolidated financial statements give a true and fair view of the assets, liabilities, financial position and financial performance of the Group in compliance with IFRSs as adopted by the EU and the additional requirements of German commercial law pursuant to Section 315e (1) HGB.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express opinions on the consolidated financial statements and on the group management report. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our opinions.
- Evaluate the consistency of the group management report with the consolidated financial statements, its conformity with German law, and the view of the Group's position it provides.
- Perform audit procedures on the prospective information presented by management in the group management report. On the basis of sufficient appropriate audit evidence we evaluate, in particular, the significant assumptions used by management as a basis for the prospective information, and evaluate the proper derivation of the prospective information from these assumptions. We do not express a separate opinion on the prospective information and on the assumptions used as a basis. There is a substantial unavoidable risk that future events will differ materially from the prospective information.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with the relevant independence requirements, and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, the related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditors' report unless law or regulation precludes public disclosure about the matter.

Other Legal and Regulatory Requirements

Further Information pursuant to Article 10 of the EU Audit Regulation

We were elected as group auditor by the annual general meeting on April 26, 2017. We were engaged by the supervisory board on June 22, 2017. We have been the group auditor of Schaeffler AG without interruption since the financial year 2015.

We declare that the opinions expressed in this auditors' report are consistent with the additional report to the audit committee pursuant to Article 11 of the EU Audit Regulation (long-form audit report).

In addition to the financial statement audit, we have provided to group entities the following services that are not disclosed in the consolidated financial statements or in the group management report:

In addition to the consolidated financial statements, we audited the annual financial statements of Schaeffler AG and conducted various annual financial statements audits at subsidiaries. We performed a review of interim financial statements, as well as audited parts of the internal control system (ICS). In addition, we audited the combined separate non-financial consolidated information of the Management Report of Schaeffler AG as well as performed statutory or contractual audits; for example: audits in accordance with the EEG, EMIR audits in accordance with section 20 WpHG and confirmations of compliance with contractual conditions. We also provided tax advice to certain employees of Schaeffler AG in connection with their relocation to foreign subsidiaries of Schaeffler AG.

German Public Auditor Responsible for the Engagement

The German Public Auditor responsible for the engagement is Angelika Alt-Scherer

Munich, February 20, 2018

KPMG AG
Wirtschaftsprüfungsgesellschaft

gez. Alt-Scherer Wirtschaftsprüferin	gez. Koeplin Wirtschaftsprüfer

Responsibility statement by the company's legal representatives

To the best of our knowledge, and in accordance with the applicable reporting principles, the consolidated financial statements provide a true and fair view of the assets, liabilities, financial position, and profit or loss of the group, and the group management report includes a fair review of the development and performance of the business and the position of the group, together with a description of the principal opportunities and risks associated with the expected development of the group.

Herzogenaurach, February 19, 2018

Schaeffler Aktiengesellschaft
The Board of Managing Directors

Klaus Rosenfeld
Chief Executive Officer

Prof. Dr.-Ing. Peter Gutzmer

Dietmar Heinrich

Oliver Jung

Prof. Dr. Peter Pleus

Corinna Schittenhelm

Michael Söding

Dr. Stefan Spindler

Matthias Zink

Additional information

Glossary

A

Additive manufacturing: Process by which digital 3D design data is used to build up a component in layers by depositing material, for instance in the form of fine powder.

AfS: Abbreviation of "Available for sale".

Agenda 4 plus One: Excellence program of the Schaeffler Group to help execute the strategy "Mobility for tomorrow". It includes the five categories Customer focus, Operational excellence, Financial flexibility, Leadership and talent management, as well as Securing long-term competitiveness and value creation. 20 strategic initiatives that have significance worldwide and have been selected from a variety of initiatives are in turn assigned to these categories.

AKO: Abbreviation of "Aftermarket Kitting Operation": project to establish a state-of-the-art assembly and packaging center.

Automotive Aftermarket: New division established effective January 01, 2018. With its Automotive Aftermarket division, the Schaeffler Group is represented worldwide in the spare parts business, offering both products and services.

Automotive OEM: As a reliable partner to nearly all automobile manufacturers, the Schaeffler Group's Automotive OEM division offers important supplier expertise for the entire drive train (engines, transmissions, chassis, and accessory units). The division's product range includes components and systems for vehicles with drive trains based on internal combustion engines as well as for hybrid and electric vehicle applications.

Average capital employed: Calculated as the sum of property, plant and equipment, intangible assets, and working capital, which in turn comprises trade receivables and inventories net of trade payables. The annual average is determined as the mathematical average of the balance at the end of each of the four quarters.

B

Bearing & Components Technologies (BCT): Functionally coordinated department of the Schaeffler Group that acts as an internal supplier.

Bio-Hybrid: The Bio-Hybrid is an advanced e-bike offering protection from the weather as well as storage space and is aimed at dealing with the growing volume of traffic in urban centers.

C

Capex: Capital expenditures on property, plant and equipment and intangible assets.

Capex ratio: Capital expenditures on property, plant and equipment and intangible assets as a percentage of revenue.

Capital employed: Working capital plus property, plant and equipment and intangible assets.

Cash flow: Net inflow of funds generated by an entity's business activities. Cash flow is a measure of an entity's ability to generate financing internally.

CEEMEA: Abbreviation of "Central and Eastern Europe & Middle East and Africa".

Charta der Vielfalt: "Diversity charter"; corporate initiative to promote diversity within companies and institutions. Organizations are encouraged to create a working environment free of prejudice. All employees deserve respect, irrespective of gender, nationality, ethnic background, religion or worldview, disability, age, and sexual preference and identity.

Cloud: Digital platform that can be used to store and transfer data.

Code of Conduct: A set of rules adopted or accepted by companies, in this case the Schaeffler Group, that defines rules for the employees and typically contains ordinances and prohibitions.

Common non-voting share: Non-voting no-par-value bearer shares carrying a preferential right to profits in the form of a preferred dividend.

Common share: Share conveying all rights laid down in the German Stock Corporations Act, for instance the right to vote at shareholder meetings, the right to dividends, etc.

Compliance: Ensuring that all rules and regulations applicable to a process are adhered to.

Compliance Fit & Proper: Schaeffler Group initiative to implement certain compliance requirements and measures.

CORE: The Schaeffler Group's program designed to realign the operations of the Industrial division in order to return the division to lasting growth and increased profitability.

Corporate Governance: Set of legal and constructive requirements for the management and supervision of companies.

COSO model: An internal control model to help document, evaluate, and design internal control systems.

Cost of capital: Calculated by multiplying average capital employed with the cost of capital percentage.

Cost of capital percentage: The cost of capital percentage is derived from the return investors require for providing capital to the entity.

D

DAX: Abbreviation of "Deutscher Aktienindex" ("German Share Index"): Leading share index of Deutsche Börse.

Declaration of conformity: Declaration by the Board of Managing Directors and the Supervisory Board in accordance with section 161 AktG regarding whether the company has complied and/or is complying with the German Corporate Governance Code and which recommendations were and/or are not applied and the reasons therefore.

Deferred taxes: Deferred tax assets and liabilities are calculated based on temporary differences between carrying amounts for financial reporting and for tax purposes. They include differences arising on consolidation, loss carryforwards, and tax credits.

Degree of localization: Relation of a region's total sales to sales volume manufactured in that region.

Derivative financial instruments: Financial products whose value is predominantly driven by the price, price changes, and expected prices of the underlying instrument.

Digital Agenda: Initiative under the excellence program "Agenda 4 plus One" for coordinating, establishing, and expanding the Schaeffler Group's digital activities. Starting with the customer, it reflects four central digital business scenarios (Products & services, Machines & processes, Analyses & simulation, User experience & customer value) the Schaeffler Group is focusing on.

Directors' dealings: Transactions in the Schaeffler Group's securities by members of Schaeffler AG's Board of Managing Directors or its Supervisory Board or persons related to them.

Diversity: Diversity with respect to aspects including gender, ethnic origin, age, disability, sexual orientation, religion, life style.

Dividend payout ratio: Percentage of the Schaeffler Group's net income before special items that is paid out to shareholders in dividends.

DJIA: Abbreviation of "Dow Jones Industrial Average": Leading share index of the U.S. stock exchange.

E

Earnings per share: Earnings per share are calculated by dividing net income attributable to Schaeffler AG's shareholders by the weighted average number of common and common non-voting shares outstanding during the reporting period.

EBIT: Abbreviation of "earnings before interest and taxes": earnings before financial result and income taxes.

EBIT before special items: Earnings before financial result, income taxes, and special items.

EBITDA: Abbreviation of "earnings before interest, taxes, depreciation and amortization": earnings before financial result, income taxes, depreciation, amortization, and impairment losses.

EBITDA before special items: Earnings before financial result, income taxes, depreciation, amortization, and impairment losses before special items.

EBIT margin: EBIT as a percentage of revenue.

EDC: Abbreviation of "European Distribution Center": represents a significant element of the strategic alignment of the Schaeffler Group's logistics activities.

Effectiveness: The effectiveness of a hedging instrument is the degree to which changes in the fair value or the cash flows that are attributable to a hedged risk are offset by the hedging instrument.

Effective tax rate: Income tax expense as a percentage of earnings before income taxes.

Electric axle: With the electric axle, Schaeffler has developed a modular kit solution for hybrid and all-electric vehicles. The fully electric drive system features a modular design for flexible use, either as coaxial or parallel-axis versions on the front and rear ends, and can be complemented by functions such as torque vectoring or a parking lock as needed.

Electric camshaft phasing unit: The electromechanical camshaft phasing unit adjusts the camshaft to the relevant operating conditions of the engine even faster and more precisely. Using electromechanical technology, the camshaft can be adjusted at a crankshaft angular velocity of up to 600 degrees per second. The significantly increased range of adjustment allows for modern, highly-efficient combustion processes.

EMAS: Abbreviation of "Eco-Management and Audit Scheme": community eco-management and audit scheme setting out requirements under which Schaeffler Group locations are validated.

E-Mobility: Abbreviation of "electric mobility": mobility that is powered by electricity. This includes electric and hybrid vehicles. Ranging from high-voltage hybrid modules and electric axles through to wheel hub motors – the Schaeffler Group offers a broad range of products for the age of electrified powertrain architectures.

EnEHS: Abbreviation for "energy, environment, health and safety".

Equity ratio: Shareholders' equity including non-controlling interests as a percentage of total capital.

ESMA: Abbreviation of "European Securities and Markets Authority".

Euribor: Abbreviation for "Euro Interbank Offered Rate": interest rate that European banks charge each other on unsecured loans denominated in euro.

EURO MTF: Abbreviation of "Multilateral Trading Facility": trading platform similar to a stock exchange that brings together sell and buy orders for shares and other financial instruments according to a defined set of rules resulting in trades.

Euro STOXX 50: Reflects the share trends of the 50 largest companies in the euro currency area.

eWheelDrive: Schaeffler's electric wheel hub motor "eWheelDrive" offers innovative technology for mobility of tomorrow. This highly-integrated drive facilitates completely new vehicle designs. Advantages in terms of space utilization, maneuverability, driving dynamics, and active safety predestine it as a future technology for automated driving.

F

Factory for Tomorrow: Factory for Tomorrow is a response to the current megatrends and the prototype for the Schaeffler Group's factory of the future. For instance, the concept is being implemented at the new plant under construction in Xiangtan, China, for the first time.

Fair value: The amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction.

Financial covenant: Agreement included in the terms of loan or bond agreements or in the form of side-agreements requiring the debtor to adhere to certain limits defined in terms of financial indicators.

FLAC: Abbreviation of "Financial liability at amortized cost".

Free cash flow: Sum of cash flows from operating activities and cash flows from investing activities.

Fully variable valve control system UniAir: First electro-hydraulic system allowing for the fully variable control of the intake valves in fuel-powered engines. This reduces fuel consumption while at the same time increasing performance and improving torque.

G

Gearing ratio: Ratio of net financial debt to shareholders' equity including non-controlling interests.

German Corporate Governance Code: Presents essential statutory regulations for the management and supervision of German listed companies and contains, in the form of recommendations and suggestions, internationally and nationally acknowledged standards of good and responsible corporate governance.

Goodwill: Amount by which the cost of a business combination exceeds the sum of the fair values of the individually identifiable assets and liabilities acquired.

GRI G4: Abbreviation of "Fourth Generation Global Reporting Initiative": initiative that formulates guidelines for preparing corporate sustainability reports.

Gross margin: Gross profit as a percentage of revenue.

Group Compliance and Risk Committee (GCRC): The Schaeffler Group's centralized committee responsible for coordinating the flow of information about risks throughout the organization.

H

Hedge accounting: Using financial instruments to hedge items recognized in the statement of financial position and future cash flows. Both effectiveness and documentation of the hedging relationship are prerequisites for reflecting hedging relationships in the financial statements.

HfT: Abbreviation of "Held for trading".

I

IAS: Abbreviation of "International Accounting Standards".

IASB: Abbreviation of "International Accounting Standards Board".

IATF 16949:2016: Standard for quality management in the automotive sector.

IFRIC: Abbreviation of "International Financial Reporting Interpretation Committee".

IFRS: Abbreviation of "International Financial Reporting Standards".

IHO Holding: A group of holding companies held indirectly by the Schaeffler family.

IHS: Abbreviation of "Information Handling Services": research institution based in London, England.

Impact of currency translation: Revenue figures are adjusted for currency fluctuations by translating revenue for both the current and the prior year reporting period using the same exchange rate.

Industrial: Division of the Schaeffler Group that includes the business with customers in the mobility, production machinery, energy and raw materials, and aerospace sectors.

Industry 4.0: Refers to the integration of industrial production with state-of-the-art information and communications technology.

Invention reports: Invention reports represent the starting point for potential patent registrations. Ideas and inventions of Schaeffler Group employees are reported to the Schaeffler Group's centralized patent department and analyzed for potential use in a patent registration.

iTraxx CrossOver: Indicator of credit risk and the cost of credit in the European high yield market.

iTraxx Europe: Indicator of risk in the European investment-grade market.

L

LaR: Abbreviation of "Loans and receivables".

M

M&A: Abbreviation of "Mergers & Acquisitions": mergers of companies and acquisitions/disposals of companies or interests in companies.

MDAX: Abbreviation of "Mid-Cap-DAX": comprises the shares of the 50 German companies directly below the 30 DAX companies in terms of trading volume and market capitalization.

Mild hybrid (48 Volt): See "System 48 Volt".

Mobility for tomorrow: The Schaeffler Group's strategy, consisting of 4 key elements: vision and mission, 8 strategic pillars, the excellence program "Agenda 4 plus One" comprising 20 strategic initiatives, and the Schaeffler Group's Financial Ambitions 2020.

N

Net debt to EBITDA ratio: Ratio of net financial debt to EBITDA.

Net financial debt: Total of current and non-current financial debt net of cash and cash equivalents.

Nikkei 225: Leading share index of the Japanese stock exchange.

Non-controlling interest: Interest in the company's shareholders' equity held by third parties that does not give the holder control.

O

OCI: Abbreviation of "other comprehensive income": total income recognized directly in shareholders' equity less total expenses recognized directly in shareholders' equity.

OEM: Abbreviation of "original equipment manufacturer": manufacturer of a branded product.

OES: Abbreviation of "original equipment supplier": supplier manufacturing spare parts for distribution by the automobile manufacturer under its own brand.

Overrunning alternator pulley: The overrunning alternator pulley is mounted directly on the drive shaft of the generator. It transmits the drive force only in one rotational direction of the generator, ensuring a quiet and smooth belt drive.

P

Plug-in hybrid: Motor vehicle with a hybrid drive whose battery can be charged by the internal combustion engine as well as by connecting to the power grid.

Production volume: Production output delivered to a finished goods or work-in-process warehouse, valued at group production cost.

R

R&D ratio: Research and development expenses as a percentage of revenue.

Rating: Assessment of a company's creditworthiness by rating agencies.

Responsibility for tomorrow 2030+: The Schaeffler Group's sustainability strategy. Is based on the Schaeffler Group's mission and vision and supports the objective of adding long-term shareholder value. Understanding the internal and external interests and expectations vis-à-vis the company and taking them into account in order to add long-term value is essential to this.

Revolving credit facility (RCF): Contractually agreed credit facility that can be utilized repeatedly.

ROCE: Abbreviation of "return on capital employed": ratio of EBIT to average capital employed.

S

Schaeffler Academy: Schaeffler Academy combines all personnel development activities at Schaeffler worldwide. It supports strategic corporate objectives, promotes a culture of lifelong learning and enables employees to achieve their personal and professional goals.

Scope of consolidation: Total of all companies included in the consolidated financial statements.

SHARE: Abbreviation of "Schaeffler Hub for Advanced Research": research collaborations of the Schaeffler Group with research and teaching institutions.

SHARE at FAU: Research collaboration of the Schaeffler Group with Friedrich-Alexander-University of Erlangen-Nuremberg.

SHARE at KIT: Research collaboration of the Schaeffler Group with the Karlsruhe Institute of Technology.

SHARE at NTU: Research collaboration of the Schaeffler Group with Nanyang Technological University in Singapore.

SHARE at SWJTU: Research collaboration of the Schaeffler Group with Southwest Jiaotong University in Chengdu, China.

SIC: Abbreviation of the former "Standing Interpretations Committee".

Smart EcoSystem: With its Smart EcoSystem, the Schaeffler Group is setting up a digital infrastructure for new business models based on digital services that increases availability, reliability, and process quality of machines and plants.

Special items: Special items are items whose nature, frequency, and/or size may render the financial indicators less meaningful for evaluating the sustainability of the Schaeffler Group's profitability.

STOXX Europe 600: Reflects the share trends of the 600 largest listed companies from 18 European countries.

STOXX Europe 600 Automobiles & Parts: Reflects the share price trends of the European automobile manufacturers and automotive supplier sector contained in the cross-sector STOXX Europe 600 index.

Sustainability: Sustainability means utilizing natural resources while taking economic, ecological, and social conditions into account without ignoring the interests of future generations.

SVA: Abbreviation of "Schaeffler Value Added": represents EBIT less the cost of capital.

System 48 Volt: Schaeffler's 48 Volt hybrid module (mild hybrid) facilitates the introduction of hybridization and offers attractive potential for reducing CO_2. The disc-shaped, compact hybrid module for electrifying vehicles with manual transmissions is mounted as one unit between the engine and the transmission. The module requires neither changes to the transmission nor a water cooling system. Power can be recuperated by braking.

T

Thermal management module: Temperature control unit for the entire drive train. It is integrated in a compact component manufactured from high-strength plastic and combines numerous functions. The thermal management module enables Schaeffler to help unlock greater potential through the optimization of internal combustion engines.

Three lines of defense model: Model assigning clear responsibility for dealing with risks to the company's continued existence or development and based on the principle that primary responsibility for a risk lies with its originator.

Torque converter: Hydraulic component that facilitates the transmission of force between components rotating at different speeds.

W

Working capital: Inventories plus trade receivables less trade payables.

Z

ZOLLHOF Tech-Incubator Nuremberg: Digital business incubator located in Nuremberg. The incubator provides office space, consulting, and coaching and helps establish contacts with scientists and companies. Dual-mass flywheel: Component of the drive train of modern vehicles (passenger cars, buses, commercial vehicles) that helps reduce torsional vibration.

List of figures

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Forward-looking statements
This document contains forward-looking statements that reflect management's current views with respect to future events. Such statements are subject to risks and uncertainties that are beyond Schaeffler AG's ability to control or estimate precisely, such as future market and economic conditions, the behavior of other market participants, the ability to successfully integrate acquired businesses and achieve anticipated synergies, and the actions of government regulators. If any of these or other risks and uncertainties occur, or if the assumptions underlying any of these statements prove incorrect, then actual results may be materially different from those expressed or implied by such statements. Schaeffler AG does not intend or assume any obligation to update any forward-looking statements to reflect events or circumstances after the date of this report.

Variances for technical reasons
For technical reasons (e.g. conversion of electronic formats) there may be variances between the accounting documents contained in this annual report and those submitted to the Federal Gazette (Bundesanzeiger). In this case, the version submitted to the Federal Gazette shall be binding.

The reporting period comprises the financial year 2017, which runs from January 01 to December 31, 2017. This report reflects relevant information available by the editorial deadline on February 19, 2018.

Rounding differences may occur.

This English version of the annual report is a translation of the original German version; in the event of variances, the German version shall take precedence over the English translation.

For better readability, this report generally uses only the masculine form when referring to groups of persons. Unless indicated otherwise, these statements should not be construed to refer to a specific gender.

Schaeffler in Social Media

Summary – 1st quarter 2016 to 4th quarter 2017

	2016				2017			
Income statement (in € millions)	1st quarter	2nd quarter	3rd quarter	4th quarter	1st quarter	2nd quarter	3rd quarter	4th quarter
Revenue	3,343	3,369	3,265	3,361	3,574	3,472	3,434	3,541
EBIT	421	438	417	280	435	358	416	319
• in % of revenue	12.6	13.0	12.8	8.3	12.2	10.3	12.1	9.0
EBIT before special items [1]	421	438	417	424	435	345	416	388
• in % of revenue	12.6	13.0	12.8	12.6	12.2	9.9	12.1	11.0
Net income [2]	253	241	178	187	279	206	306	189
Earnings per common non-voting share (basic/diluted, in €)	0.38	0.37	0.27	0.28	0.42	0.31	0.46	0.29
Statement of financial position (in € millions)								
Total assets	12,607	12,554	12,862	11,564	11,941	11,120	11,536	11,537
Shareholders' equity [3]	1,609	1,425	1,554	1,997	2,400	2,168	2,401	2,548
• in % of total assets	12.8	11.4	12.1	17.3	20.1	19.5	20.8	22.1
Net financial debt	4,909	4,874	2,876	2,636	2,742	2,956	2,620	2,370
• Net financial debt to EBITDA ratio before special items [1) 4)]	2.1	2.0	1.2	1.1	1.1	1.2	1.1	1.0
• Gearing ratio (Net financial debt to shareholders' equity [3], in %)	305.1	342.0	185.1	132.0	114.3	136.3	109.1	93.0
Statement of cash flows (in € millions)								
EBITDA	598	619	600	476	624	551	605	515
• in % of revenue	17.9	18.4	18.4	14.2	17.5	15.9	17.6	14.5
EBITDA before special items [1]	598	619	600	620	624	538	605	584
• in % of revenue	17.9	18.4	18.4	18.4	17.5	15.5	17.6	16.5
Cash flows from operating activities	206	571	528	571	186	320	610	662
Capital expenditures (capex) [5]	318	243	268	317	299	295	279	400
• in % of revenue (capex ratio)	9.5	7.2	8.2	9.4	8.4	8.5	8.1	11.3
Free cash flow	-112	328	263	256	-130	41	333	244
Value-based management								
ROCE before special items (in %) [1) 4)]	22.8	23.2	22.6	22.3	22.1	20.7	20.5	19.9
Schaeffler Value Added before special items (in € millions) [1) 4)]	928	973	944	939	938	837	829	787
Employees								
Headcount (at end of reporting period)	85,016	85,225	86,029	86,662	87,341	87,937	89,359	90,151

1) Please refer to pp. 60 et seq. for the definition of special items.
2) Attributable to shareholders of the parent company.
3) Including non-controlling interests.
4) EBIT/ EBITDA based on the last twelve months.
5) Capital expenditures on intangible assets and property, plant and equipment.

	2016				2017			
Automotive (in € millions)	1st quarter	2nd quarter	3rd quarter	4th quarter	1st quarter	2nd quarter	3rd quarter	4th quarter
Revenue	2,578	2,604	2,525	2,631	2,791	2,664	2,643	2,771
EBIT	367	368	362	276	367	290	345	281
• in % of revenue	14.2	14.1	14.3	10.5	13.1	10.9	13.1	10.1
EBIT before special items [1]	367	368	362	384	367	277	345	341
• in % of revenue	14.2	14.1	14.3	14.6	13.1	10.4	13.1	12.3
Industrial (in € millions)								
Revenue	765	765	740	730	783	808	791	770
EBIT	54	70	55	4	68	68	71	38
• in % of revenue	7.1	9.2	7.4	0.5	8.7	8.4	9.0	4.9
EBIT before special items [1]	54	70	55	40	68	68	71	47
• in % of revenue	7.1	9.2	7.4	5.5	8.7	8.4	9.0	6.1

Prior year information presented based on 2017 segment structure.
1) Please refer to pp. 60 et seq. for the definition of special items.

Multi-year comparison

	2013	2014	2015	2016	2017
Income statement (in € million)					
Revenue	11,205	12,124	13,179	13,338	14,021
EBIT	1,008	1,523	1,402	1,556	1,528
• in % of revenue	9.0	12.6	10.6	11.7	10.9
EBIT before special items [1]	1,436	1,561	1,676	1,700	1,584
• in % of revenue	12.8	12.9	12.7	12.7	11.3
Net income [2]	127	654	591	859	980
Earnings per common non-voting share (basic/diluted, in €)	-	1.29	1.28	1.30	1.48
Statement of financial position (in € millions)					
Total assets	8,387	11,617	12,480	11,564	11,537
Shareholders' equity [3]	-1,966	258	1,568	1,997	2,548
• in % of total assets	-23.4	2.2	12.6	17.3	22.1
Net financial debt	5,447	5,778	4,889	2,636	2,370
• Net financial debt to EBITDA ratio before special items [1]	2.6	2.6	2.1	1.1	1.0
• Gearing ratio (Net financial debt to shareholders' equity [3], in %)	-	2,239.5	311.8	132.0	93.0
Statement of cash flows (in € millions)					
EBITDA	1,660	2,172	2,096	2,293	2,295
• in % of revenue	14.8	17.9	15.9	17.2	16.4
EBITDA before special items [1]	2,088	2,210	2,370	2,437	2,351
• in % of revenue	18.6	18.2	18.0	18.3	16.8
Cash flows from operating activities [4]	1,027	900	1,372	1,876	1,778
Capital expenditures (capex) [5]	572	857	1,025	1,146	1,273
• in % of revenue (capex ratio)	5.1	7.1	7.8	8.6	9.1
Free cash flow [4]	473	48	370	735	488
Value-based management					
ROCE before special items (in %) [1]	22.6	23.7	23.1	22.3	19.9
Schaeffler Value Added before special items (in € millions) [1]	801	902	952	939	787
Employees					
Headcount (at end of reporting period)	78,258	82,294	84,198	86,662	90,151

[1] Please refer to pp. 60 et seq. for the definition of special items.
[2] Attributable to shareholders of the parent company.
[3] Including non-controlling interests.
[4] Including an outflow of EUR 371 m for the EU antitrust penalty in 2014.
[5] Capital expenditures on intangible assets and property, plant and equipment.

Financial calendar

March 07, 2018

Publication of annual results 2017

April 20, 2018

Annual general meeting 2018

May 08, 2018

Publication of results for the first three months 2018

August 07, 2018

Publication of results for the first six months 2018

November 07, 2018

Publication of results for the first nine months 2018

All information is subject to correction and
may be changed at short notice.

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Strategic initiative “Agenda 4 plus One”

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