

2.4 Financial position and finance management

Cash flow and liquidity

The Schaeffler Group generated free cash flow of EUR 735 m (prior year: EUR 370 m) in 2016.

Cash flow		No. 048	
in € millions	2016	2015	Change in %
Cash flows from operating activities	1,876	1,372	36.7
Cash used in investing activities	-1,141	-1,002	13.9
Free cash flow	735	370	98.6
Cash used in financing activities	-466	-212	> 100
Net increase in cash and cash equivalents	269	158	70.3
Effects of foreign exchange rate changes on cash and cash equivalents	3	5	-40.0
Cash and cash equivalents as at beginning of period	799	636	25.6
Cash and cash equivalents	1,071	799	34.0

The increase in cash flows from operating activities by EUR 504 m to EUR 1,876 m (prior year: EUR 1,372 m) was mainly the result of significantly lower interest payments as well as higher EBITDA. Net interest paid and received amounted to EUR -181 m (prior year: EUR -465 m). The company paid EUR 327 m (prior year: EUR 358 m) in income taxes. Cash outflows related to expanding working capital amounted to EUR 22 m and were lower than the prior year amount of EUR 116 m.

Capital expenditures on property, plant and equipment and intangible assets (capex) amounted to EUR 1,146 m (prior year: EUR 1,025 m) in 2016. The capex ratio was 8.6 % (prior year: 7.8 %) of consolidated revenue in 2016. Capital expenditures of EUR 657 m (prior year: EUR 556 m) related to the Europe Region, EUR 234 m (prior year: EUR 250 m) to Greater China, EUR 209 m (prior year: EUR 170 m) to Americas, and EUR 46 m (prior year: EUR 49 m) to Asia/Pacific. In order to strengthen its competitive position, the Schaeffler Group primarily invested in expanding capacity and in equipment and machinery for product start-ups.

Capital expenditures by region (Capex)		No. 049	
		in € millions	Change in %
Europe		657 556	18.2
Americas		209 170	22.9
Greater China		234 250	-6.4
Asia/Pacific		46 49	-6.1
Schaeffler Group		1,146 1,025	11.8

Regions reflect the regional structure of the Schaeffler Group.

These developments resulted in free cash flow of EUR 735 m (prior year: EUR 370 m) for 2016.

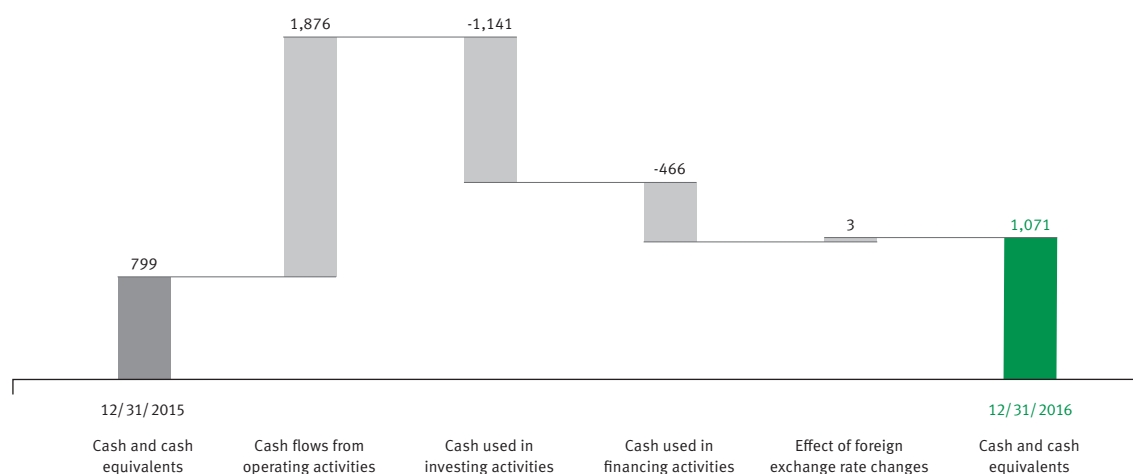
EUR 466 m in net cash was used in financing activities (prior year: EUR 212 m) during the year, including cash provided by the prepayment in full of a loan receivable by Schaeffler AG from its shareholder IHO Verwaltungs GmbH of EUR 1,773 m (prior year: EUR 197 m). These funds were used to redeem bonds with a principal of EUR 1,756 m in the fourth quarter. EUR 1.0 bn in cash was provided to the Schaeffler Group by a new Facilities Agreement signed in the third quarter of 2016; these funds were used to repay the two remaining institutional term loans totaling EUR 418 m, and to redeem the EUR 600 m EUR bond series. A total of EUR 136 m in cash was used for additional repayments and to terminate related cross-currency derivatives. The company paid EUR 329 m in dividends, including EUR 328 m paid to shareholders of Schaeffler AG.

Cash and cash equivalents increased by EUR 272 m to EUR 1,071 m as at December 31, 2016.

Change in cash and cash equivalents

No. 050

in € millions



At December 31, 2016, cash and cash equivalents amounted to EUR 1,071 m (prior year: EUR 799 m) and consisted primarily of bank balances. EUR 325 m (prior year: EUR 198 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 1.0 bn), of which EUR 13 m (EUR 24 m) were utilized at December 31, 2016, primarily in the form of letters of credit.

Financial debt

The group's net financial debt was reduced by EUR 2,253 m to EUR 2,636 m (prior year: EUR 4,889 m), primarily as a result of the prepayment in full of a loan receivable from the company's shareholder IHO Verwaltungs GmbH of EUR 1,674 m in September 2016. In May 2016, IHO Verwaltungs GmbH had already repaid approximately EUR 99 m of this loan. The Schaeffler Group used these funds as well as additional available liquidity to prepay financial debt. A significant improvement in free cash flow further reduced net financial debt.

Net financial debt

No. 051

in € millions	12/31/2016	12/31/2015	Change in %
Bonds	2,719	5,048	-46.1
Facilities Agreement	982	632	55.4
Other financial debt	6	8	-25.0
Total financial debt	3,707	5,688	-34.8
Cash and cash equivalents	1,071	799	34.0
Net financial debt	2,636	4,889	-46.1

The debt to EBITDA ratio, defined as the ratio of net financial debt to earnings before financial result, income taxes, depreciation and amortization and impairment losses (EBITDA), amounted to 1.1 at December 31, 2016 (prior year: 2.3). The net debt to EBITDA ratio before special items, was 1.1 (prior year: 2.1).

The gearing ratio, the ratio of net debt to equity, was 132.0 % at December 31, 2016 (prior year: 311.8 %).

In May 2016, Schaeffler AG voluntarily prepaid approximately EUR 229 m of its institutional term loans using the proceeds of a partial prepayment of a loan receivable from the company's shareholder IHO Verwaltungs GmbH of approximately EUR 99 m and additional available liquidity.

Schaeffler AG signed a new Facilities Agreement on July 18, 2016. The funds were used to repay the two institutional term loans totaling approximately EUR 418 m still outstanding at that date and to fully redeem EUR bonds totaling EUR 600 m, bearing interest at 4.25 %, and originally due in 2018.

The new Facilities Agreement consists of a EUR 1.0 bn term loan and a EUR 1.3 bn revolving credit facility. Both facilities have a five year maturity plus certain renewal options and are provided by a consortium of 15 international banks. In addition to offering considerably better interest terms, the new Facilities Agreement especially enhanced the Schaeffler Group's operating and financial flexibility by providing for significantly more favorable credit terms and the release of nearly all assets pledged as in rem security, which were subsequently also released from such pledges under the secured bond agreements.

In September 2016, IHO Verwaltungs GmbH prepaid loans payable to Schaeffler AG of approximately EUR 1,674 m. The Schaeffler Group used these funds together with additional available liquidity to redeem three bond series. On October 07, 2016, the company fully redeemed a USD bond series with a principal of USD 850 m, a coupon of 4.75 %, and an original maturity of 2021. On October 13, 2016, the company fully repaid two EUR bond

series with a principal of EUR 500 m each, a coupon of 3.25 % and 2.75 %, respectively, and an original maturity of 2019.

In connection with the refinancing of IHO Verwaltungs GmbH, rating agency Moody's announced the separation of the previous Schaeffler Group company rating into two separate company ratings for Schaeffler AG and IHO Verwaltungs GmbH on September 07, 2016. As a result, the Schaeffler AG company rating has improved to Baa3 (investment grade) with a stable outlook. At the same time, Moody's also upgraded the issuance ratings of all bonds issued by Schaeffler Finance B.V., Barneveld, Netherlands, to Baa3.

Having upgraded Schaeffler AG's company rating to BB on April 28, 2016, rating agency Standard & Poor's once again raised the rating to BB+ (outlook: stable) on September 21, 2016 in connection with the refinancing of IHO Verwaltungs GmbH referred to above. The issuance ratings of the secured bonds issued by Schaeffler Finance B.V., Barneveld, Netherlands, were also improved to BB+ at the same time.

At December 31, 2016, the Schaeffler Group's Facilities Agreement comprised the following tranches:

Facilities Agreement Schaeffler Group

No. 052

Tranche	Currency	12/31/2016	12/31/2015	12/31/2016	12/31/2015	12/31/2016	12/31/2015	Maturity
		Face value in millions		Carrying amount in € millions		Coupon		
Senior Term Loan B	EUR	0	250	0	251	n/a	Euribor ¹⁾ + 3.50 %	05/15/2020
Senior Term Loan B	USD	0	440	0	392	n/a	Libor ¹⁾ + 3.50 %	05/15/2020
Senior Term Loan	EUR	1,000	0	992	0	Euribor ²⁾ + 1.20 % ³⁾	n/a	07/18/2021
Revolving Credit Facility ⁴⁾	EUR	0	1,000	0	-11	n/a	Euribor + 2.6875 %	10/27/2019
Revolving Credit Facility ⁴⁾	EUR	1,300	0	-10	0	Euribor ²⁾ + 0.80 % ³⁾	n/a	07/18/2021
Total				982	632			

¹⁾ Euribor/Libor floor of 0.75 %.

²⁾ Euribor floor of 0.00 %.

³⁾ Since November 10, 2016.

⁴⁾ EUR 13 m (December 31, 2015: EUR 24 m) were drawn down as at December 31, 2016, primarily in the form of letters of credit.

In addition, the Schaeffler Group had further lines of credit in the equivalent of approximately EUR 166 m, primarily for the U.S. and China.

The following bonds issued by Schaeffler Finance B.V., Barneveld, Netherlands, were outstanding as at December 31, 2016:

Schaeffler Group bonds

No. 053

ISIN	Currency	Face value in millions		Carrying amount in € millions		Coupon	Maturity
		12/31/2016	12/31/2015	12/31/2016	12/31/2015		
XS0923613060 ¹⁾	EUR	0	600	0	597	4.25 %	05/15/2018
XS1067864881 ^{2) 3)}	EUR	0	500	0	497	3.25 %	05/15/2019
XS1067862919 ³⁾	EUR	0	500	0	497	2.75 %	05/15/2019
XS1212469966	EUR	400	400	397	396	2.50 %	05/15/2020
US806261AJ29	USD	700	700	658	637	4.25 %	05/15/2021
US806261AE32 ⁴⁾	USD	0	850	0	777	4.75 %	05/15/2021
XS1067864022	EUR	500	500	498	499	3.50 %	05/15/2022
US806261AM57	USD	600	600	571	553	4.75 %	05/15/2023
XS1212470972	EUR	600	600	595	595	3.25 %	05/15/2025
Total				2,719	5,048		

¹⁾ Redeemed in full on August 18, 2016.

²⁾ Bonds are unsecured.

³⁾ Redeemed in full on October 13, 2016.

⁴⁾ Redeemed in full on October 07, 2016.

The Schaeffler bonds are listed on the Euro MTF market of the Luxembourg Stock Exchange.

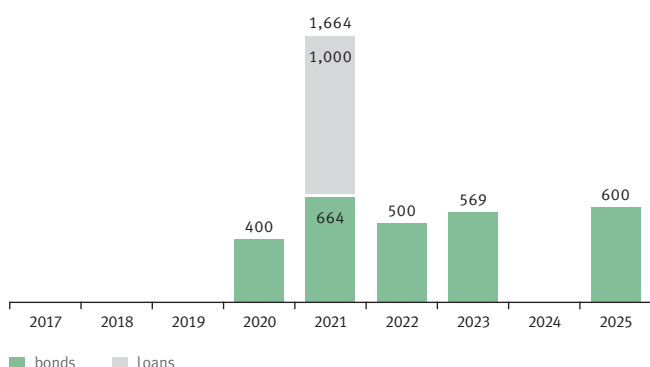
The company's maturity profile, which consists of the term loan and the bonds issued by Schaeffler Finance B.V., Barneveld, Netherlands, was as follows as at December 31, 2016:

financial covenants is monitored continually and reported to the lending banks on a regular basis. Until Schaeffler AG entered into its new Facilities Agreement on July 18, 2016, the financial covenants consisted of a leverage covenant and an interest cover covenant. The new Facilities Agreement only contains a leverage covenant. The company has complied with the financial covenants as stipulated in the Facilities Agreement throughout 2016.

Maturity profile

No. 054

Principal outstanding as at December 31, 2016 in € millions



Schaeffler AG's Facilities Agreement requires the group to comply with certain financial covenants. Compliance with these

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.

External group financing is primarily provided by capital market instruments as well as syndicated and bilateral lines of credit from international banks. One such line of credit is a contractually agreed revolving credit facility of EUR 1,300 m available to cover any short- to medium-term liquidity needs. Please refer to section 2.4 “Financial position and finance management” – “Financial debt” for further detail on the various instruments representing the group financing arrangements.

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’s total assets decreased by EUR 916 m or 7.3 % to EUR 11,564 m (prior year: EUR 12,480 m) in 2016.

Consolidated statement of financial position (abbreviated) No. 055

in € millions	12/31/2016	12/31/2015	Change in %
Total non-current assets	5,979	7,438	-19.6
Total current assets	5,585	5,042	10.8
Total assets	11,564	12,480	-7.3
Total shareholders equity	1,997	1,568	27.4
Total non-current liabilities	6,361	8,144	-21.9
Total current liabilities	3,206	2,768	15.8
Total assets	11,564	12,480	-7.3

Non-current assets declined by EUR 1,459 m to EUR 5,979 m as at December 31, 2016 (prior year: EUR 7,438 m), primarily due to the prepayment of a loan of EUR 1,773 m that was receivable from the company’s shareholder IHO Verwaltungs GmbH. The decrease was partially offset by a EUR 327 m increase in property, plant and equipment. Additions to intangible assets and property, plant and equipment amounted to EUR 1,115 m and were primarily invested in expanding capacity and in equipment and machinery for product start-ups in the Automotive division. The Automotive division accounted for approximately 81 % of total additions for the reporting period.

Current assets increased by EUR 543 m to EUR 5,585 m (prior year: EUR 5,042 m) in 2016. The increase was largely attributable to the increase in cash and cash equivalents (see “Cash flow”, pp. 49 et seq.). Higher inventories and trade receivables also contributed to the increase in current assets.