SCHAEFFLER

Annual Report 2016 | Mobility for tomorrow

Digitalization – A Key Opportunity for 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)	2016	2015		Change
Revenue	13,338	13,179	1.2	%
• at constant currency			3.4	%
EBIT	1,556	1,402	11.0	%
• in % of revenue	11.7	10.6	1.1	%-pts.
EBIT before special items [1]	1,700	1,676	1.4	%
• in % of revenue	12.7	12.7	0.0	%-pts.
Net income [2]	859	591	45.3	%
Earnings per common non-voting share (basic/diluted, in €) [3]	1.30	1.28	1.6	%
Statement of financial position (in € millions)	**12/31/2016**	**12/31/2015**		Change
Total assets	11,564	12,480	-7.3	%
Shareholders' equity [4]	1,997	1,568	429	€ millions
• in % of total assets	17.3	12.6	4.7	%-pts.
Net financial debt	2,636	4,889	-46.1	%
• Net financial debt to EBITDA ratio before special items [1]	1.1	2.1		
• Gearing Ratio (Net financial debt to shareholders' equity, in %)	132.0	311.8	-179.8	%-pts.
Statement of cash flows (in € millions)	**2016**	**2015**		Change
EBITDA	2,293	2,096	9.4	%
• in % of revenue	17.2	15.9	1.3	%-pts.
EBITDA before special items [1]	2,437	2,370	2.8	%
• in % of revenue	18.3	18.0	0.3	%-pts.
Cash flows from operating activities	1,876	1,372	504	€ millions
Capital expenditures (capex) [5]	1,146	1,025	121	€ millions
• in % of revenue (capex ratio)	8.6	7.8	0.8	%-pts.
Free cash flow	735	370	365	€ millions
Value Added	**2016**	**2015**		Change
ROCE before special items (in %) [1]	21.7	22.5	-0.8	%-pts.
Schaeffler Value Added before special items (in € millions) [1]	915	931	-1.7	%
Employees	**12/31/2016**	**12/31/2015**		Change
Headcount	86,662	84,198	2.9	%

[1] EBIT, debt to EBITDA ratio, EBITDA, ROCE, and Schaeffler Value Added before special items, please refer to page 48.
[2] Attributable to shareholders of the parent company.
[3] Earnings per share were calculated in accordance with IAS 33, please refer to page 42.
[4] Including non-controlling interests.
[5] Capital expenditures on intangible assets and property, plant and equipment.

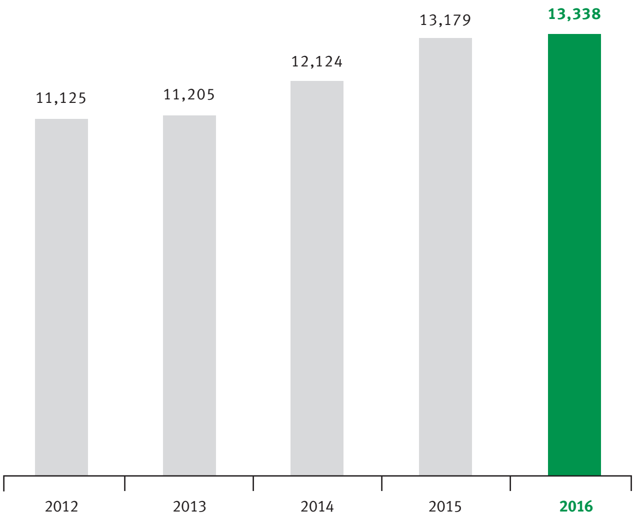
Automotive (in € millions)	2016	2015		Change
Revenue	10,333	9,977	3.6	%
• at constant currency			6.0	%
EBIT	1,383	1,135	21.9	%
• in % of revenue	13.4	11.4	2.0	%-pts.
EBIT before special items [1]	1,491	1,373	8.6	%
• in % of revenue	14.4	13.8	0.6	%-pts.
Industrial (in € millions)	**2016**	**2015**		Change
Revenue	3,005	3,202	-6.2	%
• at constant currency			-4.8	%
EBIT	173	267	-35.2	%
• in % of revenue	5.8	8.3	-2.5	%-pts.
EBIT before special items [1]	209	303	-31.0	%
• in % of revenue	7.0	9.5	-2.5	%-pts.

Prior year information presented based on 2016 segment structure.
[1] EBIT before special items, please refer to page 48.

Key financials

Revenue 2012 – 2016

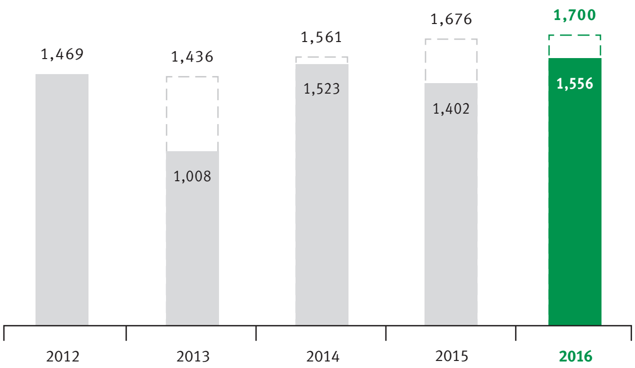
in € millions



	2012	2013	2014	2015	2016
Revenue growth vs. prior year	+ 4.0 %	+ 0.7 %	+ 8.2 %	+ 8.7 %	**+ 1.2 %**
Revenue growth at constant currency					**+ 3.4 %**

EBIT 2012 – 2016

in € millions

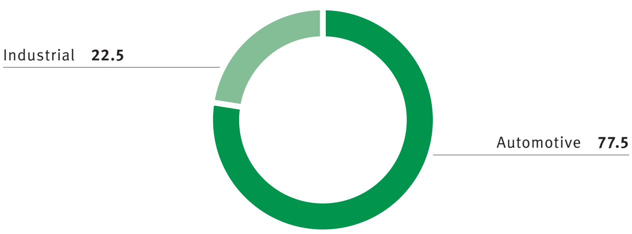


	2012	2013	2014	2015	2016
EBIT margin	13.2 %	9.0 %	12.6 %	10.6 %	**11.7 %**
EBIT margin before special items	–	12.8 %	12.9 %	12.7 %	**12.7 %**

EBIT before special items

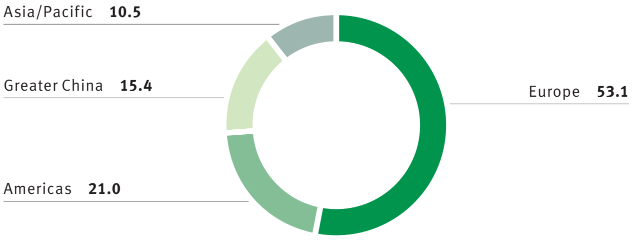
Schaeffler Group revenue by division

in percent



Schaeffler Group revenue by region

in percent by market view



Highlights 2016

Revenue increased further

Revenue at **EUR 13.3 bn**
(up 3.4 % at constant currency)

EBIT margin at high prior year level

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

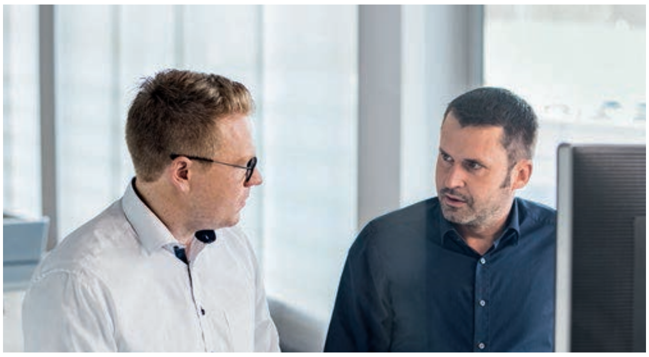
Positive free cash flow trend

Free cash flow at **EUR 735 m**
(prior year: EUR 370 m)

Net income up significantly from prior year

Net income at **EUR 859 m**
(prior year: EUR 591 m)

Digitalization – A Key Opportunity for the Future



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Major events in 2016

January

Detroit: At the North American International Auto Show (NAIAS), Schaeffler presents innovations that make automobiles safer, more environmentally friendly, and more comfortable. The products on show are customized to the requirements of the region. One means of display is the “Glass Car”, an exhibit that includes around 40 products and technologies.

April

Nuremberg: The first Annual General Meeting after the initial public offering is another milestone in corporate history. The Chairman of the Supervisory Board, Georg F. W. Schaeffler, welcomes over 350 shareholders and media representatives in Nuremberg’s Frankenhalle.

Berlin: Schaeffler’s E-Clutch takes first place in the “Automobility” category at the environmental and business prize, the GreenTec Awards. The technology reduces CO2 emissions by between three and eight percent under real operating conditions.

Herzogenaurach: Schaeffler is presented with the “2016 German Innovation Award” in the “Large Companies” category for its active mechatronic roll control. With the volume production of this system, which started in August 2015, Schaeffler has opened up a new chapter in chassis technology.

Hanover: At the 2016 Hannover Messe, Schaeffler showcases solutions for digitalized production and machine monitoring with its “Drive Train 4.0” technology exhibit. In focus are two new digital services: the calculation of rolling bearings’ remaining useful life and automated rolling bearing diagnostics.

May

Fort Mill/Wooster: The Schaeffler Group increases its capacity at two U.S. locations by building new manufacturing halls and administration buildings. Schaeffler invests about 80 million euros and creates more than 350 new jobs.

Carisio/Momo: The Schaeffler Group’s most modern warehouse is now officially in operation. As part of the step-by-step expansion of its European distribution network, Schaeffler opens its European Distribution Center (EDC) South in Carisio, Italy. The EDC South will supply products to all customers of the Industrial Division in southeastern and southern European countries. The new warehouse is designed to ensure even faster and more reliable supplies.

July

Erlangen: SHARE – Schaeffler Hub for Advanced REsearch – is synonymous with Schaeffler's strategic cooperation with colleges and universities. Following the collaboration with KIT (Karlsruhe Institute of Technology), Schaeffler forms another collaborative research project with the Friedrich-Alexander University of Erlangen-Nuremberg. The focus of the research undertaken by SHARE at FAU is on digitalization and production processes.

October

Herzogenaurach: Schaeffler enters into a strategic partnership with IBM as its partner for digital transformation. IBM will act as the technology provider, consultant and development partner for a digital ecosystem to support Schaeffler in the integration of its mechatronic components, systems, and machines into the rapidly expanding world of the "Internet of Things" (IoT), as well as implementing market-ready new business models based on digital services.

Nanjing/Chonburi: Schaeffler celebrates the opening of new production halls in China and the inauguration of a new plant in Thailand with traditional local ceremonies. The increase in production capacity means that Schaeffler has moved even closer to its customers in Chinese and Asian markets.

November

Herzogenaurach: With its strategy "Mobility for tomorrow", adopted in November following in-depth consultations with management and the Supervisory Board, Schaeffler sets the course for future sustainable growth. Based on four crucial megatrends – climate change, urbanization, globalization and digitalization, the company concentrates on 4 focus areas across divisions and regions: "Eco-friendly drives", "Urban mobility", "Interurban mobility," and "Energy chain". 8 strategic pillars define the scope for action for the next years. The content of the strategy is based on three main topics: E-Mobility, Industry 4.0, and Digitalization; implementation is to proceed in accordance with the excellence program "Agenda 4 plus One" which comprises 16 strategic initiatives.

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."

December

Herzogenaurach: Quality summary 2016: Schaeffler's top quality convinces customers worldwide – and it is getting better all the time. In 2016, the company receives more awards than ever before. In 75 plants around the world, Schaeffler manufactures about 60,000 automotive and 90,000 industrial products in large volumes. In total, the company sells more than 7.1 billion products.

Romanshorn/Magdeburg/Starnberg: Schaeffler concentrates on selected core competencies and future fields of development. With this strategic portfolio focus in mind, the company sells its fine blanking activities in Switzerland and its cylinder head manufacturing unit in Magdeburg, Germany. In turn, Schaeffler increases its expertise for the expansion of electric mobility by acquiring a 51 percent stake in electric motor manufacturer Compact Dynamics. In addition, Schaeffler and SEMIKRON agree on a cooperation for the development of power electronics systems and the integration of power electronics components.

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

Ladies and Gentlemen,

As a listed company and a family business, for which we bear responsibility as family shareholders, Schaeffler successfully rose to the challenges which emerged during the year 2016. The Schaeffler Group continued on its path of growth despite further increasing competition and complex economic, technological, social, and geopolitical conditions. Thanks to another year of strong Automotive business, total revenue increased to 13.3 billion euros. The Industrial Division, however, continued to operate in the face of a difficult market environment, which necessitated the implementation of additional measures as part of our "CORE" program. Aimed at further streamlining the industrial business structures and reducing production and administrative costs, these were applied in an effort to sustainably improve the results of the entire Industrial division.

Our deeply committed employees and the close proximity to our customers are two of the key success factors for our company. To this end, Schaeffler once again invested both in existing and new locations around the world during the past year. Enabling us to further expand our capacities and delivery performance, we enlarged our plants in the U.S. and China, opened a new plant in Thailand, established a new office in Moscow, inaugurated our logistics center in Italy and started construction work on our new central warehouse in Kitzingen, Germany.

Following in-depth consultations with management and the Supervisory Board, the Executive Board finalized our strategy "Mobility for tomorrow" as a long-term approach to addressing the major challenges and opportunities facing our company. In the tradition of a family business, a strong foundation of values is part of our corporate culture, which we have summarized in four core values: sustainable, innovative, excellent, and passionate.

Being family shareholders, everything we do is determined by long-term entrepreneurial thinking. E-Mobility, Industry 4.0, and Digitalization are areas signifying substantial technological, social, and economic changes and will create new opportunities for future growth. We have already taken major steps to actively shape this development. In late 2016, Schaeffler acquired 51 percent of the shares of electric motor manufacturer Compact Dynamics as a move to expand its expertise in electric mobility. Furthermore, the "Digital Agenda" was adopted in the middle of last year, and the strategic partnership with IBM marked the beginning of the company's digital transformation. It was with this in mind that "Digitalization – A Key Opportunity for the Future" was chosen as the theme for the 2016 annual report. We want to demonstrate exactly what Schaeffler is doing to make Products & Services, Machines & Processes, Analyses & Simulation, as well as User Experience & Customer Value even smarter, thereby generating added value for our customers.

"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." This philosophy of the Schaeffler Group is put into practice by our approximately 86,000 employees worldwide. Their knowledge, commitment, creativity, and high level of identification with the company make a decisive contribution to Schaeffler's success. We would therefore like to express our sincere thanks to all our employees, as well as to our customers, suppliers, service providers, and research partners for their continued trust and cooperation.

Yours sincerely,

Schaeffler-Thumann | Georg F.W. Schaeffler

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

Klaus Rosenfeld
Chief Executive Officer

Ladies and gentlemen,

With this annual report, it is our pleasure to present and explain to you the development of the Schaeffler Group during the past financial year.

2016 was an eventful year. We moved things forward and achieved a great deal. This is true not only for our financial result and business successes, but most notably with regard to the further advancement of the Schaeffler Group into becoming a leading global automotive and industrial supplier.

The environment in which we operate has become increasingly uncertain, complex, volatile, and ambiguous. This holds true for the macroeconomic uncertainties and political risks to which we are exposed, as well as for the overall operating conditions and technological change that affect our business worldwide. Therefore, it is all the more important for us to focus on our strengths and address issues that can and need to be improved.

Strong result – Financial flexibility restored

The result delivered by the Schaeffler Group in the 2016 financial year is impressive. We continued to grow. Our revenue rose to around EUR 13.3 bn, corresponding to a 3.4 % increase p.a. at constant currency. The main driving force for this development was our Automotive business, which grew by 6.0 % p.a. at constant currency. Revenue in our Industrial division decreased by 4.8 % at constant currency due to market-related factors. In the course of the year, a stabilization in revenue development became evident.

On this basis, we generated earnings before interest and taxes (EBIT) before special items of EUR 1,700 m. This corresponds to an adjusted EBIT margin of 12.7 %, which means that we have maintained our earnings quality at an above-average level.

Free cash flow developed in a particularly positive manner. Totaling EUR 370 m in the prior year, it rose to EUR 735 m in the 2016 financial year. Even if the figure for the prior year was adjusted for one-time items of approximately EUR 170 m, this increase is impressive proof of the exceptional high quality and cash flow generation power of our operating business. This is all the more evidenced by the fact that our capital expenditure in financial year 2016 was higher than in the prior year.

Additionally, in the course of 2016 we achieved a significant reduction in the Schaeffler Group's net debt. While net debt had amounted to EUR 4.9 bn at the end of 2015, it stood at EUR 2.6 bn on December 31, 2016. At the same time, the net debt to adjusted EBITDA ratio improved from 2.1x to 1.1x. Thanks to the early repayment of liabilities by IHO Holding and the resulting cash inflow, which we used for prepayments of loans, we were assigned an investment grade rating from Moody's in October 2016. This means we not only achieved our strategic targets much earlier than expected, but also regained the necessary financial flexibility to supplement our growth strategy by making selective, technology-oriented acquisitions.

**Strategy "Mobility for tomorrow" adopted –
Excellence program "Agenda 4 plus One" launched**

The year 2016 was characterized by more than just our strong result and restored financial flexibility. In my view, it was particularly important that, after intensive preliminary work and discussions, the Executive Board and Supervisory Board of Schaeffler AG adopted the strategy "Mobility for tomorrow" finalized during 2016, and that we communicated it externally and internally. Following our IPO in 2015, this means we have reached another milestone in consistently making the Schaeffler Group equipped for the future.

Our strategy "Mobility for tomorrow" encompasses four main elements. The starting point is our vision to shape the future of mobility with a passion for innovation and the highest standards of quality as a technology partner of our customers. We thereby want to make a contribution to a world that will be cleaner, safer and smarter.

As an integrated automotive and industrial supplier, we are wherever things move. Here, we concentrate on 4 focus areas: (1) Eco-friendly drives, (2) Urban mobility, (3) Interurban mobility, and (4) Energy chain. At the heart of our strategy are 8 strategic pillars, which describe the scope for future action. In addition, there is an implementation program of 16 strategic initiatives, which we call "Agenda 4 plus One". Read more about our strategy and its elements on pages 18 to 22 of this annual report.

As the Executive Board of Schaeffler AG, we are convinced that our strategy "Mobility for tomorrow" provides a resilient framework with which we can successfully position the Schaeffler Group for the future. The positive feedback we have received from our customers and business partners, as well as from our employees and management, confirms this assessment.

E-Mobility, Industry 4.0, and Digitalization – Key opportunities for the future

As can be seen from the 5th strategic pillar of our strategy "Mobility for tomorrow", we will be focusing on three key items that are relevant for the future: E-Mobility, Industry 4.0, and Digitalization.

Without any doubt, the global automotive industry is facing major technological changes. The electrification of the drive train is one of the most important future trends in this context. As an automotive supplier with a high level of manufacturing expertise and in-depth understanding of systems – please remember the motto of our 2015 annual report – we consider this development a challenge, but also a great opportunity for the future. We have been investing in the required capacities over the past few years. This also applies to the fields of R&D and production. The number of customer projects and volume production orders is growing steadily. The purchase of electric motor manufacturer Compact Dynamics is a first step in strengthening the Schaeffler Group's technological competence through external acquisitions.

While electric mobility plays a crucial role for our Automotive division, its equivalent for our Industrial division is the topic of Industry 4.0. This is another promising future opportunity for us. Here, too, manufacturing expertise and an in-depth understanding of systems are called for. Anyone who knows how to design and build rolling bearings and is familiar with complex systems at the same time – whether in mechanical, automotive, or plant engineering – will understand that bearings are ideally suited to generate data. Based on these data, we are able to gain insights that we will utilize to create additional benefits and added value for our customers. This is our concept of Industry 4.0.

Digitalization, our third key opportunity for the future, goes even beyond this. It is not just about new products and services that are in the interest of customers. It is also about our own machines and processes. This involves analysis and simulation options, as well as the development of new algorithms and interfaces that help us optimize and control our own operations. In this, we are aware that the acceptance of digital offers – both internal and external – depends not only on the quality of the data used, but also on positive user experiences. There is enormous potential in all these areas, and we are determined to consistently leverage and put it to good use. These are highly challenging tasks for which we are preparing systematically. To this end, we have developed our "Digital Agenda" as part of our "Agenda 4 plus One". It includes four elements – Products & Services, Machines & Processes, Analyses & Simulation, and User Experience & Customer Value. Implementation of the "Digital Agenda" needs to proceed at a fast pace and we are making good headway. It is not without reason that we have chosen "Digitalization – A Key Opportunity for the Future" as the motto for our 2016 annual report. Take a tour of discovery and pay particular attention to pages i18 to i35 of this report.

Continued growth – Creating lasting value

Despite a continually challenging environment, we have set ourselves ambitious targets for 2017. We want to grow 4 to 5 % p.a. at constant currency, achieve an EBIT margin before special items of between 12 and 13 % and a free cash flow of around EUR 600 m before external growth. In addition, we want to pay 30 to 40 % of our adjusted net income in dividends. These are ambitious goals. But in addition to these financial targets, we also want to make the Schaeffler Group even more attractive and enhance its image internally and externally. We want to continue to invest, and to create new and, above all, future-oriented jobs. We want to play an active part in shaping the vast changes in the markets and regions in which we operate. We want to continue to be innovative. And we want to create lasting value and assets – all of this in the interest of our customers, business partners and our many employees, and of course, in the interest of you.

Ladies and gentlemen, dear shareholders, the year 2016 was an eventful year. We made significant headway. Our results are impressive. Our strategy is adopted. We are looking forward to the future with confidence. At the same time, we are aware that we will only be successful if we combine long-term thinking and our proven success factors with strength in innovation and future-oriented action. We want to shape the "mobility for tomorrow" with and for our customers. That is our aspiration. This can only be achieved through good leadership and a strong foundation of values: sustainable, innovative, excellent and passionate. That's what we stand for.

On this note, and on behalf of my colleagues on the Executive Board, I would like to extend my sincere thanks to our family shareholders, members of the Supervisory Board, and to you for the good, constructive and trustful cooperation throughout 2016. Special thanks go to our employees around the world, whose excellent and hard work has made the remarkable results of 2016 possible. I look forward to our continued cooperation in the years ahead.

Kind regards,

Klaus Rosenfeld
Chief Executive Officer

Executive Board

Dietmar Heinrich	Bruce Warmbold	Dr. Yilin Zhang	Andreas Schick	Prof. Dr.-Ing. Peter Gutzmer	Dr. Stefan Spindler
Regional CEO Europe	Regional CEO Americas	Regional CEO Greater China	Regional CEO Asia/Pacific	Chief Technology Officer and Deputy CEO	CEO Industrial

Klaus Rosenfeld
Chief Executive Officer

Corinna Schittenhelm
Chief Human Resources Officer

Matthias Zink
CEO Automotive

Dr. Ulrich Hauck
Chief Financial Officer

Oliver Jung
Chief Operating Officer

Prof. Dr. Peter Pleus
CEO Automotive

Our strategy "Mobility for tomorrow"

"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." This is the vision of the Schaeffler Group. To live up to this claim, Schaeffler adopted its strategy "Mobility for tomorrow" in 2016. Based on long-term trends, it defines 4 focus areas and 8 strategic pillars for continued profitable growth, as well as 16 initiatives for implementation. Digitalization is a significant megatrend and consequentially an important future opportunity for Schaeffler. This is to be accordingly leveraged by means of the "Digital Agenda" initiative.

Our world is in motion at a pace that is gathering speed. Climate change is progressing, and urbanization, globalization, and digitalization are on the rise. These factors will impact and alter the way we live and work in the future. That applies in particular to the area of mobility and goes well beyond our cars to other forms of transportation, both in cities and in the spaces between them. Schaeffler is determined to play an active role in shaping these changes.

With its strategy “Mobility for tomorrow”, finalized during the course of the year 2016 following in-depth consultations with executives and the Supervisory Board and adopted in November, Schaeffler has set the course for sustainable profitable growth.

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 customers and business partners, top-level expertise in manufacturing technology, and advanced systems know-how. The Schaeffler Group’s vision and mission complement and amplify one another, with the vision encompassing the goals and aspirations that guide the company’s course of action.

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.”

4 Focus areas

The 21st century world is changing at an unprecedented pace. Rising demands for environmental protection have led to the transformation of energy systems. Urbanization is progressing rapidly, and globalization and digitalization connect the entire world, both physically and in virtual space. Based on these long-term trends, automotive and industrial supplier Schaeffler has defined 4 focus areas as part of its strategy "Mobility for tomorrow" on which the company intends to concentrate in the future.

Eco-friendly drives

Whether in cars, heavy-duty trucks, or production machines: Maximum energy efficiency and the lowest possible emission values are required wherever mechanical movement is generated. Schaeffler develops and produces components and systems for optimized internal combustion engines, as well as for hybrid and electric drives.

Urban mobility

Nowhere is the shift in mobility as noticeable as it is in megacities across the globe. New mobility concepts, based on the intelligent combination of individual vehicles with public transportation services are rapidly gaining acceptance. Schaeffler is on board, from micro-mobiles all the way to subway trains.

Interurban mobility

In a networked world, mobility between large conurbations plays an especially important role. Increasing rail and air transportation requires innovative technological solutions – just as modern agriculture does. Schaeffler offers adapted solutions for all these sectors.

Energy chain

Climate protection can only be achieved if the entire energy chain from generation to transport to use is continuously optimized. As a partner of the energy industry, Schaeffler supports the expansion of renewable energy generation, focusing particularly on wind power, but also on hydropower and solar energy.

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

In order to achieve profitable growth in all focus areas, Schaeffler has determined 8 strategic pillars that define the scope for future entrepreneurial action (see graphic above). On one hand, these pillars define the company's self-understanding as a global technology partner of the automotive sector and industry, that delivers both components and systems. On the other hand, they specify the prerequisites as well as the values by which Schaeffler lives.

Schaeffler views E-Mobility, Industry 4.0, and Digitalization as key opportunities for the future. These areas offer vast potential for change. For example, Schaeffler estimates that in 2030 more than every other new car will be equipped with electric drives (hybrid vehicles included). Industrial 4.0 has a similar significance for the industrial business: Machines and production plants will communicate largely without human intervention in the coming decade. Digitalization changes not only products and production processes in both divisions, but also all processes from development all the way to utilization by the customer. The convergence of the real and digital worlds enables new business models and a sustained increase in added value.

16 Strategic initiatives

Each strategy is only as good as the results that come of it. In developing its strategy, the company intensively addressed the question of how to implement it as efficiently and consistently as possible. Based on the positive experience, the Schaeffler Group gained with its first transformation program, "One Schaeffler", which was successfully implemented by the end of 2015, the company has developed a tailor-made excellence program that summarizes the most important strategic initiatives and places them in five categories. Fittingly, the Schaeffler Group calls this excellence program "Agenda 4 plus One".

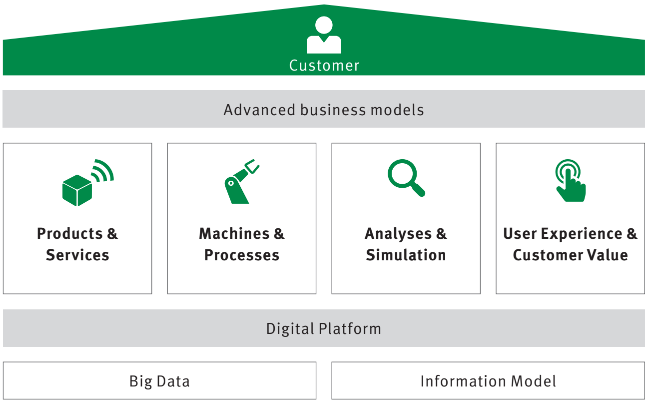
"Agenda 4 plus One" includes the following 5 categories: Customer focus, Operational excellence, Financial flexibility, Leadership and talent management, and – as "plus One" – Securing long-term competitiveness and value creation. "Agenda 4 plus One" comprises 16 strategic initiatives that are of utmost importance worldwide. The declared goal is to successfully implement all initiatives by the end of 2020. The "Digital Agenda" plays a central role in this context.

Our “Digital Agenda”

These days, the value of a car or machine is less and less determined by hardware and software alone. Digital services, based on networked operating data, complement the classic business models in the automotive and mechanical engineering sectors. As a supplier to these industries, Schaeffler not only reacts to this trend, but also thinks ahead, as evidenced by its “Digital Agenda” adopted last year, which is an integral part of the “Agenda 4 plus One”. Thus, the company plays an active role in shaping the future.

Cars alert each other to hazards. Wind turbines schedule necessary maintenance outside of windy seasons. Machine tools determine the order in which workpieces are processed so that the tools don't have to be changed as frequently. The Internet of Things is making massive inroads into the world of technology. It enables new data-driven business models. With its "Digital Agenda", Schaeffler is specifically expanding those pillars on which these business models are based:

Digital Agenda of the Schaeffler Group



Products & Services: Data don't simply appear, they must be generated. Whether city vehicles, high-speed trains, or wind turbines, Schaeffler's mechatronic products are already in place wherever something moves. Fitted with sensors, electronics and actuators, bearings, and other drive components, they provide the information required for big data analysis and business models based on networking.

Machines & Processes: The digital networking of production facilities along the entire value chain is one of the most important goals of Industry 4.0. Schaeffler sees itself not only as a supplier for smart factories, but also implements new technologies at an early stage in its own volume production. The goal of being able to respond more quickly and flexibly to current developments in a rapidly changing world is a key motivation for Schaeffler to digitize its processes in all corporate areas. In the future, the company will therefore digitally map the entire product life cycle, from the initial idea to a new product, and from digital production planning to sales management.

Analyses & Simulation: Knowing at the development stage under exactly which conditions a product will later be used – that's what every engineer dreams of. Schaeffler is significantly increasing its competitiveness by leveraging real operating data to test innovations before the first prototype is even built, and making such data available throughout the product's lifecycle.

User Experience & Customer Value: Acceptance of digital services on the part of customers and employees depends not only on the quality of data provided, but also on user-friendly operator interfaces. Smartphones and tablet PCs are becoming more and more important in professional applications. Schaeffler is working to expand its expertise in the optimal design of man-machine interaction.

Schaeffler laid the essential foundations in 2016 to ensure that these strategic pillars can be developed in such a way that they enable real growth in the future. On one hand, this required the development of a digital platform that provides the basis for big data analyses as the central data hub. Our partnership with IBM goes even beyond this. Schaeffler and IBM are working together to apply innovative methods, such as artificial intelligence, to our products and processes. On the other hand, in a digitally networked world, Schaeffler is more dependent than ever on the creativity of individuals. With a host of exciting tasks available in an industrial environment, Schaeffler ranks high as an attractive employer for digital talents.

The "Digital Agenda" is a Group-wide initiative that is supported by the Executive Board and will continue to be vigorously advanced at Schaeffler in 2017. After all, the best thing a company can do in times of change is to actively drive it forward – just as the Schaeffler employees portrayed on the following pages do in their day-to-day work.

We combine steel with digital expertise.

The rolling bearing of the future works as a sensor. In this way, Schaeffler creates the prerequisite for higher productivity, whether in production, energy generation, or rail transport. In the digital age, Schaeffler's mechatronics expertise is in greater demand than ever before.

Dr. Joanna Procelewska studied both chemistry and computer science. The surface technology specialist works on laying the foundation for intelligent products.

1.
Hand in Hand: Physical testing improves the forecast accuracy of simulations.
2.
Small structures, big impact: Sensotect® bottom bracket bearings with nano-functional layer.

1.

20

Number of nanotechnology coating variants developed by Schaeffler's Surface Technology Competence Center.

"Could I borrow your pen for a moment, please?" Dr. Joanna Procelewska wants to draw a sketch to help her explain how her virtual tribo-lab works. Apparently, she does not always have such analog tools ready at hand. The surface technology specialist studied both chemistry and computer science. Now she is advancing digitalization in her area. "Combining my domain knowledge in my area of expertise with digital technologies for data exploration has always fascinated me," she says. Her domain is tribology – the science of friction.

When it comes to designing coating systems for Schaeffler products, such as rolling bearings, bucket tappets and finger followers, the virtual tribo-lab developed by Dr. Procelewska is set to become an important tool. At its core element is an interactive tribological database for coatings, which holds experimental data on layer systems and characteristic values derived from preliminary tribological tests with coated components. Based on these data, the friction and wear properties of coated components can be precisely predicted using data mining methods. This will significantly increase the success rate during the development process, as well as the quality of real-life tests – consequently, Schaeffler engineers will be able to develop new coating systems much faster and more efficiently in the future.

This fundamental work not only allows the production of components with lower friction levels, but also the development of completely new intelligent layers. One such example is the Schaeffler Sensotect® coating system, with which mechanical components can be turned into sensors. A very thin, electrically conductive layer is applied, for example to a rolling bearing. During operation, tiny deformations occur in this sensor layer which give rise to electrical signals. Important information – such as load and torque conditions – can be derived from these.

The great advantage of Sensotect® is that the sensor system does not require a larger design envelope. However, Schaeffler is also developing retrofit solutions for existing systems, such as the FAG SmartQB early warning system. This detects the vibration data of machines and observes changes in the vibration patterns. Based on that, it automatically assigns defect causes and issues recommendations for action via a display. Measuring the vibration patterns is relatively easy with the help of an externally applied sensor system, as the vibrations are transmitted from the machine interior to its outside via structure-borne sound.

More and more often, Schaeffler components are becoming sensors in their own right, which is creating the prerequisite for the company's range of digital services. But the offer extends much further, as is shown, for instance, by the "Drivetrain 4.0" that Schaeffler presented at the 2016 Hannover Messe for the first time. The system approach also encompasses intelligent on-site electronics and the Schaeffler Cloud, which enables automated data analysis. The remaining operating life of gearbox bearings in production machines can thus be calculated individually for each bearing, for example. This in turn allows predictive maintenance to be carried out without downtimes, and operation to be adapted to the specific machine status. Schaeffler is pursuing further similar concepts with its "Rail 4.0" and "Wind 4.0" for the railway and wind power sectors. What is common to all of these concepts is that knowing precisely what happens inside a machine is indispensable for correctly interpreting the derived data. So in the digital age, Schaeffler's application expertise is in even greater demand than ever before.

»Combining my domain knowledge in my area of expertise with digital technologies for data exploration has always fascinated me.«

2.

Machines & Processes

We plan and control our plants digitally.

The digital transformation is in full swing at the Schaeffler plants. Innovative digital tools and intelligent data usage are being deployed to increase productivity, from planning new production facilities or entire factories to effecting modifications during ongoing operation.

Working on concrete applications is important to computer scientist **Dr. Dennis Arnhold**. He uses his knowledge to implement new production planning methods at Schaeffler.

1.

1.
To see is to understand: Realistic simulations of new plants improve decision-making quality.
2.
Testing on the shop floor: The Machine Tool 4.0 proves itself under real production conditions.
3.
X-ray view: The goings-on in the machine tool of the future can also be seen on a tablet PC.

A plain office in Herzogenaurach. Dennis Arnhold opens his laptop. It takes just a few mouse clicks and he is right in the middle of a factory located in Kysucké Nové Mesto, a small Slovakian town near the Polish border. Here Schaeffler recently expanded its wheel bearings manufacturing capacities in an existing plant. "This is a digital twin of the complete production line," explains Arnhold, zooming in on the 3D view. All the details that make up a factory can be seen; not only the machines, but every single lamp and even the logistics containers that are used in component supply – with the quality of animation similar to a modern computer game. But for Arnhold, this "3D Experience Platform" is anything but a leisure pastime. It serves for the planning of new production lines or even entire factories.

Being able to plan in three dimensions offers great advantages, from the expert's point of view: "We can, for example, design workstations with optimum ergonomic comfort even in advance." Arnhold is particularly proud of the floor space that has been saved: Compared to an older production line with a comparable output in the Schaeffler network, the required space is 40 percent less at the Kysucké factory. What works with a traditional product, such as the wheel bearing, is of even greater importance when it comes to innovative systems: Where complex assembly lines are planned for the first time – such as for electrified drive systems, for example, the virtual systems enable product and process developers to discuss and determine the optimal production layout in advance.

Factory planning in a virtual environment is only one aspect of the digital transformation that is currently going on in the Schaeffler workshops. One example is in Höchstadt where the Machine Tool 4.0 was put into operation in cooperation with DMG MORI at the end of 2015. Integrated into the regular production process, the machine continuously transmits over 170 signals. “We have already achieved initial success,” says Ronny Hüttner, Digitalization Project Manager at Höchstadt. Frequent retooling is a special challenge at this plant, which specializes in the small-batch manufacture of high-precision bearings. Thanks to the digital order control system, setup times have been reduced by up to 25 percent, since changing over to a new product no longer means that all the tools have to be removed: Now the machine knows which tools can be used for the next job as well. Currently, Hüttner is working on interlinking the Machine Tool 4.0 with a further lathe center, a grinding machine and a robot used for the feeding of workpieces. “As a next step, we’re converting a networked machine into a networked production island,” explains Hüttner.

»We can design ergonomic workstations even during the early planning stages.«

Specialists at Höchstadt are also working on how to ensure the meaningful use of the obtained data. In the future, it will for instance be possible to issue an “energy certificate” for every component. As the energy requirements of different workpieces vary considerably, the goal is to achieve more targeted purchasing of electric power. Moreover, in the event of technical breakdown, machines should automatically be able to report the failure cause to the higher-level manufacturing execution system. Once this is working throughout the Group, the obtained information could be used to purchase or develop machines in a more target-oriented manner. And ultimately, it should be possible even during the manufacturing process to predict whether the quality of the components meets all requirements and to adjust the machining process accordingly, if necessary.

Hüttner and Arnhold have a simple common goal: perfection. Errors and defects, whether during planning or ongoing processes, should only happen in a digital environment in the future.

25

Percent reduction in setup time resulting from digital order management alone

2.

3.

Analyses & Simulation

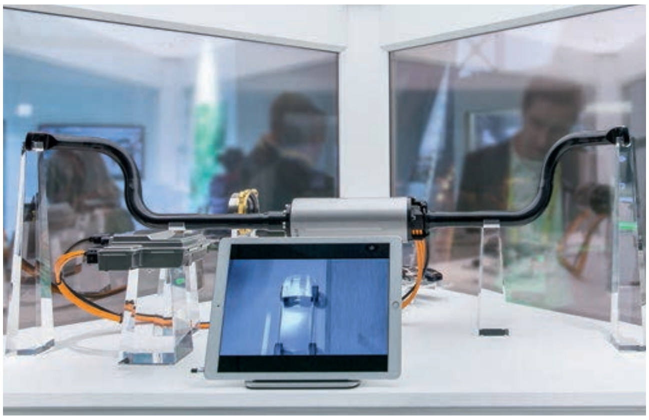
Ideas abound for the Internet of Things. We ensure that it becomes a reality.

Schaeffler is creating the technical prerequisites for digital transformation through its partnership with IBM and the further development of its IT infrastructure. Powerful algorithms sift through the wealth of data from industrial applications within a matter of seconds, learning systems with artificial intelligence will complement human expertise in the future.

Dr. Pankaj Joshi has been working for Schaeffler as a data analyst since mid-2016. The photonics specialist contributes his expertise to support the development of new services and business models.

1.
Premiere: Schaeffler took part in the Consumer Electronics Show in Las Vegas for the first time in January 2017.
2.
New findings: Dialog with application experts is of crucial importance for big data specialists.

1.



600

Number of digitalization and IT specialists Schaeffler plans to hire in the coming years.

2.

Delhi, Stockholm, Ghent. And now Herzogenaurach. It was no coincidence that Pankaj Joshi, who holds a doctorate in photonics engineering, decided in favor of Schaeffler in mid-2016. The data analysis expert was specifically looking for an employer for which he could use his knowledge to make a difference. "Schaeffler holds a huge treasure: countless data, both from applications in the industrial business and from its own production," says Joshi. Unearthing this treasure, however, is laborious work. For example, Schaeffler has been active in the area of "Condition Monitoring" for many years now. The data obtained in the past – such as that from the monitoring of wind turbines – are to be used to establish correlations between the operating conditions, maintenance intensity, and the key components supplied by Schaeffler. "To

achieve this, we need not only consistent data, but must also ask the right questions," explains Joshi. "That is why I work very closely with the wind power specialists from Schaeffler Industrial."

Powerful algorithms that scan billions of sets of data in a matter of seconds are to be made available to answer these questions. In the fall of 2016, Schaeffler entered into a strategic partnership with IBM to build the necessary know-how. This involves much more than just utilizing the digital platform that will henceforth be used as Schaeffler's central data hub. Schaeffler and IBM will also collaborate on advancing the development of networked solutions and technologies for the analysis of industrial data. In the future, learning computer systems with artificial intelligence are to complement human expertise in many areas – for example, when it comes to optimized energy consumption or logistics at Schaeffler plants.

To be prepared for the challenges of the future, Schaeffler continues to forge ahead with the development of its IT solutions, complementing its portfolio where appropriate for digital transformation. The customer-friendly display of data evaluations is of great importance in this context, such as when it comes to setting up a new service platform for Schaeffler. This will primarily be used to offer condition monitoring services. "In the past, our experts prepared the data for the customer. Now it is crucial to automate data evaluation and make it available to the user online in an easily comprehensible form," explains Jürgen Wernsdörfer, one of two project managers responsible for Schaeffler's digital platform. His colleague, Christof Heurung, adds: "Moreover, it is imperative for the applications to run reliably and securely on various mobile devices and be usable everywhere, not just in the Schaeffler network." And in fact, there are now already plants where maintenance specialists are able to access relevant SAP data via their smartphones, for example.

»At Schaeffler it is possible to apply IT knowledge to the real, physical world. «

From data analysts to IT specialists for mobile computing, Schaeffler is increasingly creating jobs for digitalization experts. "We will be recruiting on a massive scale in this field in the coming years," explains Ingo Krauß, the responsible HR Manager at Schaeffler. Many applicants join the company directly after obtaining their university doctorates, while others come from small start-ups or even from the digital labs of DAX companies. "We have exciting tasks and challenges to offer," says Krauß. "At Schaeffler, these people can apply their IT knowledge to the real, physical world." Nevertheless, Schaeffler is not only focusing on the recruitment of external specialists, but also aims to intensify its own training and further education opportunities. To illustrate this, in mid-2017 a new trainee program will be launched that explicitly focuses on digitalization. For whether in Delhi or Herzogenaurach, digitalization expertise will be indispensable for the working world of the future.

User Experience & Customer Value

We see what happens before it happens.

The trend toward digitalization has spread to all sectors in which Schaeffler operates, from the automotive industry to the energy sector. It is anticipated that data collection and evaluation in real-time will lead to increased productivity. Even today, Schaeffler offers digital services such as the online monitoring of wind turbines – a business model that is to be significantly expanded in the future.

Graduate electronics engineer **Harald Reiners** has headed Schaeffler's condition monitoring services for the past ten years. Using a new service platform, he has machinery and equipment continuously under control even when he is out of the office.

Harald Reiners, based at the condition monitoring center in Herzogenrath, brings up data from one particular wind turbine. "This one here was fitted with a new gearbox several weeks ago," he explains. "Our sensors provide an accurate picture of the vibration behavior of such plants. Using automated parameters, we can check whether they are running smoothly." The graduate electronics engineer has headed Schaeffler's condition monitoring services for the past ten years. Along with his team consisting of about a dozen experts, he continuously monitors around 1,000 machines, including wind turbines, steel rolling mills, paper machines, and marine drives. "We want to provide peace of mind for our customers and free them of concerns regarding their machines so they can attend to their real business," emphasizes Reiners. "If problems crop up, we give the operators concrete recommendations on what needs to be done." In addition to performing digital analyses in the online monitoring center, the technicians carry out on-site inspections at regular intervals.

1,000

Number of wind turbines, cold rolling mills, paper mills, and marine drives that are already included in the Schaeffler condition monitoring network today.

All sectors are now affected by the trend toward digitalization; digital services are becoming an important addition to the actual

1.

2.

1.
Guaranteed to pay off: Proactive condition monitoring helps to achieve longer maintenance intervals and better operating performance for rail vehicles.
2.
Analysis competence: The Schaeffler experts understand what really happens inside a machine.

product. They can also form the basis for completely new applications. An example in the automotive sector is the further development of the active mechatronic roll control. This particularly efficient electric actuator, which is in volume production at Schaeffler, compensates for the rolling motion of the vehicle. The next generation of this intelligent system will have the potential to also act as a sensor which will capture data on the condition of the road. If combined with an accurate positioning system, it would be possible to produce detailed road maps in real-time, which could be accessed via the Cloud and alert the infrastructure operator, as well as vehicles following behind, to hazards such as potholes or bumps.

Digital solutions can also be of considerable added value to operators and manufacturers of rail vehicles. Accordingly, Schaeffler is developing mechatronic systems used in the railway sector for monitoring and predictive maintenance of axlebox bearings and drive motors. These are equipped with sensors that measure temperatures, vibrations and speeds. An intelligent processor unit processes the raw data which are then merged with further data in the Cloud where they are evaluated and made available as service data. The results are made available to the customer in a clearly structured overview. The concept developed by the Schaeffler engineering specialists meets current European legal requirements for hot box detection used in high-speed trains. Thanks to proactive condition monitoring, it also allows for extended maintenance intervals and therefore longer operating times. In China, Schaeffler is undertaking the development of an axlebox monitoring system specifically for high-speed trains. Top speeds of up to 500 km/h place the highest demands on drive technology. Schaeffler is developing solutions as part of a strategic partnership with the leading Southwest Jiaotong University.

This principle also applies to the online monitoring center in Herzogenrath. "Depending on the application, we agree on certain service levels including regular status reports and response times with our customers," says Reiners. In addition, he and his colleagues prepare concrete recommendations for action as soon as the measurement systems indicate critical anomalies. Sometimes all that is required is the addition of more lubricant, while in other cases components have to be replaced. Another digital service slotted to be available in the future will be the calculation of residual operating times for rolling bearings. This service can be used by operators to schedule maintenance based on the seasons, for example, and utilize less profitable months to replace parts pinpointed by the system.

»We want to provide peace of mind for our customers and free them of concerns regarding their machines so they can attend to their real business.«

Schaeffler on the capital markets

1.1 Events 2016

Following Schaeffler AG's listing on October 09, 2015, in which an initial 11 % of share capital were placed, Schaeffler AG has expanded and bolstered its presence on the capital markets with several transactions and measures.

Free float increased to 25 %

On April 05, 2016, IHO Beteiligungs GmbH (until September 28, 2016: Schaeffler Verwaltungs GmbH) placed 94.4 million common non-voting Schaeffler AG shares in an accelerated bookbuild. Since this transaction was completed, 166 million common non-voting shares representing 100 % common non-voting share capital are widely held. The free float amounts to approximately 25 % of Schaeffler AG's total common and common non-voting share capital.

First annual general meeting passes resolution on special dividend

Schaeffler AG's first annual general meeting since the listing, which was held on April 22, 2016, passed a resolution to pay a dividend of EUR 0.34 per common share and EUR 0.35 per common non-voting share to Schaeffler AG's shareholders for 2015. This represents a dividend of 28.9 % of net income attributable to shareholders before special items. In addition, the company paid a special dividend of EUR 0.15 per common share and per common non-voting share for 2015.

Advanced to MDAX

Deutsche Börse included Schaeffler AG in its MDAX index effective June 20, 2016. Thus, the Schaeffler shares meet not only the high transparency requirements of the Prime Standard, but also the size criteria regarding market capitalization and liquidity that are relevant for inclusion in this index.

Schaeffler AG's first capital markets day

At its first capital markets day since its successful listing in October 2015, which was held on July 20, 2016, Schaeffler AG presented its plans for growth and its financial ambitions for the coming years. The group stated that it plans to grow its revenue – excluding the impact of currency translation and external growth – by an average of 4 to 6 % per year by 2020. The targeted EBIT margin of 12 to 13 % before special items is aimed at maintaining the company's high earnings quality. On this basis, the Schaeffler Group intends to achieve free cash flow of approximately EUR 900 m in 2020.

Debt reduced significantly and investment grade rating obtained

In connection with the successful refinancing transaction completed at the level of IHO Holding, a group of holding companies owned indirectly by the Schaeffler family, rating agency Moody's upgraded Schaeffler AG's company rating to Baa3 (investment grade) on September 07, 2016. Schaeffler AG received approximately EUR 1.7 bn when its loan receivable from IHO Holding was prepaid in connection with the refinancing transaction. As a result, Schaeffler AG has achieved its objective of reducing its debt to EBITDA ratio (net debt in relation to EBITDA before special items) to less than 1.5x by 2018 two years ahead of schedule.

Advanced to STOXX Europe 600

STOXX Ltd., a subsidiary of Deutsche Börse AG, has included Schaeffler AG in its STOXX Europe 600 index. As a result, Schaeffler AG has also become part of the European STOXX Europe 600 Automobiles & Parts sector index. These changes became effective as of the start of trading on September 19, 2016.

Capital structure improved further

Having optimized its bank debt in July and August 2016 and fully redeemed a bond issue with a principal of EUR 600 m, a coupon of 4.25 %, and an original maturity of 2018, Schaeffler AG redeemed three further bond series in full in October 2016. On October 07, 2016, Schaeffler AG initially redeemed one 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 then redeemed another two 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. The redemption was funded using the proceeds of the repayment of the loan receivable from IHO Holding referred to above.

Strategy "Mobility for tomorrow" and Financial Ambitions 2020

On November 09, 2016, Schaeffler AG presented its strategy "Mobility for tomorrow" to the public; the strategy was developed over the course of 2016 and was approved by the Board of Managing Directors and the Supervisory Board. The presentation of the strategy also included Schaeffler AG's first set of multi-year targets, known as Financial Ambitions 2020. Based on the operating targets approved back in the summer – average revenue growth excluding the impact of currency translation and external growth of 4 to 6 % p.a., an EBIT margin of 12 to 13 % before special items, and free cash flow excluding external growth of approximately EUR 900 m in 2020 – Schaeffler AG aims to generate earnings per share of EUR 2.00 in 2020. The deleveraging target achieved ahead of schedule has been replaced with a gearing ratio (net debt to equity) to be improved to below 75 % by 2020. In addition, Schaeffler AG intends to pay out dividends amounting to 30 to 40 % of net income to its shareholders in the future (previously 25 to 35 %).

Business portfolio adjusted

On November 21, 2016, Schaeffler Schweiz GmbH in Romanshorn, a wholly-owned subsidiary of Schaeffler AG, sold its fine blanking activities to owner-operated Swiss Güntensperger Group. The fine blanking activities generated revenue of approximately CHF 50 m last year. This strategic decision was made to focus the Schaeffler Group on its core areas of expertise.

On December 20, 2016, Schaeffler entered into a purchase agreement with SEMIKRON International GmbH to acquire 51 % of the shares in Compact Dynamics GmbH, a manufacturer of high-performance electric motors. At the same time, Schaeffler and SEMIKRON agreed to cooperate on developing power electronics systems and integrating power electronics components. The acquisition and collaboration expand Schaeffler's expertise in the field of electric motors and power electronics for developing and manufacturing electric drives.

On December 22, 2016, Schaeffler sold its cylinder head manufacturer Schaeffler Motorenelemente AG & Co. KG in Magdeburg to the Weber Group. The company specializes in the mechanical processing of cylinder heads and other complex housings for the automotive industry, which are not an integral part of the Schaeffler Group's core business. The company generated approximately EUR 42 m in revenue in 2015. The transaction enabled Schaeffler to free up resources in order to invest in the key future-oriented fields that are part of its strategy "Mobility for tomorrow".

Analyst coverage expanded

The company's coverage by analysts expanded significantly in 2016. While only five analysts were regularly publishing updates on the company in company-specific research reports or more in-depth industry research reports, this number had risen to 13 by year-end. As two more analysts began tracking the company in early 2017, the company was covered by analysts representing a total of 15 banks as at February 20, 2017. Eight of these banks issued a recommendation of either buy or overweight on Schaeffler AG's common non-voting shares. Their average upside target was EUR 15.57.

1.2 Capital market trends

In early 2016, the global capital markets were characterized by sluggish economic data from China and an oil price that continued to drop. The referendum in the United Kingdom on remaining in the EU and the election campaign in the U.S. also contributed to the turbulence in the capital markets during the year. In addition, the Fed raised its benchmark interest rate for the first time in a year. As a result, exchange rates remained volatile. The oil price rose considerably over the course of the year, driven by the decisions of the OPEC countries to curtail production volumes.

As global equities markets rallied significantly during the last quarter, they showed a positive trend overall in 2016. While the Euro STOXX 50 was up slightly by 0.7 %, the Dow Jones Industrial gained 13.4 % on the back of the robust economy in the U.S., rising to a new all-time high. The Nikkei 225 also rose slightly by 0.4 %.

The Deutsche Aktienindex (DAX) was up 6.9 % in 2016. The first quarter was marked by high volatility, driving the DAX to a low of 8,753 points in early February. The main reason was a further decline in the oil price, triggered by concerns about the Chinese economy and its potential impact on the global economy. The equities markets began to recover around the middle of the first quarter; nevertheless, the DAX was initially unable to sustain a level above 10,000 points.

During the second quarter of 2016, the German leading share index recovered to 10,436 points by April 21, the high for the first half of the year. However, the DAX slumped again following the British Brexit referendum, reaching another low of 9,269 points on June 27, 2016 from which it only recovered to a minimal degree by the end of the second quarter.

In early July 2016, the DAX started to make a rapid comeback and reached 10,753 points on September 07. Better than expected economic data, particularly from Germany and the U.S., had a calming effect on prices. Based on this, the DAX settled at a closing level of 10,511 points on September 30.

The equities markets continued to recover during the fourth quarter of 2016; the DAX reached its year-to-date closing high of 10,761 points on October 24, 2016. Overall, the impact of the U.S. election on November 08, 2016 on the global equities markets was considerably better than expected. For instance, the DAX, the leading share index, dropped to 10,259 in the run-up to the election only to rise to its annual high of 11,481 in a fulminant rally after the election, closing out the year at this level.

The MDAX increased by 6.8 % in 2016, while the European sector index, the STOXX Europe 600 Automobiles & Parts, lost 3.9 % as the automotive sector is very sensitive to the economy and due to the debate on E-mobility.

The corporate bond market was flat overall in 2016. The iTraxx CrossOver (5 year maturity), an indicator of credit risk in the European high yield market, closed at 288 basis points on December 31, 2016 compared to 314 basis points on December 31, 2015. The lowest premium was charged in December 2016 (284 basis points), when the DAX was also at its all-time high and demand for risky assets was particularly strong. The highest premium, on the other hand, was charged in mid-February (487 basis points), paralleling the negative trend of the DAX. The iTraxx Europe (5 year maturity), an indicator of credit risk in the European investment grade market, was also marked by volatility during the year. Having reached a high of 126 basis points in mid-February and a low of 65 basis points in early September, it closed at 72 basis points on December 31, 2016 (December 31, 2015: 77 basis points), approximately returning to its level at the beginning of the year.

1.3 Schaeffler shares

Schaeffler AG's common non-voting shares were listed on the stock exchange on October 09, 2015. A total of 166 million common non-voting shares are listed for trading. All common non-voting shares have been widely held by national and international investors since April 05, 2016.

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 (until September 27, 2016: Schaeffler Verwaltung Zwei GmbH) that are not listed on the stock exchange. 166 million common non-voting bearer shares are widely held. Thus, the free float amounts to approximately 24.9 % of Schaeffler AG's total common and common non-voting share capital.

Schaeffler AG intends to pay a dividend of 30 to 40 % of consolidated net income before special items to its shareholders in the future. 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.

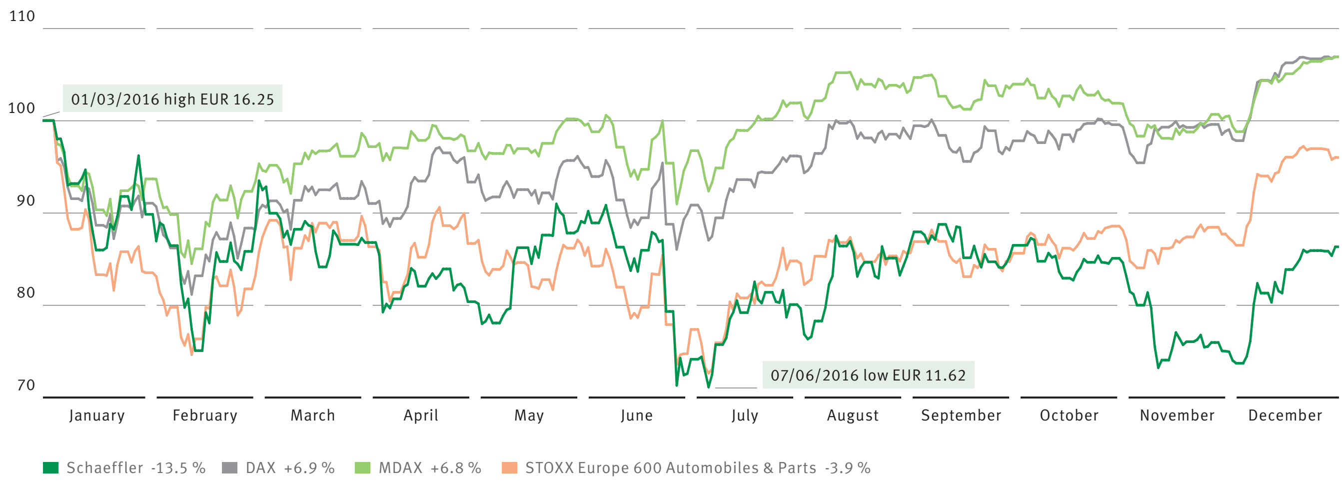
The Board of Managing Directors and the Supervisory Board will propose a dividend for 2016 of EUR 0.49 per common share and EUR 0.50 per common non-voting share to the annual general meeting. This represents a dividend of 34.1 % of net income attributable to shareholders before special items.

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, 2016	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 share price trend 2016
in percent (12/31/2015 = 100)



Source: Bloomberg.

Performance of Schaeffler shares

Schaeffler shares dropped approximately 14 % in 2016, a weaker performance than that of the benchmark indexes, the MDAX and the STOXX Europe 600 Automobiles & Parts. The primary reason was that share prices of automotive suppliers with a large proportion of products for internal combustion engines suffered as a result of the extensive debate on E-mobility.

On March 31, 2016, the common non-voting shares of Schaeffler AG were quoted at EUR 14.13, 13.0 % less than on December 31, 2015. This trend was approximately in line with that of the european STOXX Europe 600 Automobiles & Parts sector index which came under significant pressure as a result of the drop in the oil price and the sluggish economic data from China (-11.2 % compared to December 31, 2015). The share price reached its high on January 05 (EUR 15.94) and its low on February 12 (EUR 12.25).

On June 30, 2016, the common non-voting shares of Schaeffler AG were quoted at EUR 11.85, 16.1 % less than on March 31, 2016. Schaeffler shares did not escape the once more below-average trend in the STOXX Europe 600 Automobiles & Parts compared to the DAX and the MDAX (-15.5 % compared to March 31, 2016). The dire mood in the capital markets was due in particular to the British Brexit referendum, which led capital market participants to expect the economy to weaken. The Schaeffler share price reached its high on May 24, 2016 (EUR 14.80) and its low on June 27, 2016 (EUR 11.65).

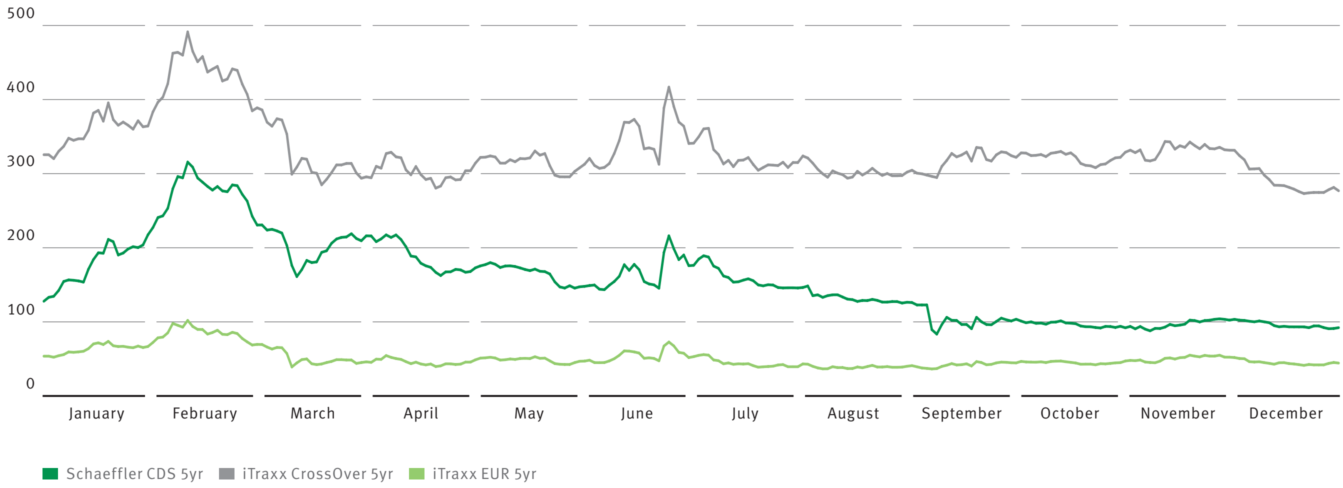
On September 30, 2016, the common non-voting shares of Schaeffler AG were quoted at EUR 14.08, 18.8 % higher than on June 30, 2016. Thus, Schaeffler shares fared somewhat better than the STOXX Europe 600 Automobiles & Parts (+14.3 %) and considerably better than the DAX and the MDAX (+8.6 %/+8.8 %, all compared to June 30, 2016). The recovery in the third quarter was mainly driven by the improving general capital market sentiment and the weak performance of the automotive supply sector in the previous quarters. The share price reached its high on September 09, 2016 (EUR 14.45) and its low on July 06, 2016 (EUR 11.62).

Schaeffler share performance

in €	2016	2015
Share price at year-end	14.06	16.25
Share price (high)	16.25	17.05
Share price (low)	11.62	11.92
Average number of shares		
• Common shares	500,000,000	500,000,000
• Common non-voting shares	166,000,000	115,912,329
Earnings per share [1]		
• Common shares	1.29	0.88
• Common non-voting shares	1.30	1.28
Proposed dividend per share		
• Common shares	0.49	0.34
• Common non-voting shares	0.50	0.35
Proposed special dividend per share		
• Common share and common non-voting shares	-	0.15

[1] Earnings per share were calculated in accordance with IAS 33.

Credit default swap (CDS) price trend 2016
in percent



Source: Bloomberg.

On December 31, 2016, the common non-voting shares of Schaeffler AG were quoted at EUR 14.06, approximately in line with its September 30 level, lagging considerably behind automotive sector equities in the last quarter (+12.0 % compared to September 30). Especially the capital markets' overly high expectations with respect to the quarterly report published on November 09 played a role here, as did the particularly extensive uncertainty in the capital markets regarding future changes within the automotive sector toward electric mobility. The share price reached its high on October 05, 2016 (EUR 14.21) and its low on November 10, 2016 (EUR 11.95).

On December 31, 2016, Schaeffler AG's shares were up 6.9 % from their closing price on October 09, 2015 (EUR 13.15), Schaeffler's first day of trading, performing slightly better than the relevant benchmark index, the STOXX Europe 600 Automobiles & Parts (+5.7 %).

1.4 Schaeffler bonds and rating

The Schaeffler Group took advantage of the favorable financing environment in 2016 to enter into a new EUR 2.3 bn Facilities Agreement. The Facilities Agreement was signed in 2016 and consists of a EUR 1.0 bn term loan and a EUR 1.3 bn revolving credit facility. The funds were used to repay the two institutional term loans of EUR 165 m and USD 280 m, and to fully redeem a bond series with a principal of EUR 600 m. In October, the company redeemed another two EUR bond series with a principal of EUR 500 m each as well as one USD bond series with a principal of USD 850 m. The funds for these redemptions were largely obtained from IHO Holding as prepayment in full of a loan receivable of approximately EUR 1.7 bn.

Schaeffler bonds – overview

As a result of the above transactions, the Schaeffler Group had five series of bonds outstanding as at December 31, 2016, three of them denominated in EUR and two in USD. All of the bonds were issued by Schaeffler Finance B.V., Barneveld, Netherlands.

The Schaeffler Group had the following bonds outstanding at December 31, 2016:

Schaeffler Group bonds

ISIN	Currency	Face value in millions	Coupon	Maturity	Price in % [1] 12/31/2016	Price in % [1] 12/31/2015
XS1212469966	EUR	400	2.50 %	05/15/2020	102.30	100.98
US806261AJ29	USD	700	4.25 %	05/15/2021	102.44	99.94
XS1067864022	EUR	500	3.50 %	05/15/2022	102.96	102.35
US806261AM57	USD	600	4.75 %	05/15/2023	101.75	98.94
XS1212470972	EUR	600	3.25 %	05/15/2025	106.72	97.52

[1] Source: Bloomberg.

Performance of Schaeffler bonds

Bond prices largely experienced considerable upward trends in 2016. All five bond series' prices increased slightly, reducing the effective yield. The encouraging price trend was due not only to the general market trend, but also to further improvements in Schaeffler AG's capital structure and the rating upgrades by rating agencies Standard & Poor's and Moody's. Premiums for Schaeffler AG 5-year credit default swaps decreased from 150 basis points at December 31, 2015 to 117 basis points as at December 31, 2016, outperforming the benchmark indexes iTraxx CrossOver and iTraxx Europe.

Schaeffler's rating

Rating agency Standard & Poor's upgraded the Schaeffler AG company rating to BB with a stable outlook on April 28, 2016. The rating for the secured bonds was raised to BB and the rating for the unsecured bonds to B+ at the same time.

On July 20, 2016, rating agency Moody's upgraded the unsecured bond rating to Ba3.

On September 07, 2016, rating agency Moody's upgraded Schaeffler AG's company rating to Baa3 (investment grade) with a stable outlook. At the same time, Moody's upgraded the issuance ratings of Schaeffler Finance B.V., Barneveld, Netherlands, from Ba2 to Baa3 for secured bonds and from Ba3 to Baa3 for the unsecured bond series.

Rating agency Standard & Poor's upgraded the Schaeffler AG company rating to BB+ with a stable outlook on September 21, 2016. At the same time, the issuance ratings of Schaeffler Finance B.V., Barneveld, Netherlands, improved from BB to BB+ for the secured bonds and from B+ to BB- for the unsecured bond series.

The ratings of the only series of unsecured bonds has been withdrawn since the unsecured bonds were redeemed in full on October 13, 2016.

The following summary shows the two rating agencies' ratings for the Schaeffler Group:

Schaeffler Group rating

	12/31/2016		
		Company	Bonds
Rating agency	Rating	Outlook	Rating
Standard & Poor's	BB+	stable	BB+
Moody's	Baa3	stable	Baa3

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. For instance, the company has been presenting and discussing its quarterly and annual results via conference calls for several years. In addition, it regularly holds roadshows in key European financial centers as well as in the U.S.

In 2016, the Board of Managing Directors and the Investor Relations team participated in a total of 14 investor conferences in New York, London, Paris, and Amsterdam. In addition, six road shows were held in Frankfurt, London, and in the U.S.

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 2016, seven such tours and discussions were requested.

The company was covered by analysts representing a total of 15 banks as at February 20, 2017. Eight of these banks issued a recommendation of either buy or overweight on Schaeffler AG's common non-voting shares. Their average upside target was EUR 15.57.

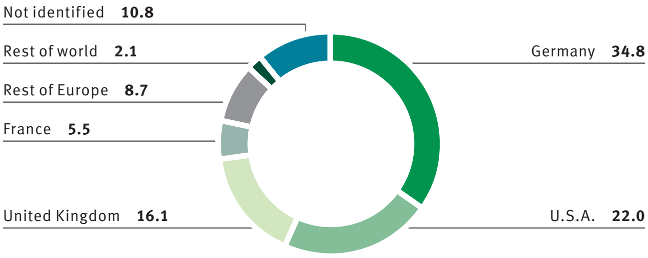
Analyst opinions for Schaeffler AG shares [1)]

Bank	Recommen-dation	Price target in €
Bankhaus Metzler	Hold	13.50
Berenberg Bank	Hold	13.00
BoA Merrill Lynch	Buy	17.00
Citigroup	Neutral	15.00
Deutsche Bank	Buy	18.00
Exane BNP Paribas	Outperform	15.50
HSBC	Buy	18.00
J.P. Morgan Cazenove	Underperform	13.00
Jefferies	Buy	16.00
Kepler Cheuvreux	Buy	18.00
MainFirst Bank	Outperform	17.00
Morgan Stanley	Equal-weight	15.50
NordLB	Hold	13.00
quirin Bank AG	Buy	17.00
UBS	Neutral	14.00

[1)] Recommendations up to February 20, 2017.

1.6 Geographic distribution of free float 2016

Geographic distribution of free float
in percent, as at December 31, 2016



The distribution of the Schaeffler shares' free float as at December 31, 2016 was determined using a shareholder identification survey (Share ID). The identification rate was approximately 89 %, i.e. out of the 166 million shares that are widely held, the survey was able to attribute 148.1 million shares to institutional or private investors. 131.3 million shares were held by approximately 185 institutional investors in 20 countries. Approximately 11.5 million shares were included in the trading portfolios of mainly U.S. Banks as at the reporting date. At year-end, approximately 3 % or 5.3 million shares were held by private shareholders, mainly in Germany.

For further detail please contact:

Investor Relations
tel.: +49 (0) 9132 82-4440
fax: +49 (0) 9132 82-4444
e-mail: ir@schaeffler.com

www.schaeffler.com/ir

See back cover for financial calendar.

Schaeffler Group

Annual Report 2016

Management report

Combined management report in accordance with section 315 (3) 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.

References
Content of websites referenced in the combined management report merely provides further information and is not part of the combined management report. This does not apply to the corporate governance declaration in accordance with section 289a HGB, which includes the declaration of conformity in accordance with section 161 AktG.

Disclaimer in respect of forward-looking statements
This 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.

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.

1. Fundamental information about the group

1.1 Overview of the Schaeffler Group

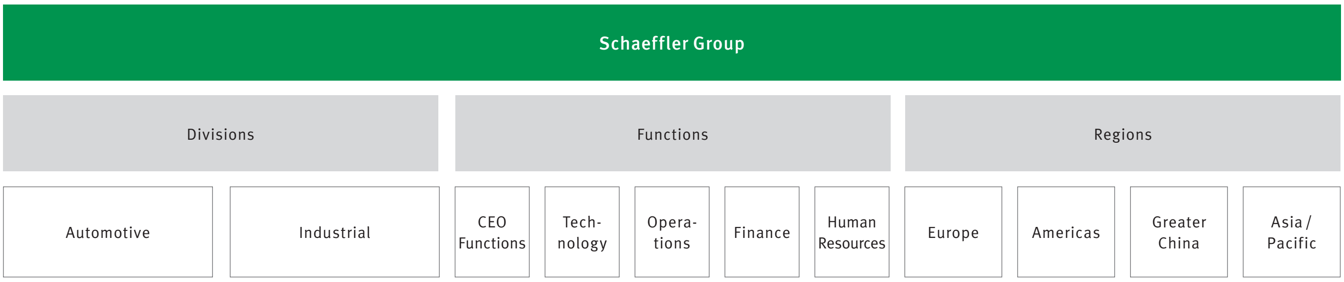
The Schaeffler Group (also referred to as “Schaeffler” below) is a global automotive and industrial supplier. Top quality, outstanding technology, and exceptionally innovative spirit form the basis for the continued success of the company. The Schaeffler Group identifies key trends early on, invests in researching and developing new forward-looking products, and sets new standards in technology. 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. The company already offers innovative products for hybrid and electric vehicles today.

With its approximately 86,000 employees, the Schaeffler Group is one of the leading global technology companies, and its network of manufacturing locations, research and development facilities, and distribution companies consists of approximately 170 locations in over 50 countries. The group’s 75 production facilities are the cornerstone of its operations. As a global development partner and supplier, Schaeffler maintains stable long-term relationships with its customers and suppliers. In addition to Schaeffler AG, a publicly listed stock corporation incorporated under German law with its registered office in Herzogenaurach that acts as the group’s lead company, the Schaeffler Group includes 152 domestic and foreign subsidiaries as at December 31, 2016.

On November 09, 2016, Schaeffler AG presented its strategy “Mobility for tomorrow” to the public; the strategy was developed over the course of 2016 and has been approved by the Board of Managing Directors and the Supervisory Board. Under its strategy “Mobility for tomorrow”, the Schaeffler Group concentrates on four Focus Areas: Eco-friendly drives, urban mobility, interurban mobility, and energy chain. These four 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. Building on these megatrends and Focus Areas, the Schaeffler Group’s Board of Managing Directors developed 8 strategic pillars in cooperation with the Supervisory Board and senior management worldwide. These pillars define the company’s scope for strategic action for the next several years and constitute the basis for the continuous further development of the Schaeffler Group. The “Agenda 4 plus One” excellence program ensures that the strategy is executed; it comprises 16 Strategic Initiatives that have significance worldwide and have been selected from a variety of initiatives. The Schaeffler Group has set itself Financial Ambitions up to 2020 in order to consistently implement its strategy.

Schaeffler AG’s common non-voting shares are listed on the Frankfurt Stock Exchange. In April 2016, IHO Beteiligungs GmbH (until September 28, 2016: Schaeffler Verwaltungs GmbH) sold its remaining holding of common non-voting Schaeffler AG shares. As a result, all common non-voting shares are now widely held. IHO Holding, a group of holding companies owned indirectly by the Schaeffler family, continues to hold all of Schaeffler AG’s common shares. The above transactions have completed the realignment of the company’s corporate and capital structure and have increased the free float to approximately 24.9 % of Schaeffler AG’s total common and common non-voting share capital. Following a review of its mid-cap index, Deutsche Börse had decided in June 2016 to include Schaeffler’s shares in its MDAX index.

Schaeffler Group organizational structure No. 001



Simplified presentation for illustration purposes.

Organizational structure

The Schaeffler Group's organizational structure is characterized by a three-dimensional organizational and leadership structure which differentiates between divisional, functional and regional units. Thus, the Schaeffler Group's business is primarily managed based on its Automotive and Industrial divisions, which consist of several business divisions or regions. The divisions include both the OEM business and the Aftermarket/trading business.

The Automotive division business is divided into the four business divisions Engine Systems, Transmission Systems, Chassis Systems, and Automotive Aftermarket. Since the beginning of 2016, the Industrial division 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 addition to the two divisions, the Schaeffler Group's organizational model includes five functions: (1) CEO Functions, (2) Technology, (3) Operations, (4) Finance, and (5) Human Resources. Distribution is embedded directly in each of the Automotive and Industrial 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. In addition to the Chairman of the Board of Managing Directors (Chief Executive Officer – CEO), the Board of Managing Directors comprises 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). 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.

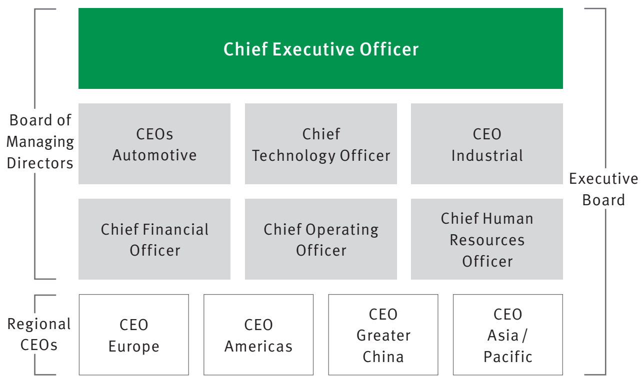
The Supervisory Board of Schaeffler AG appoints, advises, and oversees the Board of Managing Directors and is involved in fundamental decisions. The Chairman of the Supervisory Board coordinates the work of the Supervisory Board.

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 required by section 161 German Stock Corporations Act ("Aktiengesetz" – AktG) in December 2016. The corporate governance report including the corporate governance declaration in accordance with section 289a HGB, which includes the declaration of conformity required by section 161 AktG, is publicly available from the company's website.

See chapter entitled "Corporate governance" for further detail.

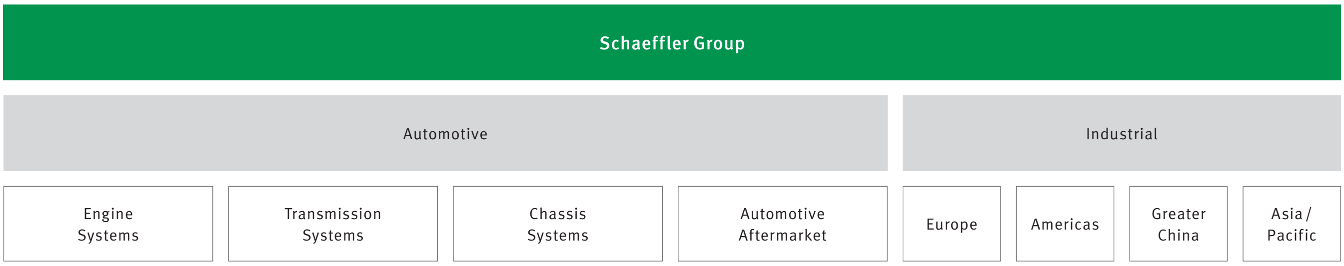
Corporate governance report including the corporate governance declaration in accordance with section 289a HGB, which includes the declaration of conformity in accordance with section 161 AktG at: www.schaeffler.com/ir

Schaeffler Group leadership structure No. 002



Schaeffler Group divisions and business divisions No. 003

since January 01, 2016



Simplified presentation for illustration purposes.

Legal group structure

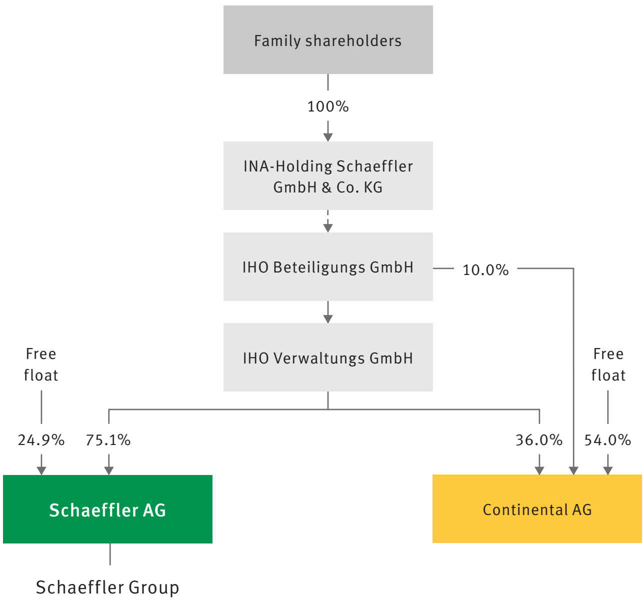
In addition to Schaeffler AG, a publicly listed stock corporation incorporated under German law with its registered office in Herzogenaurach that acts as the group's lead company, the Schaeffler Group includes 152 (prior year: 153) domestic and foreign subsidiaries as at December 31, 2016; 51 (prior year: 51) entities are domiciled in Germany and 101 (prior year: 102) in other countries.

Schaeffler AG's share capital is divided into 500 million common bearer shares and 166 million common non-voting bearer shares as at December 31, 2016.

Each common share and each common non-voting share represents an interest in total share capital of EUR 1.00 each. The company's main shareholder is IHO Verwaltungs GmbH (until September 27, 2016: Schaeffler Verwaltung Zwei GmbH), which

Simplified ownership structure No. 004

as at December 31, 2016



holds approximately 75.1 % of the shares in Schaeffler AG (500 million common shares). 166 million common non-voting bearer shares in Schaeffler AG are widely held. The free float amounted to approximately 24.9 % as at December 31, 2016. IHO Beteiligungs GmbH and IHO Verwaltungs GmbH also hold approximately 46.0 % of the shares in Continental AG.

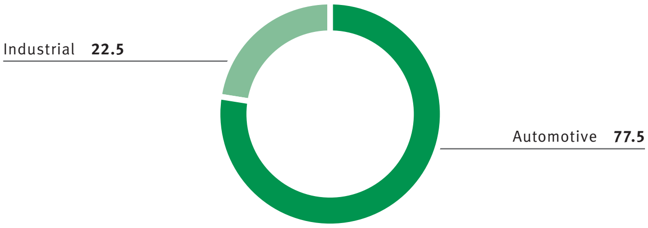
1.2 Business activities

Divisions

The Schaeffler Group has divided its business activities into the two divisions Automotive and Industrial. The Automotive division is subdivided into four business divisions, which in turn comprise several business units. Since January 01, 2016, the Industrial division is primarily managed based on regions. The regions are divided into eight sectors and the trading business. The realigned management model is part of the program "CORE" initiated by the Board of Managing Directors in 2015.

The Automotive division supplies all major automotive manufacturers worldwide as well as approximately 3,300 automotive suppliers (Tier 1) and Automotive Aftermarket customers. The Automotive division generates approximately 77 % (prior year: 76 %) of the Schaeffler Group's revenue. The Industrial division supplies precision products to approximately 8,500 customers in various industrial sectors. The Industrial division contributes approximately 23 % (prior year: 24 %) of the Schaeffler Group's total revenue.

Schaeffler Group revenue by division No. 005
in percent



Automotive

As a partner to the automotive sector, the Schaeffler Group leads the field when it comes to developing and manufacturing groundbreaking components and systems for engines, transmissions, and chassis, for both vehicles with drive trains based on the internal combustion engine and hybrid and electric vehicles. The Automotive division business is organized into the business divisions (BD) Engine Systems, Transmission Systems, Chassis Systems, and Automotive Aftermarket.

Market trends for the Automotive division are driven by the global production volumes of passenger cars and light commercial vehicles. The growth of the global vehicle fleet also plays a crucial role in the automotive Aftermarket business. The Automotive division has the objective of achieving lasting growth of approximately 4 % over and above the increase in worldwide automobile production by 2020.

The Automotive division's main products include clutch systems, transmission components, torsion dampers, valve train systems, camshaft phasing units, electric drives, and bearing solutions in transmissions and chassis. The Schaeffler Group's precision products and systems are key to helping make engines use less fuel and comply with increasingly strict emission requirements. At the same time, they also extend engine and transmission life and increase driving comfort and dynamics. Its comprehensive technical expertise for the entire drive train is what sets apart Schaeffler Automotive, one of the leading automotive suppliers worldwide. As future consumption and emissions targets can only be fully met by electrifying the drive train, the Schaeffler Group offers solutions for the entire range of electrification types – from hybrid through to fully electric drive systems.

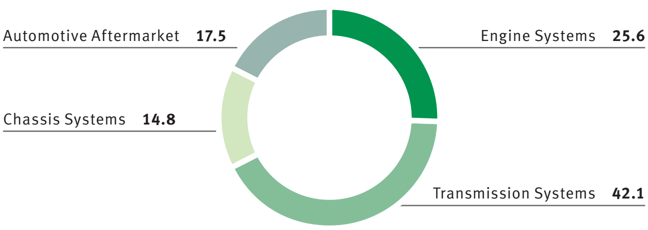
A comprehensive Aftermarket portfolio rounds out the business of the Automotive division. The product range covers applications in clutch and release systems, engine and transmission applications, and chassis applications. In addition, Schaeffler Automotive Aftermarket offers a comprehensive variety of services such as practice-oriented training courses, advice provided by the Schaeffler repair hotline or the group's online garage portal, as well as the development of specialized tools.

Industrial

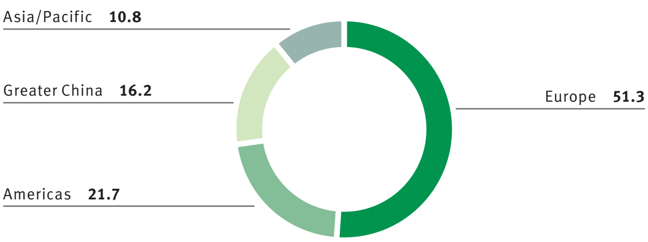
Since January 01, 2016, the Industrial division is primarily managed based on regions due to its wide customer and business structure. On this basis, the Europe, Americas, Greater China, and Asia/Pacific regions operate as profit centers responsible for the Industrial business in their respective markets. Within the regions, the Industrial business is grouped into eight sectors: (1) wind, (2) raw materials, (3) aerospace, (4) rail, (5) offroad, (6) two wheelers, (7) power transmission, and (8) industrial automation. Sales to distributors (Industrial Distribution) round out the Industrial division's regional business.

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. Components are increasingly being integrated in system solutions, some of which are designed as mechatronic systems with data-generating sensors.

Automotive division revenue by business division No. 006
in percent



Automotive division revenue by region No. 007
in percent by market view



With its rolling bearing, linear technology, and direct drive solutions, the Schaeffler Group offers comprehensive technological and application engineering expertise for complete systems from one source that are precisely matched to one another. The focus is increasingly on smart products and on connecting components. One example is the "Machine Tool 4.0", whose sensor-equipped components measure and report vibrations, forces and temperatures at all relevant bearing positions.

The majority of rolling bearings is supplied by the "Bearing & Components Technologies" (BCT) unit as an internal supplier. The bearings and related products are used in applications in drive technology, production machinery, and wind turbines, as well as in heavy industries. In the aerospace sector, the Schaeffler Group is a leading manufacturer of high-precision bearings for jet and helicopter engines as well as for space travel applications.

The key indicator for trends in the Industrial division's relevant market is the global market volume for rolling and plain bearings, for linear technology, and for service products in these areas.

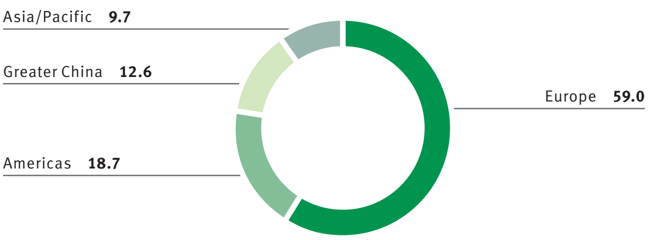
Program "CORE"

First wave: In 2015, Schaeffler AG's Board of Managing Directors decided to realign the company's Industrial division based on the program "CORE". The Schaeffler Group's program "CORE" is aimed at strengthening the Industrial division's core competencies to improve the efficiency and competitive position of the Industrial business for the long term. The program is designed to return the Industrial division to lasting growth and increased profitability.

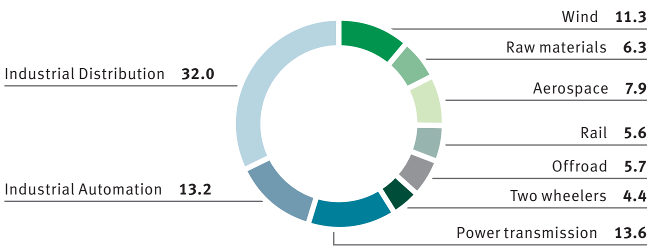
Its key elements are increased sales growth, enhanced delivery performance and service quality, stronger customer orientation, as well as cost savings and efficiency improvements. The organizational realignment serves as the basis for streamlining workflows and processes and improving their efficiency. It includes streamlining the organizational and management structure of the corporate functions and of the corporate product and application development units. The reorganization of the Industrial division also involved taking the necessary steps to implement the new delivery performance and management model "Business is local" and to support its introduction. In connection with this model, the Schaeffler Group has been managing the Industrial business primarily based on regions since January 01, 2016. 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. A further core component of the program "CORE", in addition to increasing efficiency and strengthening the division's competitive position, is stronger customer orientation. The reorganization of the Industrial division included laying down the foundation for a centralized, efficient key account management. As part of the program "CORE", the company decided in 2015 to reduce the Industrial workforce by up to 500 jobs in a socially acceptable manner, particularly in Germany and Europe. These measures were largely completed by the end of 2016.

Second wave: In light of the continued weak economic market environment and the unsatisfactory current earnings situation of the Industrial division during the year, the Board of Managing Directors of Schaeffler AG decided in November 2016 to step up its measures to revitalize the Industrial division and increase its efficiency. It initiated a second wave of measures which also covers the regions outside of Germany as well as functional areas not directly part of the Industrial division. The measures are designed to improve the results of the entire Industrial division for the long-term by further streamlining its structure and reducing production and administrative costs. The second wave focuses on consolidating plant structures, mainly in the Europe region, and reducing the workforce in Industrial-related administrative departments.

Industrial division revenue by region No. 008
in percent by market view



Industrial division revenue by sector No. 009
in percent



Schaeffler Group functions No. 010

Schaeffler Group

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

Simplified presentation for illustration purposes.
Structure presented without divisions.

The second wave is expected to reduce the workforce by a total of approximately 500 jobs. These measures are designed to sustainably improve Industrial division earnings by approximately EUR 60 m over the next three years. At the same time, the company is stepping up program “CORE” measures designed to return the Industrial division to a growth path despite the current challenging market conditions.

Both the first wave of the program “CORE” set up in 2015 and the second wave of measures initiated in November 2016 are designed to return the Industrial division to lasting growth and increased profitability with a target EBIT margin of approximately 10 to 11 % in 2018.

Functions

The multi-dimensional structure of the Schaeffler Group includes the functional management level with five functions: (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) and Operations are discussed in more detail below.

Quality

Quality management and quality performance

The Schaeffler Group’s benchmark is consistent top quality and product safety across all applications in order to provide mobility for tomorrow – in the cities just as in long-distance transportation, eco-friendly, and energy efficient. Outstanding quality is a significant feature differentiating the Schaeffler Group from its competition and represents the basis of the group’s future long-term growth.

In order to consistently meet its standard of quality, the Schaeffler Group maintains a comprehensive quality management system. It is based on a central management handbook containing regulations and prescribed processes applicable groupwide. Compliance with and monitoring of these requirements are guaranteed by audits and reviews, and they ensure a uniform global level of quality. In addition, each unit has managers specifically responsible for quality or other quality experts to ensure that the quality management system at all Schaeffler Group locations is effective and is continuously improved. Benchmark for this is the “zero defects principle” in place at all Schaeffler Group locations, which stands for process stabilization and continuous improvement. It facilitates the early detection and elimination of weaknesses. The thorough implementation of the “zero defect principle” guarantees top process reliability and product quality across all stages – from design and manufacturing through to service.

Employees play a key role in meeting the Schaeffler Group's quality standards. The "Fit for Quality" program was initiated several years ago. "Fit for Quality" ensures a systematic approach to achieving top quality with the objective of "zero defects". The program defines policies and rules of conduct for the day-to-day work of all employees of the Schaeffler Group. It provides guidance and orientation to all employees on how to prevent errors to begin with or how to permanently eliminate them.

All of the Schaeffler Group's manufacturing locations are certified under globally recognized quality norms and standards such as ISO 9001:2015 or ISO TS 16949:2009. In August 2016, ISO (International Organization for Standardization) and IATF (International Automotive Task Force) announced that the standard for quality management systems of companies in the automotive sector recognized around the world, ISO TS 16949:2009, will be replaced by IATF 16949. Selected Schaeffler Group locations will be certified under the new IATF 16949 standard in 2017 and all remaining relevant locations in 2018.

The Schaeffler Group's high quality standards are demonstrated by, among other things, numerous awards received from customers. The Schaeffler Group has received a total of 45 quality awards in 2016, such as the "GM 2015 Supplier Quality Excellence Award" and the "Nissan Quality Supplier Award".

Product safety

Being aware of its responsibility to customers, consumers, and employees, the Schaeffler Group has made product safety its top priority. Understanding the requirements in the markets and customers' needs with respect to safe products and reflecting these in the company's processes is key here. The Schaeffler Group has initiated a communication platform, the "Product Safety Network", that includes a large number of companies and is supported by the industry associations VDA, VDMA, and ZVEI. The "Product Safety Network" receives strong support from the Federal Ministry for Economic Affairs and Energy (BMWi). Its members are companies with a broad spectrum of technical and electromechanical products. The goal of the network is to continuously improve their collective activities with respect to product safety issues in the interest of consumers. The focus is primarily on the fields of passenger transport and mechanical engineering and plant construction. A periodic product safety conference is designed to facilitate sharing of information within the network.

Schaeffler hosted the first product safety conference in January 2015. The second product safety day held by the Schaeffler Group in Shanghai, China, in August 2016 demonstrates the long-term nature of this initiative. The issue of product safety is also being reflected in the Schaeffler Group's organization. Key individuals were systematically identified throughout the organization, trained as product safety officers and authorized, either by the head of Corporate Quality Product Safety or, where needed, by the Board of Managing Directors, to be responsible for decisions related to product safety. As part of this process, the Board of Managing Directors has appointed a CE officer for the CEO Functions who is responsible for the conformity assessment of the Schaeffler Group's products for access to the European market. New information regarding product safety obtained by autonomous observation of the market is shared in a global internal network of product safety officers, evaluated with respect to whether action is required, and developed into product improvements as needed.

Technology

The Technology function has made it its goal to safeguard the Schaeffler Group's technological leadership and to thoroughly delight its customers with innovative application- and customer-oriented system solutions from a single source and with its comprehensive development expertise. Four megatrends will influence the business of the Schaeffler Group in the future: Climate change, urbanization, globalization, and digitalization. Based on these four megatrends, research and development activities are aligned with the strategy "Mobility for tomorrow" and its four Focus Areas "eco-friendly drives", "urban mobility", "interurban mobility", and "energy chain".

See chapter entitled "Group strategy and management" for further detail.

In addition to Corporate R&D Management, Corporate Innovation, R&D Processes, Methodologies & Resources, R&D Expertise & Services, Protection of Industrial Property and Surface and Information Technology, the Technology function also includes the Digitalization Coordination Office. This office is described in more detail following the group's and the divisions' research and development activities.

Schaeffler Group research and development

The Schaeffler Group is actively helping to shape technological progress for "Mobility for tomorrow" with an average of 7,121 R&D staff (prior year: 6,650) at 17 R&D centers (prior year: 17) and additional R&D locations in a total of 24 countries. Its 2,334 patent registrations filed with the German Patent and Trademark Office made the Schaeffler Group the second most innovative company for the second consecutive year in 2015. Over 2,950 inventions reported internally in 2016 (prior year: 2,643) 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 2016.

The Schaeffler Group's research and development activities benefit from the company's many years of experience and expertise with product and systems development. Today, mechanics and electronics are increasingly merged into a complete mechatronic system requiring extensive software to manage. The Schaeffler Group is a supplier who understands complex modules and complete system solutions and can deliver them. The company will continue to expand this expertise, but without neglecting the component business. Schaeffler values its component business and its systems business equally.

Another success factor is the cooperation across divisions within the Schaeffler Group. The consistent transfer of knowledge between the Automotive and Industrial divisions generates significant synergies and, consequently, competitive advantages. For instance, coordinating research and development activities, e.g. in Corporate Innovation, and the global research network facilitates the promotion of product and systems innovations across divisions. One example of this is the Sensotect coating system developed by the company. Sensotect can be used to produce multi-functional surfaces that can directly record forces or torques inside components. It has the potential for applications in places where existing sensors cannot be used. For instance, torque measurements in e-bikes and wheel force measurements in passenger car wheel bearings are now possible. This means that operating conditions in the vehicle can be monitored during operation and the results provided to electronic safety systems in real time.

Apart from the cooperation across divisions, the systematic innovation process also forms the basis of the Schaeffler Group's global technological leadership. Internal and external R&D networks are essential for innovation. For many years, the Schaeffler Group, and Corporate Innovation in particular, have been actively participating in research collaborations such as the "Schaeffler Hub for Advanced Research" at the Karlsruhe Institute for Technology, also known as "SHARE at KIT". Schaeffler and the KIT have had a research collaboration designed with a long-term perspective in place since mid-2012. Under the "Company on Campus" model, Schaeffler and the KIT are studying future-oriented issues in the field of "Mobility for tomorrow" and develop relevant solutions together. This program sets new standards of cooperation in developing electric drive systems and their components as well as in the fields of automated mobility and energy storage. A total of approximately 70 individuals are currently doing research and working in publicly funded projects at SHARE at KIT – as research engineers, Ph.D. students, or in connection with student projects and theses.

The company is transferring the successful format of SHARE at KIT to other issues, both nationally and at an international level. For instance, the Schaeffler Group entered a collaboration project with Friedrich-Alexander University of Erlangen-Nuremberg (FAU) in 2016. Mimicking SHARE at KIT, this collaboration is named SHARE at FAU, and it will also follow the "Company on campus" concept. The focus of the research is on digitalization and on processes in production, in the product, and in services. These areas of focus are summarized under the issues "Digitalization of value streams", "Digital assistance systems", and "Additive manufacturing". In addition to technological innovations, participants will also study issues like the continuing education of employees and legal issues related to digitalization.

In addition, the company is currently preparing for the "Schaeffler Hub for Advanced Research" with Nanyang Technological University in Singapore. This collaboration will concentrate on the requirements of future urban mobility, specifically in Asian metropolises. The focus is on multimodal transport concepts, i.e. on completing a journey using more than one mode of transportation. Topics range from mobility studies of commuter flows and their needs regarding first and last mile to connectivity and use of data by vehicles below the conventional automobile through to the development of new urban mobility concepts.

Research and development in the Automotive division

The megatrends increasing globalization and urbanization require new forms of mobility. A growing scarcity of resources and climate change make reducing energy consumption essential. These challenging developments offer significant opportunities for the Schaeffler Group.

Schaeffler System 48 V concept car No. 011

As a result, the field of E-mobility represents a key opportunity for the Schaeffler Group's future, and, therefore, a focus of the strategy "Mobility for tomorrow". The Schaeffler Group is a world leader in developing components and systems for the drive train and already offers innovative components and systems for hybrid and electric vehicles today. To facilitate a comprehensive approach, the company established the eMobility Systems

Division several years ago; it consolidates its wide range of activities relating to alternative types of drives across business divisions and national borders. In addition, engineers are working at research institutions such as the SHARE at KIT to share technology between the university and the company and are extensively researching solutions in the field of energy storage, electric drives, and automated mobility.

One example of the outcome of these research and development activities is the "Schaeffler System 48 V" concept car, which was presented in 2016. Starting with an Audi TT, the company developed a drive architecture containing an "electric axle" comprising a 48 V electric motor on the rear axle. In this hybrid concept featuring what is referred to as a P4 arrangement, the electric axle complements the front-wheel drive internal combustion engine. An additional belt-driven starter generator also operating at 48 V is connected to the engine.

The 48 V on-board electric subsystem uses a lithium-ion battery as its energy store. It is connected via a voltage transformer to the 12 V on-board electric system which powers all the various electrical components in the vehicle, from headlights through to seat adjusters. This electric axle also features torque vectoring, i.e. selectively distributing the drive forces to specific wheels. This improves the agility and safety of the vehicle and the electric axle provides the vehicle with all-wheel drive functionality when combined with the front-wheel drive. The energy generated during braking is fed back into the energy system via the recuperation function in most braking operations which significantly reduces consumption. Furthermore, the Schaeffler electric axle combines the electric motor and the power electronics into one unit, generating important savings in terms of space and weight.

Another component the Schaeffler Group has developed for new vehicle concepts and automotive platforms in the field of E-mobility is the electric wheel hub drive known as the "E-Wheel Drive". In this highly integrated wheel hub drive, all components required for drive, deceleration, and driving safety – such as the electric motor, power electronics, controller, brake, and cooling system – are contained within the wheel rim. In addition to optimum use of space, highly integrated wheel hub drives also offer significant benefits in terms of maneuverability, driving dynamics, and active safety. Opportunities which make the electric wheel hub drive a valuable addition to Schaeffler's portfolio of electric drive systems. As part of the test program, a development vehicle based on a Ford Fiesta was created in a collaborative project with Ford.

Based on its expertise regarding drive trains based on the internal combustion engine, the Schaeffler Group demonstrated potential reductions in CO_2 by 25 % using the Gasoline Technology Car II, which was built in co-operation with Continental and Ford, with "electronic clutch management (ECM)", including an automated clutch, as an example. Another result of the Schaeffler Group's research and development activities, the mechatronic active roll control, won the German Innovation Award. It has gone into serial production at several automobile manufacturers.

Research and development in the Industrial division

The digitalization megatrend has resulted in a fourth industrial revolution, "Industry 4.0", and is having a considerable impact, particularly on production companies. Industry 4.0 stands for intelligent networks connecting product development, production, logistics, customers, and suppliers. Its technological basis are intelligent, digitally linked systems that maximize the possibilities for autonomous production and optimum plant operation: People, machines, systems, logistics, and products communicate and collaborate directly with each other.

The Schaeffler Group is continually expanding its research and development activities in this field and presented the "Predictive Maintenance 4.0" technology in 2016. Predictive Maintenance 4.0 expands conventional maintenance systems and provides the customer with new options for increasing efficiency and reducing the total cost of ownership. The focus is on two digital services: Calculating the remaining service life of rolling bearings and automatically diagnosing rolling bearings.

Predictive Maintenance 4.0 – a wind turbine No. 012

The calculation of the remaining life of rolling bearings involves calculating the nominal remaining useful life for each bearing in the machine or system at time intervals that can be freely defined. The resulting remaining useful life data for every bearing in a machine can be viewed on an internet-capable end device. Comparing the remaining life of the rolling bearings in the machines of a production facility with the next scheduled maintenance makes it possible to manage the level of production in such a way that the bearings will not fail before the scheduled maintenance interval is reached.

Automated rolling bearing diagnosis uses vibration monitoring systems to monitor rolling bearings and to detect emerging damage to bearings and other machine components. The Schaeffler Group has started developing technology that is able to evaluate very high volumes of data from vibration analysis systems intelligently, reliably, and automatically. The vibration data will be automatically digitally processed in the Schaeffler Cloud, which provides adequately high processing power and a large number of possible analyses by linking with additional data from machines and sensors.

Far from being restricted to production plants, this technology is suitable for all applications involving high and fluctuating loads. For instance, data evaluation in passenger trains can facilitate higher average speeds, greater operating performance as well as longer maintenance intervals while also improving operating reliability. Sensor units to be developed specifically for rail applications can be used to measure structure-borne sound, temperatures, and speeds on axlebox bearings. The Schaeffler Group has entered a collaboration project to research this issue with Southwest Jiaotong University (SWJTU). In wind turbines, as well, modular sensor systems in the drive train, designed specifically for low frequencies, will use vibration measurement technology to obtain condition information during operation and process it in real time in the future.

The Industrial division's research and development activities also included, for instance, developing rolling bearings for the new third channel of the Panama Canal. Components from the Schaeffler Group play a key role in the operation of the lock gates. The slow movement poses special challenges for these bearing solutions, as it causes a quasi-static load with very high forces inside the bearings. An important feature of the new Panama Canal is its three reservoirs that are located next to each barrage. The steel guide pulleys for their gates are equipped with Schaeffler bearings that are chromium-plated, making them particularly resistant to corrosion. Different variants of the Schaeffler Group's Durotect coating are used for this application.

Digitalization and IT

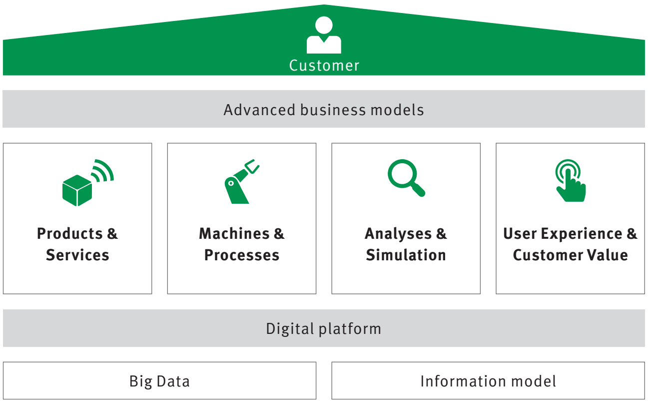
As it increasingly merges the real world and the digital world, the digitalization megatrend poses new challenges, but also offers great opportunities. Digitalization is thus transforming industries and their traditional processes. Digital technologies are becoming a core component of value added in purchasing, manufacturing, logistics, distribution as well as in the human resources and finance functions. Being a progressive, integrated automotive and industrial supplier, the Schaeffler Group considers digitalization one of the key issues of the future. Therefore, it has developed the "Digital Agenda" initiative as part of its "Agenda 4 plus One" excellence program, a component of the group's strategy "Mobility for tomorrow".

The key objective is connecting the physical and the digital world in order to increase the amount of value added. Internally, people, machines, buildings, production locations, logistics etc. are being connected with each other. To generate added value for the company and its customers, existing business models are expanded and new, digital business models are developed and implemented.

To this end, the Schaeffler Group will add sensors, actuators, and controllers including software to its components in order to be able to obtain and process valuable data on machine condition and behavior in the future. The customer does not benefit from gathering data per se, but rather from information generated by combining big data analyses with Schaeffler's thorough sector and application know-how and the resulting synergies. The Schaeffler Group agreed on a strategic partnership in this area with IBM in 2016. IBM will act as the technology provider, consultant, and research and development partner supporting Schaeffler in establishing a digital ecosystem and integrating its mechatronic components, systems and machines into the rapidly expanding world of the "Internet of Things".

The Schaeffler Group has established a centralized project management in 2016 in order to provide groupwide and cross-functional coordination and support for its digitalization projects. This "Program Office Digitalization" manages the coordination, establishment and expansion of the Schaeffler Group's digital activities. The "Digital Agenda", which was refined and put into more concrete terms in 2016, is among the significant initiatives dealing with this issue.

Digital Agenda of the Schaeffler Group No. 013



The Digital Agenda centers around the customer. New digital business models are oriented toward the customer's benefit. Four components reflect the key digital business scenarios the Schaeffler Group is focusing on:

(1) Products & Services: Data generated by sensor systems help expand product functions. Connecting products generates added benefits. Linking products to the Cloud facilitates adding further value and produces new business models.

(2) Machines & Processes: Connected machines and digital assistance for humans are continually advancing production. The Schaeffler Group will utilize this to expand its leadership role in the production and supply chain management environment and to make this know-how available to the market, as well. In addition, business processes are characterized by integration and real-time access to any data generated; as a result, once generated, any data can be used anywhere within the company without changing media. Therefore, the Schaeffler Group has decided to facilitate continuous use of data and to create new, service-oriented processes for this purpose.

(3) Analyses & Simulation: The Schaeffler Group strives to link data from products and processes with each other. Analyses based on the interaction of primary data and the sector- and application-related expertise of Schaeffler's specialists provide information that adds value. The Schaeffler Group is expanding its own know-how in the field of analytics and is integrating it into existing methodologies and domain knowledge.

(4) User Experience & Customer Value: The interaction between humans and machines is a significant factor for productivity and fun in the digital world. Therefore, the objective is quick recognition and learning as well as goal-oriented interactions.

The four components are being implemented on a digital platform on which all data-based services run. The platform was set up as the first milestone of the collaboration between the Schaeffler Group and IBM. Schaeffler is working closely with IBM to develop solutions for Schaeffler's internal needs as well as for its customers on a timely basis, using design thinking and agile development methodologies.

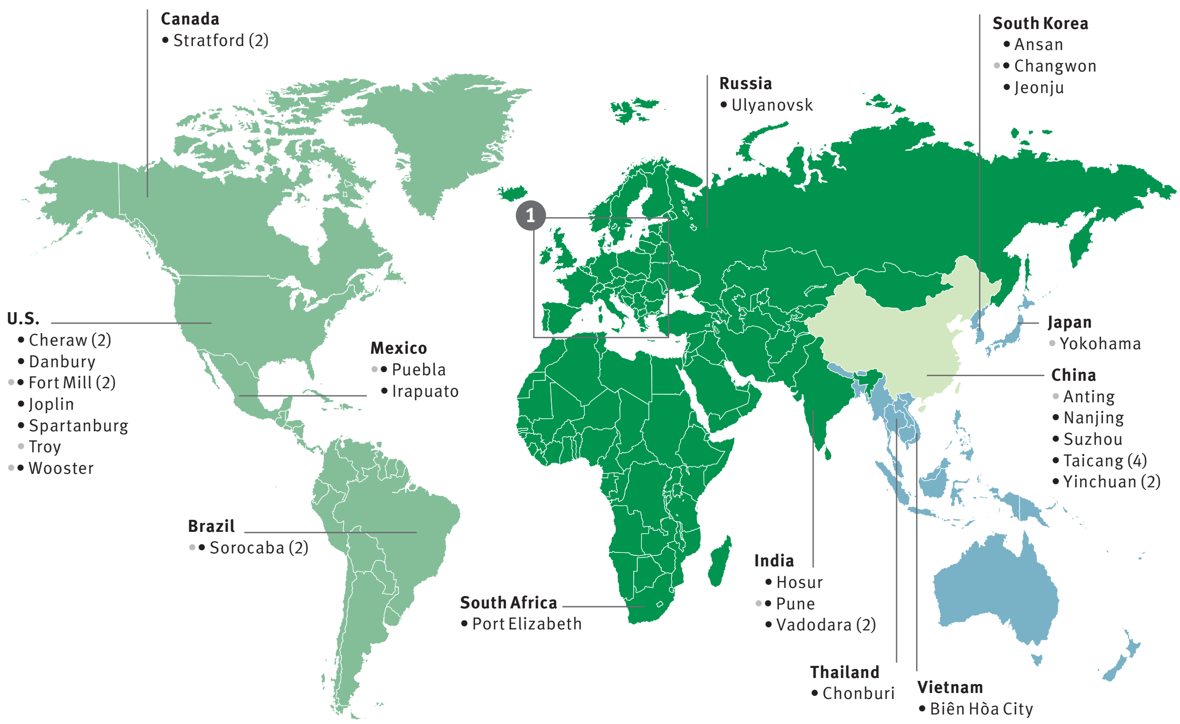
The issues of data standards, property rights, and security are defined as the basis of the Digital Agenda. As data will be a core component of value added in the future, the Schaeffler Group is implementing standards, architectures, and methodologies and has joined the Industrial Data Space Association to promote their distribution. Another important item in that regard is safeguarding digital patents for data-based services.

The Schaeffler Group's employees are fundamental to the implementation of the digital business models. In addition to the existing thorough know-how of its employees, the Schaeffler Group was able to win numerous "digital talents" in 2016 and is aiming to establish a significant talent pool.

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. Development of the IT strategy under the "IT 2020" initiative was largely completed in 2016, and implementation of the strategy has started. It focusses on rapidly putting in place the organizational and information technology prerequisites for digitalization, renewing and further developing the application and infrastructure landscape, and changing the role of IT within the company from that of an internal service provider to that of a strategic business partner and key component of the digital business models.

Schaeffler Group plants and R&D centers — No. 014

World



1 Europe

(partial view)

Regions [1]		Europe	Americas	Greater China	Asia/Pacific
R&D centers	• (grey)	9	5	1	2
Plants	•	48	14	8	5

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

Operations

Production

As an integrated global automotive and industrial supplier, the Schaeffler Group has a global manufacturing network consisting of 75 production facilities in 23 countries with approximately 60,000 employees worldwide. The plants represent the Schaeffler Group's "backbone". They 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.

Schaeffler plant in Taicang, China No. 015

The Schaeffler Group's global manufacturing network makes it possible to maintain consistent high levels of quality and efficiency at all Schaeffler plants. The plants also form the core of the Schaeffler production system, which is part of the group strategy and, as such, represents the basis for achieving outstanding results in the key measures 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. Its 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. Based on close integration with purchasing and distribution, continuous value streams are created between the Schaeffler Group's customers, plants, and suppliers.

The Schaeffler Group increased its production volume by 2.6 % in 2016. The Schaeffler Group strives to always deliver the highest-possible quality to its customers while maintaining cost efficiency and reliability of supply. It continually improves its production system, with all locations consistently applying the "zero defects principle". Modern quality management techniques and integrated planning across the entire supply chain ensure that all of these requirements are being met. The company has once again realized improvements in quality and efficiency in 2016, resulting in, among other things, a reduction in the number of customer complaints. In addition, the "Integrated Planning" program enabled the company to further improve the reliability of supply to the customer in 2016.

The internal supplier "Bearing & Components Technologies" (BCT) is part of the Operations function, as well. BCT brackets all of the Schaeffler Group's rolling bearings. In 2016, it produced approximately EUR 3.4 bn in output for the Automotive and Industrial divisions.

BCT combines the Schaeffler Group's specialized expertise regarding development and production of rolling bearings. By defining the global standards for rolling bearings within the Schaeffler Group's production system and rolling them out around the world, BCT drives operating excellence in quality, cost, and delivery performance. This streamlines organizational structures, increases transparency and standardization, and generates synergies. As a result, BCT was able to flexibly adjust production capacity in the Industrial division despite a challenging market environment. Among BCT's priorities for 2016 was expanding the production of large-size bearings in its plant in Braşov, Romania, in 2016; the plant became the Schaeffler Group's center of excellence for large-size bearings when these activities were shifted there from Wuppertal in 2016. Further priorities were the "Generation-C deep groove ball bearings" initiative and expanding the global production and development network. The company is continually working to increase the efficiency of machinery and equipment and to harmonize the common production line platform for rolling bearings.

The opportunities offered by digitalization enable the Schaeffler Group to realize significant efficiency gains from, among other things, increasingly interconnected plant and machinery. The expanded use of sensor and actuator technology and connecting them using the internet helps make machines more independent. This facilitates preventative maintenance, helping to minimize the number of unplanned breakdowns. Combined with elements of "Lean Management", this contributes to a significant improvement in the Schaeffler Group's competitive position.

In addition, the Schaeffler Group aims to make the plants attractive for employees while increasing the level of integration of all relevant areas in the value chain. Concepts such as energy efficiency, modularization, and Industry 4.0 play a significant role in this context. The new Schaeffler concept "Factory for tomorrow" demonstrates solutions in response to this and represents another step toward operating excellence. One core component of the "Factory for tomorrow" concept is the modular design of factories as well as creating ways to make adjustments over the life cycle of a factory at little cost. In total, this will improve profitability, resource efficiency, adaptability, communication across functions and excellence in all direct and indirect production areas of the Schaeffler Group.

A total of 48 plants represent the Schaeffler Group in its Europe region. In addition to manufacturing locations in Germany, France, Italy, and Spain, the group also maintains significant production plants in Central and Eastern Europe. The Schaeffler Group employs approximately 500 production staff at its production plant in Berndorf, Austria. The plant contributed approximately 1.9 % of the Europe region's production volume and is among the lead plants for the worldwide production of tapered roller bearings. In 2016, the plant took top honors in a MOVE review, an internal model for measuring the degree of maturity in terms of becoming a lean business. The award was primarily won based on the application and implementation of the "lean" principles and the consistent elimination of waste in all areas of the plant. Top quality, reliability of supply, and exceptionally innovative spirit make this plant one of the Schaeffler Group's leading plants.

Production capacity at the Central and Eastern European production plants is continually being expanded due to increasing demand for Schaeffler products. For instance, the company plans to expand the plant in Debrecen, Hungary. The new production building will be equipped with machines employing state-of-the-art grinding technology for manufacturing rolling bearings. The planned expansion will increase the plant's production volume by approximately 50 %. The Hungarian plant currently contributes 1.4 % of the Europe region's production volume. The first parts produced by the new plant are scheduled for delivery in the second half of 2017. The construction of the new plant in the Czech city of Svitavy started in the prior year was completed on schedule in 2016. The two Slovak plants in Skalica and Kysucke are among the most significant plants in Central Europe. These two plants generated 6.2 % and 7.8 % of the Europe region's production volume. In Kysucke, approximately 4,100 production staff manufacture mostly rolling bearings. The Skalica plant with approximately 4,800 production employees manufactures rolling bearings as well as linear technology products and engine components and systems. The plant in Skalica, which celebrated its 25th anniversary in 2016, also received an award from Toyota Motors Europe for its quality performance in 2016.

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 Sorocaba, Brazil, the Schaeffler Group operates a production location with two plants which employ a total of approximately 4,800 production staff. The location received numerous quality awards in 2016, such as the "Quality Excellence Performance Award" from Toyota do Brasil and the "2015 Supplier Award" from Honda Automóveis do Brasil. In addition, the location placed fourth in the "AutoData Quality and Partnership Ranking 2015", putting it among the most important suppliers to the automotive sector in Brazil.

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. A new manufacturing building was opened at the production location in Nanjing, China, in 2016. Approximately 1,000 production employees manufacture camshaft phasing units, hydraulic tappets, chains, tensioners, and other engine components there. As expansion in Taicang and Nanjing has reached its limits, the Schaeffler Group is planning a new production location in Xiangtan, China. The company intends to gradually expand the new location. Initially, it is constructing a plant for automotive parts and precision bearings approximately 200,000 square meters in size. The plant is scheduled to commence operations in late 2018.

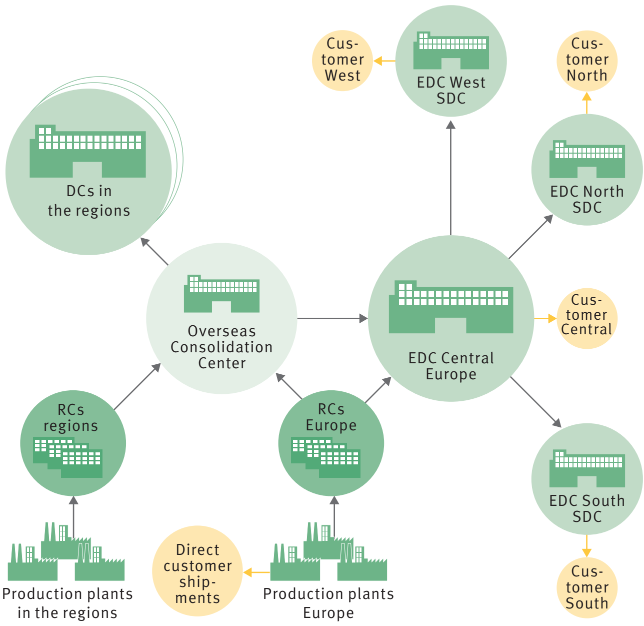
The Schaeffler Group has 5 plants in its Asia/Pacific region. By opening the plant in Chonburi, Thailand, the group has considerably expanded its manufacturing presence in the Asia/Pacific region. The new plant was constructed on a 55,000 square meter property in the immediate vicinity of several large automobile plants. It increases the local production volume and expands the portfolio of Automotive applications, providing the Schaeffler Group's customers with better access to high-quality products and modern manufacturing technology. At the initial stage, approximately 150 production staff are manufacturing various automotive parts. The production plant was built using a modular system, offering the possibility to add additional lines for Schaeffler products and solutions covering the entire Automotive value chain in subsequent stages.

Logistics

The logistics function is responsible for designing, operating, and continually improving the entire supply chain of the Schaeffler Group. 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.

Within the Schaeffler Group, the Corporate and Regional Logistics functions were responsible for managing approximately 250 warehousing locations with more than 350,000 square meters in storage space, and for moving approximately 270,000 tonnes in freight between the most significant destinations in 2016. More than 100 shipping points ensure deliveries to customers. Total logistics activities have increased approximately 1.4 % compared to the prior year. Approximately 62 % of Schaeffler's logistics activities were concentrated in the Europe region. Approximately 19 %, 13 %, and 6 % of all logistics activities related to the Americas, Greater China, and Asia/Pacific regions, respectively.

European Distribution Centers (EDC) No. 016



DC: Distribution Center
SDC: Satellite Distribution Center
RC: Replenishment Center
OCC: Overseas Consolidation Center

A significant element of the strategic direction 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 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 already met their performance requirements with an excellent delivery performance. In addition, the groundbreaking ceremony for the european central distribution center "EDC Central Europe" (Kitzingen, Germany) represents the achievement of another milestone toward completing the new distribution network for the Industrial Europe business unit.

In 2016, the company also focused on integrating suppliers into the manufacturing process. In cooperation with SupplyOn, it implemented the first stage of a transport order management system (TOMS) for global suppliers at a number of locations. The system represents the basis of a supply chain collaboration platform that will be used to map, manage, and improve processes in supply chain management, supplier risk and performance management, and in transportation management. This collaboration platform is an example of digitalization in Schaeffler's logistics function and of the increased collaborative planning, management, and monitoring of logistics-related activities designed to add value throughout the entire Schaeffler Group.

Schaeffler UK Ltd. was presented with the 2016 elogistics award by the AKJ Automotive working group for its project Seamless Supply Information Integration in 2016. To carry out this project, Schaeffler used the transport order management system (TOMS) developed and offered by SupplyOn. With this system, transport orders can be generated, combined and assigned to shipping companies in the supply chain. The pick-up sheet method is used to ensure deliveries are made on time and in the correct quantities. In addition to a considerable reduction in inventory levels of purchased parts, the company was able to significantly improve supplier performance.

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.

Purchasing consists of the corporate purchasing function for production and non-production materials, and project-related purchasing for the Automotive and Industrial 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.

Schaeffler Group regions and subregions No. 017

- Schaeffler Group
  - Europe
    - Germany
    - Western Europe
    - Southern Europe
    - CEEMEA [1]
    - India
  - Americas
    - North America
    - South America
  - Greater China
    - China
  - Asia/Pacific
    - Korea
    - Japan
    - Southeast Asia

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

In 2016, the Schaeffler Group reported a slight 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 less than production output. The purchasing volume in general purchasing (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 2016.

The Schaeffler Group obtained goods and services from approximately 34,000 suppliers in approximately 80 countries in 2016. The volume of these purchases related primarily to the Europe (63.4 %) and Americas (17.7 %) regions. 11.5 % and 7.4 % 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. The Schaeffler Group has benefitted considerably from falling raw materials prices in 2016.

Continental AG and the Schaeffler Group have been cooperating on purchasing for seven 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 slightly in 2016.

Regions

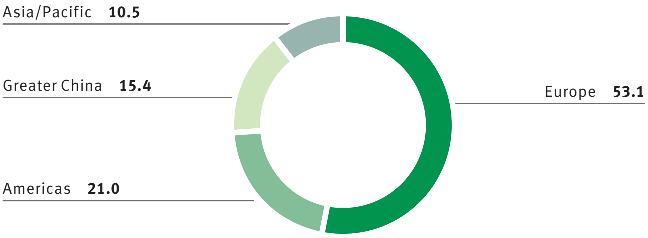
The Schaeffler Group's three-dimensional matrix organization divides the company's business not only into divisions and functions, but also groups the company's activities into the four regions Europe, Americas, Greater China, and Asia/Pacific. Each of the Schaeffler Group's four regions is managed by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

The basis for the Schaeffler Group's economic success lies in its proximity to the customer. With approximately 170 locations worldwide, 75 production facilities, 17 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 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 central headquarters 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 various benefits regarding aspects of 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 revenue by region No. 018

in percent by market view



The **Europe region** combines the subregions Germany, Western Europe, Southern Europe, Eastern Europe & Middle East and Africa (CEEMEA), as well as India. The Germany subregion represents the Schaeffler Group's most important sales market. The Europe region contributed 53.1 % (prior year: 53.3 %) of consolidated revenue in 2016. The degree of localization amounted to approximately 96 % (prior year: 96 %) in 2016. The Europe region employed a total of 60,127 employees in 2016, representing 69.4 % of the company's entire workforce. This figure includes the employees of the group's global head office in Herzogenaurach, Germany. The region has 48 plants and 9 R&D centers. Its regional head office is located in Schweinfurt, Germany. In 2016, the company started expanding the plant in Debrecen, Hungary. The expansion will raise the plant's production volume by approximately 50 %. The construction of the new plant in the Czech city of Svitavy started in the prior year was completed in 2016 as scheduled. These steps as well as the expansion of the plants in the Slovak locations of Kysucke and Skalica and in Brasov, Romania, which were finalized in the prior years, demonstrate the key significance of the Europe region to the Schaeffler Group.

The two subregions North America and South America make up the **Americas region**. This region contributed approximately 21.0 % (prior year: 22.0 %) of revenue in 2016. The degree of localization amounted to approximately 71 % (prior year: 71 %) in the Americas region. A total of 12,480 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, South Carolina, U.S.A. The Schaeffler Group has been manufacturing in this region since 1953.

As China is a strategically important sales market for the Schaeffler Group, China, Taiwan, and Hong Kong are managed as a separate **region Greater China**. 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 15.4 % (prior year: 14.4 %) of group revenue in 2016. The degree of localization amounted to approximately 74 % (prior year: 68 %). A total of 11,255 staff were employed in Greater China. 8 plants and 1 R&D center are located in this region. As expansion at the existing locations has reached its limits, the Schaeffler Group is planning a new production location in Xiangtan, China. The plant for automotive parts and precision bearings is scheduled to commence operations in late 2018.

The **Asia/Pacific region** comprises Korea, Japan, and the countries in Southeast Asia. The Schaeffler Group has been represented in this region since 1953. 10.5 % (prior year: 10.3 %) of group revenue was generated by this region in 2016. The degree of localization amounted to approximately 38 % (prior year: 41 %) in 2016. The Asia/Pacific region had 2,800 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 the plant in Chonburi, Thailand, in 2016, the group has considerably expanded its manufacturing presence in the Asia/Pacific region.

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.

On November 09, 2016, Schaeffler AG presented its strategy “Mobility for tomorrow” to the public; the strategy was developed over the course of 2016 and was approved by the Board of Managing Directors and the Supervisory Board.

Vision and Mission

In its mission, the Schaeffler Group describes the task it is committed to. Underlying the 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. 019

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.”

4 Focus areas

In developing the strategy, the company identified four megatrends that will influence the business of the Schaeffler Group in the future: Climate change, urbanization, globalization, and digitalization. The Schaeffler Group is an automotive and industrial supplier of global stature with the expertise and technology to reduce friction and thereby save energy. As such, it feels compelled to meet the challenge of helping the world tackle climate change.

This equally applies to increasing urbanization, which demands new forms of mobility. These are the reasons Schaeffler sees climate change and urbanization as two future trends that are especially important to the company and its business. Globalization is particularly relevant for the Schaeffler Group in an economic context, as is digitalization in the realm of technology. As explained within the context of the Strategic Pillars, the company sees growing digitalization as an important opportunity for further optimizing its business model in the future.

Driven by the four megatrends, Schaeffler defined four areas for action as early as 2014; being an automotive and industrial supplier with global stature, it intends to focus on these four areas for action in the future. Given the variety of the group’s products and services, and the number of industries that it supplies, this is more than a logical step – it is essential if Schaeffler wants to help shape the “Mobility of tomorrow” as a supplier. The four Focus Areas are: “Eco-friendly drives”, “urban mobility”, “interurban mobility”, and “energy chain”. They form the basis for the Schaeffler Group’s strategic direction. They also demonstrate that the company is ready and willing to use and share its knowledge and expertise across divisions.

(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 drive “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.

Mobility for tomorrow No. 020

(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.

To transform these considerations into a concrete frame of reference for its customers and business partners, employees and executives as well as family and external shareholders, the Schaeffler Group has defined further elements of its strategy "Mobility for tomorrow" based on the 4 significant megatrends and the resulting 4 Focus Areas. These elements consist of 8 Strategic Pillars defining the company's scope for strategic action over the years to come, an excellence program comprising 16 Strategic Initiatives that will help execute the strategy, and the Financial Ambitions 2020.

8 Strategic pillars No. 021

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 more than 170 locations worldwide, 75 production facilities, 17 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. 022

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!

SCHAEFFLER

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.

16 Strategic initiatives

Any strategy is only as good as its implementation. In preparing its strategy, Schaeffler has therefore put a great deal of thought into how it can implement its strategy as efficiently and consistently as possible. Building on the positive experience the Schaeffler Group had with its first transformation program “One Schaeffler” drawn up after the change of management in October 2013 and successfully rolled out by the end of 2015, it has developed a tailor-made program of excellence which summarizes its key strategic initiatives in 5 categories. The Schaeffler Group therefore calls its excellence program “Agenda 4 plus One”.

The “Agenda 4 plus One” includes the following 5 categories: Customer focus, Operational excellence, Financial flexibility, Leadership and talent management, and – as “plus One” – Securing long-term competitiveness and value creation. The “Agenda 4 plus One” comprises 16 Strategic Initiatives that have significance worldwide and have been selected from a variety of initiatives.

“Agenda 4 plus One” categories No. 023

1 Customer focus
2 Operational excellence
3 Financial flexibility
4 Leadership and talent management

Long-term competitiveness and value creation
plus One

Each initiative is the responsibility of a Member of the Executive Board as a sponsor and managed by a project manager. The stated aim is to successfully implement all initiatives by the end of 2020.

“Agenda 4 plus One” will be implemented according to the successfully established project management approach of the program “One Schaeffler”. This approach makes certain that the design, implementation and management of initiatives carried out follow standard rules and criteria, and are supported and accompanied by an independent program organization under the jurisdiction of the Chief Executive Officer.

16 Strategic initiatives No. 024

Customer focus
1 Customer Excellence
2 E-Mobility
3 Industry 4.0

Operational excellence
4 Quality for Tomorrow
5 Global Footprint
6 Factory for Tomorrow
7 Shared Services
8 Process Excellence

Leadership and talent management
10 Leadership & Corporate Values
11 Qualification for Tomorrow
12 New Work

Financial flexibility
9 Working Capital

Long-term competitiveness and value creation
13 Program CORE
14 IT 2020
15 Digital Agenda
16 Global Branding

Financial Ambitions 2020

The Schaeffler Group has set itself challenging targets for 2020. The company intends to grow its revenue – excluding the impact of currency translation and external growth – by an average of 4 to 6 % p.a. and to achieve an EBIT margin before special items of 12 to 13 %. On this basis, the Schaeffler Group wants to achieve free cash flow of around EUR 900 m by 2020, excluding external growth. Furthermore, the group intends to increase its earnings per share excluding external growth to around 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 net-debt-to-equity ratio – known as the gearing ratio, the quotient of the two variables – to be less than 75 % by 2020. Moreover, the group is planning to pay out dividends amounting to 30–40 % of the annual net income 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 the basis for further growth strategies.

Financial Ambitions 2020 No. 025

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

1) Excluding external growth.
2) Net-debt-to-equity ratio (excluding pensions).
3) 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

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

M&A strategy

Following the successful realignment of its capital structure and its renewed financial flexibility resulting from the reduced level of debt, the Schaeffler Group will no longer rely only on purely organic growth. The company will generally focus on acquisitions related to the future-oriented fields of E-Mobility, Industry 4.0, and digitalization. Smaller acquisitions will serve to expand and strengthen our expertise.

In order to appropriately manage the risks of such an acquisition strategy and to enable long-term active portfolio management, the Schaeffler Group will optimize its group structure and establish a professional M&A process.

In this vein, Schaeffler acquired electric motor manufacturer Compact Dynamics GmbH from SEMIKRON International GmbH at the end of 2016 with a view to strengthening the company's expertise in order to expand its E-mobility activities. At the same time, Schaeffler and SEMIKRON have entered into a cooperation agreement in the field of power electronics. On the other hand, Schaeffler has actively streamlined its production portfolio by disposing of its fine blanking activities in Switzerland and selling Schaeffler Motorenelemente AG & Co. KG in Magdeburg.

Strategy communication

Starting from the results of the Strategy Dialog in mid-July 2016, Schaeffler gathered suggestions and recommendations on strategy considerations from approximately 300 international senior managers in eight "Global Challenge and Feedback Meetings". The strategy "Mobility for tomorrow" and the "Agenda 4 plus One" excellence program were approved by the Supervisory Board at its meeting in October 2016.

Following that, the strategy "Mobility for tomorrow" was presented to the public for the first time on November 09, 2016. The Board of Managing Directors also explained the strategy in person to 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 is currently being communicated to individual customers and business partners.

To further convey the strategy to all employees, a comprehensive roll-out plan was prepared for 2017 in order to embed the core elements of the strategy – 4 Focus Areas, 8 Strategic Pillars, 16 Strategic Initiatives and the Corporate Values and Leadership Principles – within the company in a uniform manner for the long term.

Strategy and planning process

Since 2015, the Schaeffler Group goes through a newly developed annual strategy and planning process comprising three key components, (1) the Technology Dialog, (2) the Strategy Dialog, and (3) the Planning Dialog, which sequentially build on each other. As part of this process, the strategy "Mobility for tomorrow" was refined and developed in an extensive dialog with the group's senior management and the Schaeffler AG Supervisory Board in 2016.

The Technology Dialog takes place in February of each year and 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 five to ten 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.

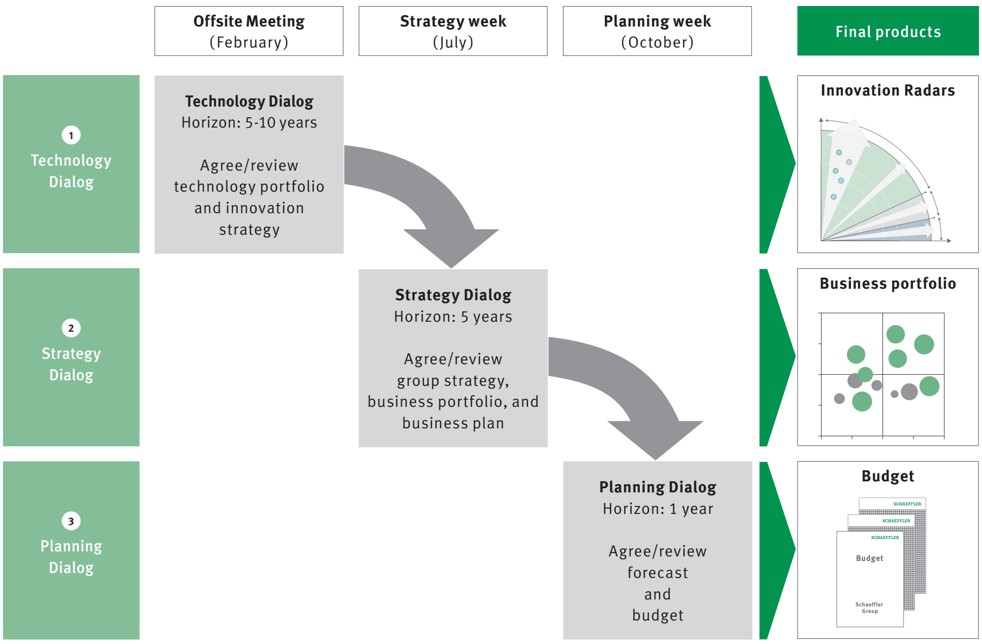
The Strategy Dialog takes place mid-year. It focuses on the Schaeffler Group's business strategy (incl. indicative business plan) for the coming 5 years, the substrategies for the divisions with their strategic business units, the regions, and the functions. A detailed market analysis and an analysis 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 each other, prioritized, and added to where necessary.

In the 2016 Strategy Dialog, approximately 400 different initiatives of the divisions, regions, and functions were identified and then evaluated and categorized. Initiatives of paramount importance for the Schaeffler Group were combined in the "Agenda 4 plus One" excellence program. The remaining initiatives are implemented and followed-up at the level of the divisions, regions, and functions. This is generally done using the "Agenda 4 plus One" format, and as a result the groupwide program is mirrored, in whole or in part, and populated with various individual initiatives at the level of the various organizational 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 broken down 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. 026



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 2016, 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 is primarily managed based on the Automotive and Industrial divisions. The Automotive division business is divided into the four business divisions Engine Systems, Transmission Systems, Chassis Systems, and Automotive Aftermarket, which operate as profit centers. Management of the Industrial division is primarily 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.

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 of 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.

Value-based management

The Schaeffler Group manages its business portfolio based on value. The most significant measures used are the strategic performance indicators ROCE (return on capital employed) [1] and Schaeffler Value Added (SVA) [2]. ROCE represents the relationship of EBIT to average capital employed (capital employed) and measures earnings generated in relation to capital employed. As the ROCE performance indicator measures long-term performance, it is not used to manage the Schaeffler Group's operations. Schaeffler Value Added, which is closely linked to ROCE is calculated as EBIT less the cost of capital. It 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.

See chapter entitled "Value management" for further detail.

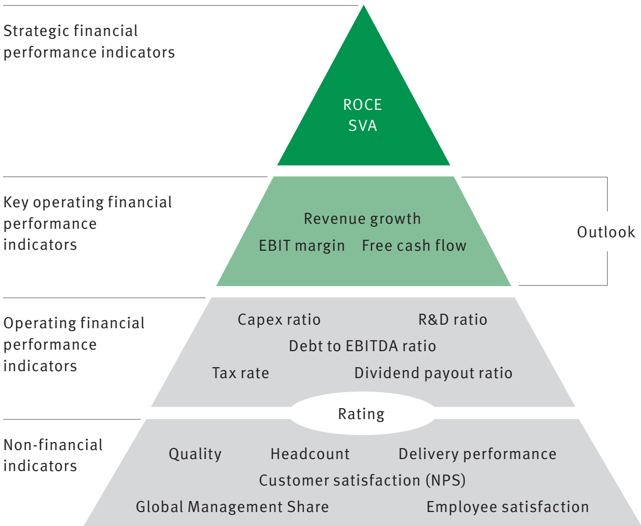
Schaeffler Group performance indicators

The performance of the Schaeffler Group's business is based on a long-term growth strategy. Group management ensures that the Schaeffler Group is growing profitably while utilizing capital efficiently. Therefore, significant emphasis is placed on the performance indicators revenue growth and EBIT margin. 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.

The Schaeffler Group focuses on continually monitoring and optimizing the following three key financial operating performance indicators to measure the economic performance of its business:

- Revenue growth
- EBIT margin
- Free cash flow

Key performance indicators No. 027



Operating decisions are based on these three key financial operating performance indicators, as is the outlook. The Board of Managing Directors also continually monitors additional financial operating performance indicators including the capex ratio, R&D ratio, debt to EBITDA ratio, tax rate and dividend payout ratio.

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

[1] Ratio of EBIT to average capital employed (property, plant and equipment + intangible assets + working capital).
[2] EBIT less cost of capital (average capital employed x pre-tax weighted average cost of capital).

operating budget embedded in a longer-range strategic corporate plan established by the Board of Managing Directors.

The management remuneration system takes these financial performance indicators into account in determining variable short- and long-term remuneration.

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 (net promoter score, NPS), Global Management Share, employee satisfaction, and rating.

Remuneration model

The Schaeffler Group aims to consistently align its corporate values, strategies, structure, management model, and brand image with each other and to focus the entire organization on common goals. A consistent performance-based remuneration system is key to achieving this aim.

When Schaeffler AG's common non-voting shares were listed in October 2015, the remuneration system was adjusted retroactively to January 01, 2015 and consistently oriented toward the Schaeffler Value Added/increasing shareholder value and free cash flow targets. In a subsequent step, the company adjusted the remuneration system for its top executives, applying the same considerations underlying the remuneration system for the Board of Managing Directors. The new remuneration system was introduced with retroactive effect from January 01, 2016.

The targets largely represent the strategic and key financial operating 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).

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 and commitment 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 in order to safeguard Schaeffler's competitive position.

HR strategy

In 2016, the Schaeffler Group reassessed its strategic areas within Human Resources (HR) and prepared the HR Roadmap 2020 comprising strategically coordinated initiatives. An overarching HR vision and mission underlying the day-to-day operations were developed, creating a unified identity for the HR function. HR's innovative ability is strongly driven by digitalization, demographics, and diversity and these issues are embedded in the human resources strategy.

At the core of the HR strategy, there are five pillars HR employs to directly support operations:

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

Strategic workforce planning

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

It forms a robust 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, such as in the E-Mobility, digitalization, and increasing globalization growth areas.

A pilot project for the hybrid and clutch systems business units uses the results of the strategic human resources planning process as a basis for deciding what actions are required, for instance internal and external recruiting, qualification programs, or in- or outsourcing strategies. These actions enable the Schaeffler Group to identify and actively mitigate risks related to excess personnel or a shortage of staff.

Employer branding & recruiting

HR's employer branding & recruiting activities promote Schaeffler's perception as an attractive employer and the position of the employer brand "Schaeffler" with the aim of recruiting the best talents 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 new talents as much as for employees that have been with the company for many years. Effectively positioning the company as an attractive employer worldwide is fundamental to successfully competing for the brightest minds. The Schaeffler Group ranked highly in recognized employer rankings in 2016. The current survey of research institution "trendence" lists the company as one of the 30 most popular employers among engineering students in Germany in 2016. In addition, market research company Universum named the Schaeffler Group "High Climber" in recognition of its ranking as an employer by engineering students. The group was also successful internationally. In China, the Schaeffler Group was named "Top Employer China 2016" by the Top Employers Institute and received the "Best Employer of the Year" award from career platform Zhaopin.com for the fifth consecutive year.

The digital shift proved particularly challenging in 2016, as the Schaeffler Group needs to position itself as an employer offering interesting assignments in the field of digitalization. To achieve this, it initiated a communications campaign that involves both creating media content and a media presence and developing excellence networks and events and is aimed at generating enthusiasm about the company among digital talents. In order to attract qualified students and graduates to the company, Schaeffler once again focused particularly on cooperative and sustainable partnerships with universities, student unions, student associations and organizations such as Formula Student Germany.

See the chapters entitled "Schaeffler Group research and development" and "Corporate responsibility" for further detail on collaborations with universities.

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.

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 the U.S., Germany, Mexico, Canada, and the Greater China region, covering approximately 65 % of relevant employees worldwide. The coming two years will see the roll-out in Brazil and the Asia/Pacific and Europe regions. A uniform system with clear processes and standardized tools will then be in place starting in 2018, ensuring all employees worldwide are systematically supported. Among the areas the system has a particularly focus on is timely succession management.

Leadership and corporate values

The "Leadership and corporate values" initiative that is part of the "Agenda 4 plus One" involves implementing a leadership model applicable around the world that is based on the corporate values and reflects the latest trends.

Defining clear leadership principles and authorities helps implement the strategy "Mobility for tomorrow" and adapts the Schaeffler management style to modern challenges such as digitalization or Industry 4.0. The new leadership model and its behavioral anchors are based on the corporate values "sustainable, innovative, excellent, and passionate".

Both senior management and employees play a key role in designing the leadership model and then integrating it into all relevant human resources processes. In addition to comprehensively integrating the leadership model into recruiting and personnel development processes, the "Leadership and corporate values" initiative also entails establishing and defining a "Leadership" career path.

Training & learning

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

With its “Qualification for Tomorrow” initiative, part of the “Agenda 4 plus One”, the Schaeffler Academy confronts 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 is a success factor for being able to compete worldwide. As a result, this initiative addresses the most important core issues and the company’s future strategy related to the issue of learning.

An improved IT infrastructure, modern systems, and tools are designed to create a worldwide platform for up to date learning.

A uniform training process tailored to the regions is defined for the Training of Tomorrow. This guarantees a consistent standard of training quality and ensures that the required infrastructure and equipment is made available.

HR uses custom-fit qualification programs to actively support the Schaeffler Group’s strategy, address trends, and retain talents for the Schaeffler Group long-term.

Employee structure and development

The Schaeffler Group employed an average of 85,733 employees (prior year: 83,930) in 2016. The number of employees at December 31, 2016 was 86,662, 2.9 % above the prior year level.

The company recruited new personnel compared to December 31, 2015 primarily in production and production-related areas – mainly in the Greater China and Europe regions, especially in Eastern Europe.

Number of employees No. 028

December 31	12/31/2016	12/31/2015	Change in %
Europe [1]	60,127	58,600	2.6
Americas	12,480	12,625	-1.1
Greater China	11,255	10,216	10.2
Asia/Pacific	2,800	2,757	1.6
Schaeffler Group	**86,662**	**84,198**	**2.9**

[1] Including employees of the corporate center.

Workforce structure

The following table summarizes data on the structure of the Schaeffler Group’s global workforce:

Workforce – structural data No. 029

	12/31/2016	12/31/2015	Change	
Average age (years)	39.8	39.7	0.3	%
Average tenure (years)	11.2	11.1	0.9	%
Proportion of female employees (%)	21.4	21.0	0.4	%-pts.
Proportion of female managers (%) [1]	11.8	11.4	0.4	%-pts.
Absenteeism due to illness (%) [2]	3.8	3.6	0.2	%-pts.

[1] Managers are defined as employees in a supervisory function.
[2] Number of sick days as a percentage of scheduled working days.

The average period employees have been with the Schaeffler Group (tenure) amounted to 11.2 years in 2016 (prior year: 11.1). The average age of the Schaeffler Group’s workforce was 39.8 years (prior year: 39.7).

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 21.4 % (prior year: 21.0 %), and the proportion of female managers was 11.8 % (prior year: 11.4 %).

The company signed the “Charta der Vielfalt” (diversity charter) as early as in 2008, committing to implementing the Charta’s guidelines internally by putting in place 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.

See the chapter entitled “Corporate responsibility” for further detail on diversity.

A comprehensive demographics framework helps the company prepare for future demographic trends and the challenges they bring. For instance, several workshops were held examining the needs of “generation Y and Z” as well as investigating the requirements of a more senior workforce regarding a working environment that is conducive to their health. To this end, the “Demographics on the Shop Floor” project involved setting up a job register which facilitates presenting and planning jobs that are age-appropriate and appropriate for aging staff and helps assign employees with impaired abilities to appropriate jobs.

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.

4,054 classroom training sessions (prior year: 3,931) attended by 37,345 participants (prior year: 36,485) were held in Germany in 2016.

In addition, 90 different e-learning courses were offered to staff and were taken by 25,074 employees (prior year: 63 e-learning courses offered; 18,068 participants). 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 Germany- and Europe-wide management programs as well as the international management programs (IMP) which received the Global Human Resource Development Award 2015. 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. Its outstanding culture of learning with excellent training offerings and learning methods earned the Schaeffler Group the "Golden Peacock National Training Award" in India.

See the chapter entitled "Corporate responsibility" for further detail on the IMP.

Employee qualification and continuing education No. 030

Number in Germany	12/31/2016	12/31/2015	Change in %
Classroom training sessions	4,054	3,931	3.1
• Participations in – classroom training sessions	37,345	36,485	2.4
E-learning courses	90	63	42.9
• Participations in – e-learning courses	25,074	18,068	38.8

1) Figures as at December 31.

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 full-time project managers who combine extensive technical expertise and key know-how with outstanding project management skills.

In 2016, a global project team refined and adjusted the established specialist and project career path in order to meet the needs of the business, especially the regions. The new global framework now combines additional entry-level career stages, greater regional flexibility – particularly at the lower-level career stages – with clearly defined requirements and global standards for higher-level career stages in management.

This creates more regional flexibility overall to develop employees toward this career path early on while increasing transparency and comparability of specialists and project managers worldwide.

Supporting new talents

Attracting and training new talents in all areas is essential to ensuring the company's long-term success. 2,966 trainees (or 3.4 % of the Schaeffler Group's workforce) were pursuing an apprenticeship at the Schaeffler Group (prior year: 2,897 or 3.4 % of the workforce) as at the end of 2016. The number of trainees has thus grown by approximately 2.4 % compared to the prior year. These future specialists are trained in a total of 22 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 164 students were enrolled in the "Duales Studium" and 178 in "Two-in-One" bachelor programs in 2016. The company also offers a graduate degree in the form of a master's degree program with currently 31 students.

In addition, the Schaeffler Group offers special trainee programs to above-average university graduates, 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, 40 young talents (prior year: 46) were enrolled in this trainee program as at December 31, 2016. Similar programs operate in many countries around the world, including in the U.S.

Health management and occupational safety

As a result of demographic change, the company has to develop effective preventive health care programs for its aging workforce. The workplace health care management in place is an important component of the HR initiatives.

Occupational health and safety help maintain the health and performance of employees. As a result, they represent an important issue for which the company and its employees bear equal responsibility. In order to protect and promote employee health, working conditions and compliance with occupational safety requirements are continually reviewed and improved as part of the EnEHS management system (Energy Environmental Health and Safety).

As a preventive measure, the Schaeffler Group also promotes its employees' health-at-work-related skills and awareness and maintains long-term employability by continuously building its structured workplace health management program. During the reporting period, the company started a program of corrective exercises in production. The project provides training for small groups of employees at their workspace over a period of 12 weeks. Later, multipliers from this group are trained to perpetuate the program and ensure its long-term success.

In addition, the Schaeffler Group aims to offer employees with existing health issues targeted measures on a voluntary basis over and above those offered by the public health care system to restore and sustainably maintain their health. During the reporting period, components were added to this program to help employees with impaired abilities suffering from musculo-skeletal disorders regain their employability. This involves testing the employee specifically with respect to their specific job and remediating any identified deficiencies in dedicated training centers to the extent possible.

1.5 Corporate responsibility

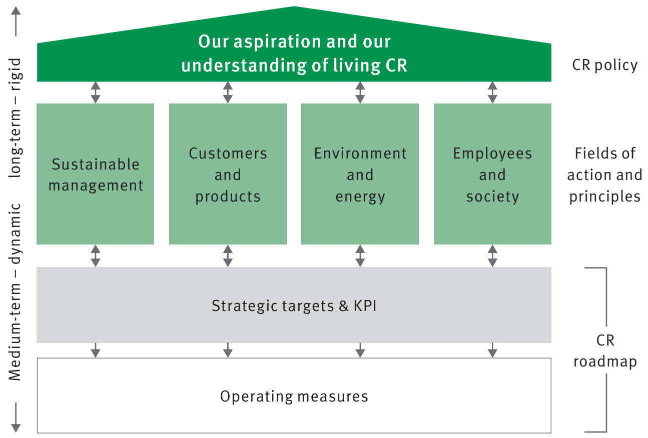
The Schaeffler Group's strategy is based on the group's commitment to drawing on its strength as an automotive and industrial supplier and partnering with its customers to shape the mobility of the future. To put this commitment into concrete terms, it has developed the following vision: "As a leader 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."

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. The Schaeffler Group accepts its corporate responsibility (CR) to minimize any adverse ecological and social impact associated with its own operations worldwide – even above and beyond legal requirements.

Sustainable management

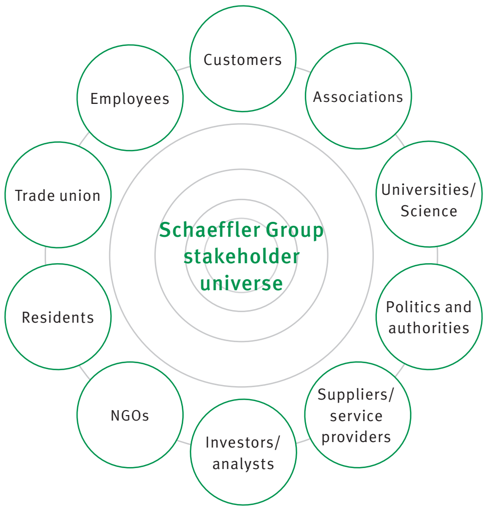
The Schaeffler Group's corporate responsibility strategy defines a framework for the group's corporate responsibility.

Corporate responsibility strategy No. 031



The CR policy sets out the Schaeffler Group's overarching standard for all of its employees, decision makers, and business partners. In the CR policy, the Schaeffler Group expresses core principles for acting sustainably in the following four areas: (1) Sustainable management, (2) Customers and products, (3) Environment and energy, and (4) Employees and society. In addition, a CR roadmap sets out specific targets and actions. It is the medium-term, dynamic component of the corporate responsibility strategy that is based on the significant issues regularly defined during a company-wide significance analysis.

Key stakeholders of the Schaeffler Group — No. 032



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 company's long-term success, the Schaeffler Group regularly and openly exchanges information with its key stakeholders. These are actively involved by way of a regular significance analysis to determine the most important issues for Schaeffler's CR activities, providing them with the opportunity to help shape the company's corporate responsibility strategy.

In an anonymous online survey in 2016, all employees worldwide as well as selected customers and suppliers were invited to assess the relevance of specific CR issues to Schaeffler as a company acting responsibly. Prior to the survey, an extensive analysis of various documents involving all of the Schaeffler Group's stakeholder groups was performed to determine and validate the issues to be included. A total of 1,250 employees and 431 customers and suppliers participated in the survey. The results were presented in a significance matrix indicating which issues the company and its stakeholders consider to be particularly relevant to the long-term success of Schaeffler's business. Behind each of the 24 issues listed, there are specific targets and actions summarized in the Schaeffler Group's CR roadmap.

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

The Schaeffler Group's actions are guided by the core values of a global family business, even after the listing: Schaeffler's actions are sustainable, innovative, excellent, and passionate. This applies to its own operations as well as to its global supply chain.

National legislators' requirements regarding responsible procurement are high. The British Modern Slavery Act introduced in 2015 requires companies to disclose steps they have taken to prevent modern slave labor in their supply chain. The Schaeffler Group enters into quality assurance agreements with relevant suppliers to ensure their compliance with high environmental and social standards and reviews potential suppliers before adding them to its supplier portfolio. If an assessment of the potential of possible new business partners with respect to environment, health and safety (EHS) issues indicates that they do not meet the required minimum standards, they are eliminated from the selection process. If violations are serious, existing business relationships are terminated, as well. In addition, the company offers its suppliers development measures designed to help them live up to its environment, health and safety requirements. Employees in Schaeffler's purchasing department also receive training in this area. The company utilizes "reasonable country of origin inquiries" (RCOI) to trace the regional origin of ores and initiate specific corrective action where necessary. This approach is designed to ensure that mining of commodities such as tin, tungsten, tantalum, or gold does not contribute to financing wars.

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 general compliance management system helps the company and its employees comply with all applicable local, national, and international laws and regulations.

Customers and products

Looking at global trends such as urbanization, digitalization, shortage of resources, and climate change, the Schaeffler Group is committed to setting new standards in modern engineering and to help customers meet the resulting challenges, such as reducing CO_2 emissions and the growing automation of vehicles with innovative products and system solutions. The relevance of this is also reflected by the results of the significance analysis performed in 2016, which identified "products and technologies" that help shape the mobility of tomorrow as the most significant issue.

For instance, at the eCarTec trade show held in Munich from October 18 to 20, 2016, the Schaeffler Group presented its Step² concept car, which is equipped with Schaeffler components. In this large series compact class vehicle, Schaeffler installed a digitally-controlled transmission and an electronic clutch, the E-Clutch, which has received the "GreenTec Award", to demonstrate how efficient these components are in combination. A semi-automated two-speed powershift transmission sets the Step² apart from conventional systems. Compared to electric drives with only one speed, it reduces energy consumption by approximately 6 % and combines high traction force for quick acceleration with high efficiency at higher driving speeds. It avoids the loss of energy by eliminating the interruption of the traction force during clutch operation.

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 also place high demands on brand protection. To be able to prove the origin of the product, product labels are equipped with a data matrix code. It makes each product uniquely identifiable and can be traced back using an internet address. By scanning the code, the customer can find out whether it is in fact an authentic Schaeffler code.

See the chapter entitled "Quality" for further detail on product safety.

For further detail on the data matrix code at: www.tecidentify.com

Another issue identified in the significance analysis is customer satisfaction. In order to measure customer satisfaction and maintain it at a consistently high level, the Schaeffler Group systematically surveys its Automotive customers regarding customer satisfaction on a regular basis; Schaeffler Automotive Aftermarket customers were surveyed in 2016. The resulting customer satisfaction index showed a slight improvement.

Environment and energy

The Schaeffler Group's corporate responsibility strategy documents the company's high standard when it comes to environmental protection and reducing greenhouse gas emissions. To help the company effectively protect the environment, Schaeffler 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 48 to 55 in 2016. Nearly all manufacturing locations worldwide have been validated under EMAS and certified under ISO 14001 by independent assessors. The Schaeffler Group plans to demonstrate its first-rate environmental management by having all of its manufacturing locations worldwide entered into the EMAS site register by the end of 2017.

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 continuously improving energy management. The Schaeffler Group measures and monitors its progress with respect to energy management using its energy data management system (EDMS).

The company also contributes to energy efficiency by converting its energy supply to generating its own energy using a highly efficient combined heat and power (CPH) unit. The new central heating stations include the CPH units, absorption chillers, as well as buffer storage for heat and cooling energy generated, and supply 41 % of the power, 77 % of the heat and 60 % of the refrigeration required by the plant. The company plans to supply the Herzogenaurach location with heat exclusively using CPH units by the end of 2018.

Reconditioning and then reusing used bearings can save up to 95 % in energy and CO_2 emissions. Schaeffler aerospace has been offering this service to its international customers in Schweinfurt for over 20 years and has had a location in the Asia/Pacific region since November 2015. At its Unna location, the Schaeffler Group has been reconditioning primarily used LuK product brand passenger car clutches since 1976. Power steering pumps and overrunning alternator pulleys for the generic and brand specific vehicle service and repair markets complement the product portfolio.

Various improvement projects aimed at enhancing the Schaeffler Group's international transportation networks also help the group use energy and resources more efficiently. They focus on better utilizing space in cargo holds by combining shipments, establishing ideal routes and transportation cycles, and utilizing consolidation hubs within the network. The Seamless Supply Information Integration project, for instance, aims to design the transport chain to be more efficient by facilitating securely combining and billing transport orders in a global supply network. The project received the "elogistics award 2016".

The Schaeffler Group also strives to support its employees in making their mobility more sustainable. It has adopted a comprehensive conceptual mobility plan comprising setting up an infrastructure for charging electric vehicles at the company's German locations. The company established a separate standard for this, covering issues such as fire safety, designation, choosing locations, and power supply. Such charging stations are currently available at a total of five locations, with particularly powerful quick charging stations being installed in Bühl and Hirschaid. In addition, the Schaeffler Group has opened up its company car policy in Germany to plug-in hybrids, allowing employees to order and use these vehicles as company vehicles.

Employees and society

The responsibility for its employees and good corporate citizenship are deeply embedded in the Schaeffler Group's core. It uses its global reach to help shape the social environment of its company locations internationally and to promote intercultural dialog around the globe.

For the first time, all employees worldwide were invited to participate in an online survey on Schaeffler's corporate responsibility as part of this year's significance process in October 2016. The results show that issues such as supporting and developing employees, work-life balance, and compensation and retirement benefits are of particular importance.

The company signed the "Charta der Vielfalt" (diversity charter) as early as in 2008 and committed to proactively promote diversity within the company. Due to the international nature of the Schaeffler Group, having a diverse range of employees is a significant success factor for the company. The diversity of its workforce is the key to identifying and meeting the expectations of the regional markets. It improves the working atmosphere, enhances many processes, e.g. in research and development, and has a positive impact on the company's earnings. To remain competitive and expand its economic success, Schaeffler is relying more strongly on an integrated diversity strategy as part of its strategic human resources plan. Internationality, promoting women in leadership positions, and the inclusion of people with disabilities are among the important issues to be dealt with here. Compared to the prior year, the proportion of women in leadership positions increased from 11.4 % to 11.8 % in 2016.

The company has continued to systemize its workplace health management program and has begun to implement it throughout the group in 2016. Among the bases underlying the program are the guidelines of the Luxembourg Declaration on Workplace Health Promotion in the European Union. All activities directly related to individuals have been subsumed under the "pit stop" ("Boxenstopp") heading. With this health program, the Schaeffler Group has introduced a prevention scheme aimed at counteracting the causes of absenteeism. The main cause of absenteeism is musculoskeletal disorders. Beginning with the "Feeling like exercising" ("Lust auf Bewegung") component increasing the motivation of sedentary employees in a low-threshold manner, appropriate measures have been implemented for all types of symptoms. With a "Job rehabilitation" ("JobReha") program based on "workplace-related medical exercise therapy" ("arbeitsplatzbezogene Medizinische Trainingstherapy" (aMTT)), the company is offering individual, professionally supervised exercise programs designed to reduce symptoms, strengthen the back and maintain the employability for the long term to employees with impaired abilities.

Schaeffler employees also have high expectations with respect to fair and transparent remuneration and attractive retirement benefit schemes that meet the employees' needs. In response, the company has converted the previous "Schaeffler function rating system" ("Schaeffler Funktionsbewertungssystem") to the uniform worldwide "Schaeffler Global Job Grading System" in 2016. The system increases transparency and makes it easier to effectively enhance the career paths and succession planning processes and coordinate them globally. 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 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 35,062 ideas via the ideas management software in 2016, generating cost savings of EUR 14.7 m. The group is currently using this system at 41 locations in twelve 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.

See the chapter entitled "Employees" for further detail on the HR strategy.

Education and science, health and social affairs, and sports and cultural events represent the core areas of the Schaeffler Group's corporate citizenship activities. It participates in a variety of initiatives and collaborations and provides support in the form of donations and scholarships. By making positive contributions to its environment, the Schaeffler Group helps overcome challenges facing society and aims to add value to the company in the long run. 2016 saw the Schaeffler Group once more supporting numerous social projects.

In the fields of education and science, the Schaeffler Group relies on collaboration agreements with universities, research institutions and other qualified project partners. A total of ten leading research institutions in Europe, the U.S., China, Japan, and Singapore participate in the "Schaeffler Innovation Network".

Schaeffler Group innovation network No. 033

Region	Partner	Focus
Europe	SHARE at FAU	Digitalization
	SHARE at KIT	E- & urban mobility
	Digital Start-up Center ZOLLHOF	
	Fraunhofer	Several locations
Greater China	Southwest Jiaotong University	High-speed trains
	Tongji University	Automotive, E-Mobility
Americas	Silicon Valley	Start-ups
	Clemson University	Urban mobility
Asia/Pacific	SHARE at NTU	Urban mobility
	Tokyo University of Science	Additive Manufacturing, Tribology

See the chapter entitled "Schaeffler Group research and development" for further detail on collaborations with universities.

In the field of health and social affairs, the Schaeffler Group provides financial assistance in emergencies and disasters and promotes social and humanitarian projects. One focus here was on South Africa in 2016. For instance, as part of the "CSR Program South Africa", the Schaeffler Group assisted the South African government with promoting equal opportunities for citizens previously socially or economically disadvantaged. For example, Schaeffler collaborated with the "SOS Children's Village Association" to help provide abandoned or orphaned children with protection and a family environment. Sponsoring an orphanage, Schaeffler covered the costs incurred in 2016. The Schaeffler Group also collaborated with the "ACVV Khayalethu Youth Centre", a facility helping boys living on the street successfully integrate into society and live up to their potential by, among other things, Schaeffler providing a safe environment and offering schooling.

The Schaeffler Group also provided assistance to welfare facilities, projects and organizations as part of its "International Management Program" (IMP). It enables managers in various functions, areas, and regions to initiate and finance social projects. In February 2016, for instance, IMP participants at the Hosur (India) location collected donations by selling calendars, giving swimming lessons, or hosting a barbecue at home. They used the funds to finance school clothes, shoes, and lunchboxes and personally delivered them to orphaned and handicapped children during a school day visit. Other social projects were carried out in Germany (Herzogenaurach), South Korea (Changwon), and the U.S. (Fort Mill).

FAG Bearings India Ltd., a Schaeffler Group subsidiary, won an award for its social commitment in India. In February 2016, it received the "True Impact Award 2016" for establishing a barrier-free hostel building in Mook Dhwani Trust. This is one of several projects of the "HOPE CSR Initiative" started by FAG at the Vadodara location. The facility provides a home for over 30 differently-abled and deaf-mute female students, and thus a good basis for attending secondary school. Projects receiving the company's support at this location also include providing mobile health stations to improve health care for the rural population.

In the field of sports and cultural events, the Schaeffler Group supports associations, foundations, and museums. In addition, the company holds memberships in nonprofit associations for the promotion of arts and cultural events.

The Schaeffler Group once again supported talented young engineers from around the world, including by acting as the main sponsor of the design competition "Formula Student Germany 2016". The award goes to the best overall package of a race car with an electric drive under the aspects of innovation, economy, efficiency, and driving ability. A total of 111 student teams from approximately 25 countries competed against each other. 22 of these teams were directly supported by Schaeffler in their development activities. Besides Germany, "Formula Student" competitions are also held in Spain, Italy, and Brazil as well as other countries, with Schaeffler supporting a total of 44 teams of young talents around the world.

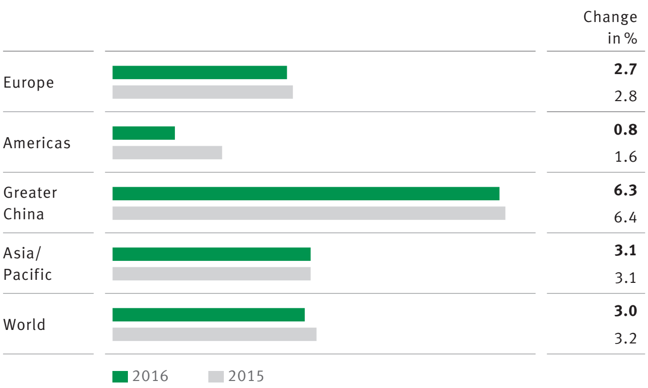
2. Report on the economic position

2.1 Economic environment

Macroeconomic environment

The global economy experienced only moderate overall growth in 2016, despite gathering speed in the latter half of 2016. Global gross domestic product for 2016 was 3.0 % higher than in the prior year (Oxford Economics, January 2017). The Euro region economy continued to recover. Its economic trend remained largely unaffected by the outcome of the referendum in the United Kingdom in favor of leaving the European Union. In the United Kingdom itself, the economy proved more robust than expected following the referendum. Economic activity in the United States improved noticeably during the latter half of 2016, following restrained growth in the first two quarters of the year.

Growth in gross domestic product No. 034



Source: Oxford Economics (January 2017).
Real gross domestic product calculated based on purchasing power parities.
Regions reflect the regional structure of the Schaeffler Group.

In light of further positive employment data and rising inflation, the Fed raised its benchmark interest rate in December 2016. Buoyed by continued government intervention, growth in China stabilized in line with the government's annual target. In Japan, the fundamental economic momentum remained weak.

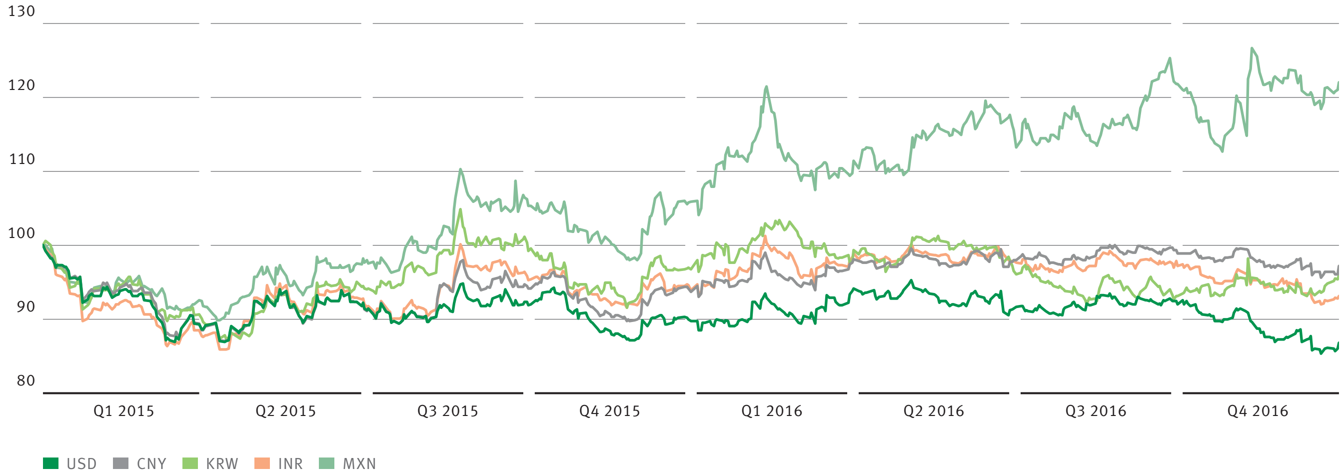
Economic growth in the Schaeffler Group's Europe region amounted to 2.7 % in 2016. The Euro region continued its economic expansion at a moderate but stabilizing pace. In the United Kingdom, growth once again exceeded that of the Euro region, despite the unexpected outcome of the referendum. Germany reported solid and steady economic growth, primarily driven by private consumption. Although the Russian economy contracted once more, there are indications that the economic situation is improving, helped especially by stabilizing raw materials prices. As in previous years, India, also part of the Europe region, continued to expand rapidly.

Economic growth in the Schaeffler Group's Americas region amounted to 0.8 %. Following temporarily weaker momentum in the first half of 2016, growth in gross domestic product in the U.S. dropped below the 2 % threshold for the year as a whole. The Latin American economy continued to contract; however, the recovering raw materials prices, among other things, are indications that the recession is coming to an end.

Growth in the Schaeffler Group's Greater China region came in at 6.3 %, once more falling behind the growth rate of the prior year. The reason for the decline was the continuing gradual slowdown in momentum in China, where gross domestic product leveled off at the 6.7 % growth rate targeted by the government.

Currency market trends No. 035

EUR against selected currencies in percent (12/31/2014 = 100)



Source: Bloomberg.

The economy in the Schaeffler Group's Asia/Pacific region grew by 3.1 %. In Japan, growth in gross domestic product was weak, while South Korea achieved a slightly higher growth rate than in the prior year. The Indonesian economy proved very dynamic.

In the currency markets, the Euro experienced a mix of trends against foreign currencies significant to the Schaeffler Group. The average rate for the year of the common European currency held its own against the U.S. Dollar. However, the Euro rose slightly against the Chinese Renminbi, the South Korean Won, the Indian Rupee, and the Mexican Peso in terms of the annual average exchange rate.

See Notes to the consolidated financial statements, chapter entitled "Summary of significant accounting policies" – "Foreign currency translation" for further detail.

Sector-specific environment

Automobile production

The global business with manufacturers of passenger cars and commercial vehicles represents the group's most important market segment. Global automobile production, measured as the number of vehicles produced, increased considerably, growing 4.8 % to approximately 93.0 million passenger cars and light commercial vehicles in 2016 (IHS, February 2017).

The Europe region grew significantly by 5.2 %. While India, Spain, France and the United Kingdom saw above-average growth, Germany expanded only slightly. The Americas region experienced a flat trend, growing by 0.2 %. While the U.S. did achieve a slight growth rate of 1.2 %, Latin America once again reported a significant decline. Automobile production in the Greater China region grew very rapidly at 13.9 %, due, among other things, to tax incentives provided by the Chinese government. The Asia/Pacific region contracted once more, with automobile production falling 2.8 % short of the prior year. The largest decline was reported by South Korea.

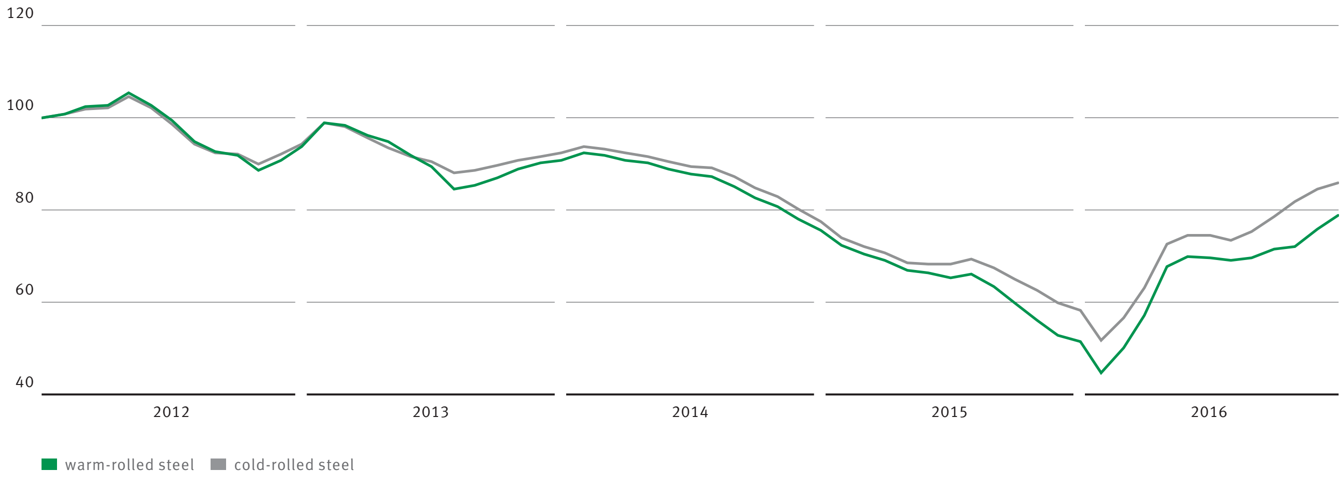
Automobile production No. 036

		Change in %	million units
Europe	2016	**5.2**	**27.9**
	2015	4.7	26.5
Americas	2016	**0.2**	**20.4**
	2015	-1.3	20.4
Greater China	2016	**13.9**	**27.3**
	2015	3.8	24.0
Asia/Pacific	2016	**-2.8**	**17.4**
	2015	-2.4	17.9
World	2016	**4.8**	**93.0**
	2015	1.6	88.7

Source: IHS (February 2017).
Regions reflect the regional structure of the Schaeffler Group.

Prices of selected steels No. 037

in percent (12/31/2011 = 100)



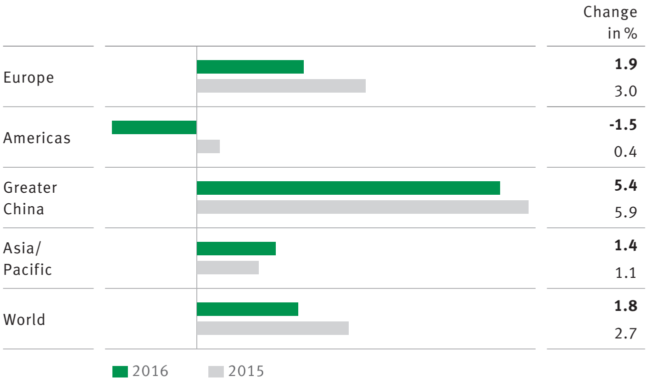
Source: Warm- and cold-rolled coil Europe from IHS ($/metric ton).

Industrial production

Preliminary figures indicate that global industrial production, measured as gross value added based on constant prices and exchange rates, grew only slightly by 1.8 % in 2016 (Oxford Economics, December 2016).

Europe region industrial production increased by 1.9 %. While Germany experienced only a slight growth rate, India reported considerable growth in industrial production. The Americas region (-1.5 %) experienced a contraction as industrial production declined below the prior year level, in the NAFTA countries as well as in Latin America. The Greater China region saw considerable growth of 5.4 %; however, this rate was once again lower than in the prior year. Industrial production in the Asia/Pacific region gained 1.4 % on the prior year, with a decline in Japan being offset by increases in South Korea, Indonesia, and Australia, among others.

Industrial production No. 038



Source: Oxford Economics (December 2016).
Real gross value added in divisions 05 to 39 of the NACE Rev. 2 system.
Regions reflect the regional structure of the Schaeffler Group.

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 generally affect the company's cost via changes in the cost to manufacturers and suppliers, which, depending on the terms of the relevant contracts, can be passed along to the Schaeffler Group to varying degrees and in some instances with some delay.

Prices in the procurement markets for all significant input materials increased during the year. However, comparing annual averages to prior year provides a mixed view.

Depending on the source region, average prices for cold- and hot-rolled steel increased by between approximately 5 to just under 20 % compared to prior year. The price of metallurgical coal, an important input material for steel and especially carbon-based castings, rose by approximately 50 %.

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. The average price of aluminum for the year declined by a good 3 %, the average copper price by just under 12 %. The price of zinc, on the other hand, was a good 6 % higher than the prior year average.

Apart from steel and non-ferrous metals, the Schaeffler Group also uses plastics and lubricants to manufacture rolling bearings and automotive components. For instance, plastics are used to produce cages for rolling bearings and lubricants are used to reduce friction in components and as preservatives. Plastics and lubricants are often made based on crude oil. Although the crude oil price increased significantly toward the end of the year due to the OPEC agreeing to limit production volumes, its annual average was still more than 10 % below 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, dropped by approximately 4 % compared to the prior year average.

2.2 Course of business

Overview of results of operations 2016

The Schaeffler Group continued moving along its successful course in 2016. Despite the uncertain market environment, the Schaeffler Group continued to grow profitably, maintained its consistently high earnings quality, and significantly increased its free cash flow. The main driver of this performance was the strong Automotive business, which grew faster than the market, i.e. global automobile production of passenger cars and light commercial vehicles. The measures to improve efficiency and reduce costs in the Industrial division were executed as planned.

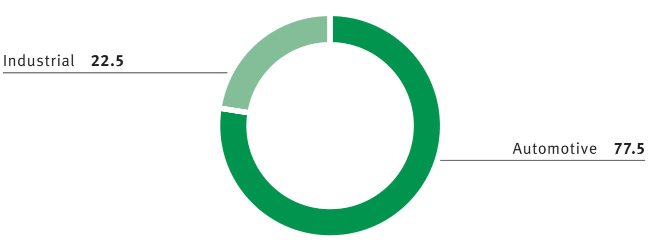
The Schaeffler Group's **revenue** increased by 1.2 % to EUR 13,338 m (prior year: EUR 13,179 m). Numerous currencies weakening against the Euro had an unfavorable effect on the company's revenue trend in 2016. Excluding the impact of currency translation, revenue rose by 3.4 %. From a regional perspective, strong demand in Greater China was the main contributor to this growth.

Automotive division revenue increased by 3.6 % to EUR 10,333 m (prior year: EUR 9,977 m) in 2016. Excluding the impact of currency translation, revenue grew by 6.0 %. Global production volumes of passenger cars and light commercial vehicles increased by 4.8 % from the prior year comparison period. Thus, the Automotive division's business outpaced the rise in global automobile production, primarily due to the increasing value of Schaeffler products installed per vehicle. The Automotive division benefitted from its strong business with customers, which was buoyed especially by the favorable trend in the Greater China region. The Aftermarket was also very successful.

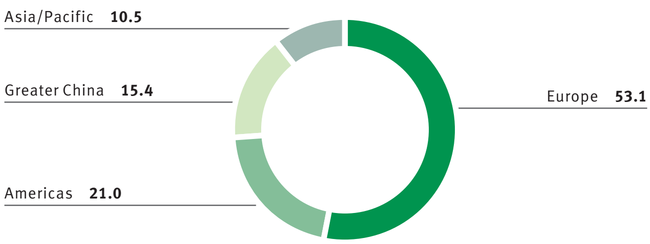
The Industrial division, on the other hand, continued to decline in a weak environment overall. Revenue decreased by 6.2 % to EUR 3,005 m (prior year: EUR 3,202 m) during the reporting period. Excluding the impact of currency translation, revenue fell by 4.8 %. The decrease affected all of the regions. The Greater China region experienced a double-digit decline in revenue, primarily due to weak investing activity in several important sectors.

The Schaeffler Group's **EBIT** grew by EUR 154 m or 11.0 % to EUR 1,556 m (prior year: EUR 1,402 m) during the reporting period, resulting in an EBIT margin of 11.7 % (prior year: 10.6 %). Before special items [3] of EUR 144 m, EBIT amounted to EUR 1,700 m (prior year: EUR 1,676 m). The company's EBIT margin before special items was 12.7 % (prior year: 12.7 %). The decline in the Industrial division's margin to 7.0 % (prior year: 9.5 %) was offset by the operating strength of the Automotive division. This division improved its EBIT margin before special items to 14.4 % (prior year: 13.8 %).

Schaeffler Group revenue by division No. 039
in percent



Schaeffler Group revenue by region No. 040
in percent by market view



[3] Please refer to page 48 for the definition of special items.

Net income increased by 44.1 % from EUR 605 m to EUR 872 m. Excluding net income attributable to non-controlling interests of EUR 13 m (prior year: EUR 14 m), net income attributable to shareholders of the parent company amounted to EUR 859 m, 45.3 % more than in the prior year (prior year: EUR 591 m). Earnings per common share amounted to EUR 1.29 (prior year: EUR 0.88). Earnings per common non-voting share amounted to EUR 1.30 (prior year: EUR 1.28) [4].

The Schaeffler Group generated **free cash flow** of EUR 735 m in 2016, EUR 365 m more than the prior year amount of EUR 370 m. The increase was driven by cash flows from operating activities, which rose from EUR 1,372 m to EUR 1,876 m mainly due to lower interest payments and changes in working capital. Capital expenditures (capex) rose from EUR 1,025 m to EUR 1,146 m (+11.8 %) or 8.6 % of revenue (prior year: 7.8 %) in 2016.

ROCE before special items was 21.7 %, slightly below the prior year (prior year: 22.5 %). An improvement in EBIT before special items for the last twelve months did not fully offset the increase in average capital employed, which was primarily driven by higher property, plant and equipment.

Significant events 2016

Schaeffler shares added to MDAX and STOXX Europe 600

On April 05, 2016, IHO Beteiligungs GmbH (until September 28, 2016: Schaeffler Verwaltungs GmbH) placed 94.4 million common non-voting Schaeffler AG shares in an accelerated bookbuild. Since this transaction was completed, 166 million common non-voting shares representing 100 % common non-voting share capital are widely held. The free float amounts to approximately 25 % of Schaeffler AG's total common and common non-voting share capital.

Due to the extensive volume of shares placed, the Schaeffler shares meet not only the high transparency requirements of the Prime Standard, but also the size criteria regarding market capitalization and liquidity that are relevant for inclusion in the MDAX index. Deutsche Börse included Schaeffler AG in its MDAX index effective June 20, 2016. In addition, STOXX Ltd., a subsidiary of Deutsche Börse AG, has included Schaeffler AG in its STOXX Europe 600 index. This change became effective as of the start of trading on September 19, 2016.

Annual general meeting passes resolution to pay a special dividend

Schaeffler AG's first annual general meeting since the listing, which was held on April 22, 2016, passed a resolution to pay a dividend of EUR 0.34 per common share and EUR 0.35 per common non-voting share to Schaeffler AG's shareholders for 2015. This represents a dividend of 28.9 % of net income attributable to shareholders before special items. In addition, the company paid a special dividend of EUR 0.15 per common share and per common non-voting share for 2015.

Capital structure improved

In connection with the successful refinancing transaction completed at the level of IHO Holding, a group of holding companies owned indirectly by the Schaeffler family, rating agency Moody's upgraded Schaeffler AG's company rating to Baa3 (investment grade) on September 07, 2016. Schaeffler AG received approximately EUR 1.7 bn when its loan receivable from IHO Holding was prepaid in connection with the refinancing transaction. As a result, Schaeffler AG has achieved its objective of reducing its debt to EBITDA ratio (net debt in relation to EBITDA before special items) to less than 1.5x by 2018 two years ahead of schedule and significantly increased its financial flexibility. The proceeds of the loan prepayment referred to above were used to redeem one USD-denominated bond series and two EUR-denominated bond series in October 2016.

Program "CORE"

On November 07, 2016, the Board of Managing Directors of Schaeffler AG decided to step up its efficiency measures aimed at revitalizing the Industrial division. Following the first wave of cost reduction measures comprising the program "CORE", which focus on Germany and have largely been implemented, the second wave of measures initiated in November 2016 also covers regions outside of Germany as well as functional areas that are not directly part of the Industrial division. The measures are designed to improve the results of the entire Industrial division for the long-term by further streamlining its structure and reducing production and administrative costs.

See chapter entitled "Business activities" – Divisions for further detail.

Strategy "Mobility for tomorrow"

On November 09, 2016, Schaeffler AG presented its strategy "Mobility for tomorrow" to the public; the strategy was developed over the course of 2016 and was approved by the Board of Managing Directors and the Supervisory Board.

[4] Earnings per share were calculated in accordance with IAS 33. As the common non-voting shares newly issued in October 2015 (66 million shares) participated in profits for the entire year 2015, earnings per common non-voting share for 2015 were calculated using proportionate net income based on 166 million common non-voting shares.

Based on 4 significant megatrends and the resulting Focus Areas (1) eco-friendly drives, (2) urban mobility, (3) interurban mobility, and (4) energy chain, Schaeffler has defined the other elements of its strategy “Mobility for tomorrow”. These elements consist of 8 Strategic Pillars defining the company’s scope for strategic action over the years to come, the excellence program “Agenda 4 plus One” comprising 16 Strategic Initiatives that will help execute the strategy, and the Financial Ambitions 2020.

For further detail on the strategy “Mobility for tomorrow” at: www.schaeffler.com

See chapter entitled “Group strategy and management” for further detail.

Business portfolio adjusted

Following the successful realignment of its capital structure and its renewed financial flexibility resulting from the reduced level of debt, the Schaeffler Group will no longer rely only on purely organic growth. The company will generally focus on acquisitions related to the future-oriented fields of E-Mobility, Industry 4.0, and digitalization.

In this vein, Schaeffler acquired electric motor manufacturer Compact Dynamics GmbH from SEMIKRON International GmbH at the end of 2016 with a view to strengthening the company’s expertise in order to expand its E-mobility activities. Compact Dynamics GmbH based in Starnberg, Germany, 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. At the same time, Schaeffler and SEMIKRON agreed to cooperate on developing power electronics systems and integrating power electronics components. The acquisition and the collaboration expand Schaeffler’s expertise in the field of electric motors and power electronics for developing and manufacturing electric drives, opening up new opportunities for growth. On the other hand, Schaeffler has proactively streamlined its production portfolio by disposing of its fine blanking activities in Switzerland and selling Schaeffler Motorenelemente AG & Co. KG in Magdeburg.

Changes in Board membership

At its meeting on March 11, 2016, Schaeffler AG’s Supervisory Board appointed Matthias Zink to the Board of Managing Directors of Schaeffler AG and the position of Co-CEO of the Automotive division effective January 01, 2017. Matthias Zink will succeed Norbert Indlekofer, whose contract was not extended at his own request. The Supervisory Board also decided to extend the contract of Prof. Dr. Peter Pleus, also Co-CEO of the Automotive division, by a further two years until December 31, 2018.

Results of operations compared to outlook 2016

The Schaeffler Group has achieved its outlook for 2016.

Comparison to outlook 2016 No. 041

	Actual 2015	Outlook 2016	Actual 2016
Revenue growth compared with prior year [1]	3.5 %	3 to 5 %	3.4 %
EBIT margin before special items	12.7 %	12 to 13 %	12.7 %
Free cash flow	EUR 370 m	~ EUR 600 m	EUR 735 m

[1] Excluding the impact of currency translation.

The Schaeffler Group had issued guidance regarding revenue growth of 3 to 5 % for 2016, excluding the impact of currency translation. This guidance was based on the expectation that its Automotive division would continue to grow faster than global automobile production of passenger cars and light commercial vehicles in 2016. The company also assumed that its Industrial division would experience flat or slightly declining revenue levels in 2016, as the economic environment in certain sectors was still strained. Excluding the impact of currency translation, the Schaeffler Group’s revenue grew by 3.4 % in 2016. Thus, Schaeffler has met its revenue target for 2016. Excluding the impact of currency translation, the Automotive division increased its revenue by 6.0 % from 2015, outpacing the global production of passenger cars and light commercial vehicles which grew by 4.8 % in 2016. The Industrial division, on the other hand, reported a decline in revenue of 4.8 % in 2016, excluding the impact of currency translation.

The Schaeffler Group generated an EBIT margin before special items of 12.7 % in 2016. Thus, the return for 2016 remained high, falling in the top third of the range of 12 to 13 % contained in the outlook.

Free cash flow for 2016 amounted to EUR 735 m, considerably higher than the outlook for 2016 of approximately EUR 600 m. The reason was improved cash flow from operations.

Schaeffler Group

Revenue EUR 13,338 m

EBIT margin before special items 12.7 %

Group continued along successful course in 2016 // Revenue and operating results increased once more compared to prior year // Revenue growth 3.4 % at constant currency // EBIT before special items at EUR 1.7 bn // Strong year for Automotive division; Industrial division earnings declined // R&D activities for electric mobility expanded considerably

Schaeffler Group earnings No. 042

in € millions	2016	2015	Change in %
Revenue	**13,338**	**13,179**	**1.2**
• at constant currency			3.4
Revenue by division			
Automotive	10,333	9,977	3.6
• at constant currency			6.0
Industrial	3,005	3,202	-6.2
• at constant currency			-4.8
Revenue by region 1)			
Europe	7,077	7,027	0.7
• at constant currency			1.8
Americas	2,800	2,901	-3.5
• at constant currency			0.1
Greater China	2,053	1,898	8.2
• at constant currency			13.3
Asia/Pacific	1,408	1,353	4.1
• at constant currency			4.7
Cost of sales	-9,552	-9,448	1.1
Gross profit	**3,786**	**3,731**	**1.5**
• in % of revenue	28.4	28.3	-
Research and development expenses	-751	-673	11.6
Selling expenses	-915	-920	-0.5
Administrative expenses	-428	-407	5.2
Earnings before financial result and income taxes (EBIT)	**1,556**	**1,402**	**11.0**
• in % of revenue	11.7	10.6	-
Special items 2)	144	274	-47.4
EBIT before special items	**1,700**	**1,676**	**1.4**
• in % of revenue	12.7	12.7	-
Financial result	-341	-547	-37.7
Income taxes	-343	-250	37.2
Net income 3)	859	591	45.3
Earnings per common non-voting share (basic/diluted, in €) 4)	1.30	1.28	1.6

1) Based on market (customer location).
2) Please refer to page 48 for the definition of special items.
3) Attributable to shareholders of the parent company.
4) Earnings per share were calculated in accordance with IAS 33.

2.3 Earnings

Schaeffler Group earnings

Revenue grew by 1.2 % to EUR 13,338 m in 2016 (prior year: EUR 13,179 m). Excluding the impact of currency translation, revenue grew by 3.4 %. The Automotive division contributed revenue growth of 6.0 % excluding the impact of currency translation, exceeding global growth in the production of passenger cars and light commercial vehicles of 4.8 %. The Industrial division, on the other hand, reported a decline in revenue of 4.8 % excluding the impact of currency translation.

Revenue in Schaeffler's Europe region was up by 0.7 % (+1.8 % at constant currency), with the added revenue in the Automotive division more than offsetting a slight decline in Industrial division revenue. The Americas region reported a drop in revenue of 3.5 %, (+0.1 % at constant currency). Considerably lower Industrial revenue in the U.S., primarily attributable to weak momentum in oil and gas production, held back this region's revenue. The revenue trend in the Greater China and Asia/Pacific regions remained positive. These regions' revenue increased by a total of 8.2 % (+13.3 % at constant currency) in Greater China and 4.1 % (+4.7 % at constant currency) in Asia/Pacific, despite the adverse impact of currency translation and a significant decline in the Industrial division.

Cost of sales increased by 1.1 % to EUR 9,552 m (prior year: EUR 9,448 m) in 2016. Gross profit improved by 1.5 % or EUR 55 m to EUR 3,786 m (prior year: EUR 3,731 m) and, consequently, gross margin of 28.4 % (prior year: 28.3 %) came in slightly above the prior year level. The Automotive division gross margin increased by 0.7 % to 28.5 % (prior year: 27.8 %), while the Industrial division's gross margin fell 2.2 percentage points to 27.8 % (prior year: 30.0 %).

Research and development expenses increased significantly by 11.6 % to EUR 751 m in 2016 (prior year: EUR 673 m) which represents an R&D ratio of 5.6 % (prior year: 5.1 %) of revenue. Apart from inflation-related cost increases, the increase is primarily attributable to a focused expansion of the headcount in connection with the strategic direction of the research and development activities of the Automotive division, as a result of, among other things, stepped-up activities in the field of E-mobility.

Research and development expenses No. 043

	2012	2013	2014	2015	2016
Research and development expenses (in € millions)	593	611	622	673	751
Research and development expenses (in % of revenue)	5.3 %	5.5 %	5.1 %	5.1 %	5.6 %
Number of research and development staff [1]	6,098	6,039	6,387	6,650	7,121

[1] Averages.

Selling and administrative expenses of EUR 1,343 m were slightly above prior year (prior year: EUR 1,327 m). Total functional costs rose by 4.7 % to EUR 2,094 m (prior year: EUR 2,000 m), growing to 15.7 % of revenue (prior year: 15.2 %).

EBIT increased by EUR 154 m or 11.0 % to EUR 1,556 m (prior year: EUR 1,402 m) during the reporting period. The Schaeffler Group's EBIT margin was 11.7 % (prior year: 10.6 %). In 2016, the Schaeffler Group's EBIT was adversely affected by EUR 144 m in special items (prior year: EUR 274 m), including EUR 86 m in special items for legal cases resulting from provisions for claims for damages in antitrust cases and for other compliance cases. In addition, the company recognized restructuring expenses of EUR 45 m for the stepped-up efficiency measures aimed at revitalizing the Industrial division – as part of the second wave of the program "CORE" – in 2016. Streamlining the production portfolio resulted in other special items of EUR 13 m. Prior year EBIT had been adversely affected by a EUR 238 m provision for legal cases recognized for potential third party claims in connection with the EU antitrust proceedings finalized in March 2014. In addition, prior year earnings were adversely affected by EUR 36 m in restructuring expenses related to the realignment of the Industrial division. The company's EBIT before special items amounted to EUR 1,700 m (prior year: EUR 1,676 m) in 2016, and its EBIT margin to 12.7 % (prior year: 12.7 %). An improvement in Automotive division gross margin more than offset the market-driven decline in the Industrial division's return as well as higher research and development expenses.

The Schaeffler Group's financial result improved by EUR 206 m to EUR -341 m (prior year: EUR -547 m) in 2016, and included EUR 158 m (prior year: EUR 196 m) in one-time charges incurred in connection with refinancing transactions in 2016.

Schaeffler Group financial result No. 044

in € millions	2016	2015
Interest expense on financial debt [1)]	-286	-513
Interest income on shareholder loans	49	72
Foreign exchange gains and losses	-12	-224
Fair value changes and compensation payments on derivatives	-21	234
Fair value changes on embedded derivatives	-30	-79
Interest income and expense on pensions and partial retirement obligations	-45	-42
Other	4	5
Total	**-341**	**-547**

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

Interest expense on financial debt amounted to EUR 286 m in 2016 (prior year: EUR 513 m) and includes EUR 48 m in prepayment penalties and EUR 31 m in deferred transaction costs derecognized. Please refer to the chapter entitled "Financial debt" for further detail. The prior year amount included a prepayment penalty of EUR 173 m and EUR 23 m in deferred transaction costs derecognized in connection with the early redemption of bonds.

Interest income on loans to a shareholder, IHO Verwaltungs GmbH (until September 27, 2016: Schaeffler Verwaltung Zwei GmbH), was EUR 49 m (prior year: EUR 72 m).

Net foreign exchange losses on financial assets and liabilities amounted to EUR 12 m (prior year: EUR 224 m) and resulted primarily from translating financing instruments denominated in U.S. Dollar to Euro. The company has hedged these instruments using cross-currency derivatives and has reported the resulting losses of EUR 21 m (prior year: gains of EUR 234 m) under fair value changes and compensation payments on derivatives. The losses largely related to the early termination of cross-currency derivatives.

Changes in the fair value of embedded derivatives, primarily prepayment options for external financing instruments, resulted in net losses of EUR 30 m (prior year: EUR 79 m), including EUR 79 m in losses related to prepayment options written off in connection with the refinancing transactions in 2016, partially offset by EUR 49 m in gains resulting from changes in the fair value of the remaining prepayment options.

Income tax expense amounted to EUR 343 m in 2016 (prior year: EUR 250 m), resulting in an effective tax rate of 28.2 % (prior year: 29.2 %)

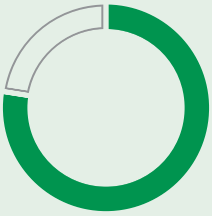
Net income attributable to shareholders of the parent company for 2016 was EUR 859 m (prior year: EUR 591 m). Net income before special items amounted to EUR 962 m (prior year: EUR 785 m). The Board of Managing Directors and the Supervisory Board will propose a dividend for 2016 of EUR 0.49 (prior year: EUR 0.34; special dividend EUR 0.15) per common share and EUR 0.50 (prior year: EUR 0.35; special dividend EUR 0.15) per common non-voting share to the annual general meeting. This represents a dividend of 34.1 % (prior year: 28.9 %) of net income attributable to shareholders before special items.

Basic and diluted earnings per common share increased to EUR 1.29 (prior year: EUR 0.88) in 2016. Basic and diluted earnings per common non-voting share amounted to EUR 1.30 (prior year: EUR 1.28). 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: 116 million), respectively. [5]

[5] Earnings per share were calculated in accordance with IAS 33. As the common non-voting shares newly issued in October 2015 (66 million shares) participated in profits for the entire year 2015, earnings per common non-voting share for all of 2015 were calculated using proportionate net income based on 166 million common non-voting shares.

Automotive division

Revenue EUR 10,333 m



77.5 %
of group revenue

EBIT margin before special items 14.4 %

Profitable growth continued – both revenue and operating results before special items increased further // Revenue increased by 6.0 % at constant currency // Growth outpaces increase in global production volumes of passenger cars and light commercial vehicles // Revenue growth in all business divisions – strong Aftermarket business // R&D activities for electric mobility expanded considerably

Automotive division earnings No. 045

in € millions	2016	2015	Change in %
Revenue	**10,333**	**9,977**	**3.6**
• at constant currency			6.0
Revenue by business division			
BD Engine Systems	2,643	2,596	1.8
• at constant currency			3.3
BD Transmission Systems	4,349	4,211	3.3
• at constant currency			5.6
BD Chassis Systems	1,531	1,465	4.5
• at constant currency			6.3
BD Automotive Aftermarket	1,810	1,705	6.2
• at constant currency			10.8
Revenue by region [1]			
Europe	5,304	5,211	1.8
• at constant currency			2.9
Americas	2,238	2,301	-2.7
• at constant currency			1.3
Greater China	1,675	1,420	18.0
• at constant currency			24.3
Asia/Pacific	1,116	1,045	6.8
• at constant currency			7.3
Cost of sales	-7,383	-7,206	2.5
Gross profit	**2,950**	**2,771**	**6.5**
• in % of revenue	28.5	27.8	-
Research and development expenses	-613	-536	14.4
Selling and administrative expenses	-828	-814	1.7
EBIT	**1,383**	**1,135**	**21.9**
• in % of revenue	13.4	11.4	-
Special items [2]	108	238	-54.6
EBIT before special items	**1,491**	**1,373**	**8.6**
• in % of revenue	14.4	13.8	-

Prior year information presented based on 2016 segment structure.
[1] Based on market (customer location).
[2] Please refer to page 48 for the definition of special items.

Automotive division earnings

Automotive division revenue increased by 3.6 % to EUR 10,333 m (prior year: EUR 9,977 m) in 2016. At constant currency, the growth rate was 6.0 %. Thus, the business once again expanded faster than global production volumes for passenger cars and light commercial vehicles, which grew by 4.8 % in 2016. The growth rate in excess of the rise in global automobile production was primarily due to an increase in the value of Schaeffler products installed per vehicle. From a regional perspective, the positive revenue trend was primarily attributable to double-digit growth in Greater China. The Aftermarket was also very successful.

Overall, revenue trends varied widely across market regions in 2016. The Europe region reported 1.8 % (+2.9 % at constant currency) in additional revenue, slightly less than average regional growth in production volumes (+5.2 %). The Americas region reported a decline in revenue of 2.7 % for the reporting period due to the adverse impact of currency translation. The region's revenue increased slightly by 1.3 % at constant currency while automobile production remained flat with prior year. The Automotive division once again significantly expanded its revenue in the Greater China region, mainly as a result of product ramp-ups and higher demand driven by tax incentives provided by the Chinese government. The Automotive division generated 18.0 % (+24.3 % at constant currency) in additional revenue in Greater China while regional vehicle production increased by 13.9 %. The reasons for the increase in Asia/Pacific region revenue by 6.8 % (+7.3 % at constant currency) included product ramp-ups, with vehicle production there declining by 2.8 %.

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 2016.

The **Engine Systems BD** generated revenue growth of 1.8 % (+3.3 % at constant currency) during the year. This growth was primarily buoyed by the start of volume production of the electromechanical camshaft phasing system within the camshaft phasing units product group. The accessory drive product group and the innovative thermal management module, which helps reduce fuel consumption and CO_2 emissions, also generated considerable additional revenue. Fully variable valve train systems (predominantly Multiair), on the other hand, experienced a significant decline in revenue, primarily as a result of the main customer in North America requiring less volume of this product due to shifts in product mix.

Transmission Systems BD revenue rose by 3.3 % (+5.6 % at constant currency), driven by higher volumes in the dual-mass flywheel product group and for components for automated transmissions, such as torque converters and dual clutches. In addition, the Automotive division also significantly increased sales of clutches and gearing components used in manual transmissions. On the other hand, continuously variable transmissions (CVT) declined, mainly due to the end of a project.

The **Chassis Systems BD** generated revenue growth of 4.5 % (+6.3 % at constant currency) mainly based on the solid performance of the newest generation of wheel bearings, highly integrated units containing mounting brackets for the brake disk, rim, and wheel carrier that ensure top running accuracy. Volume production of the electromechanical active roll control also considerably increased revenue in the chassis actuators product group.

The **Automotive Aftermarket BD** increased revenue by 6.2 % (+10.8 % at constant currency) in 2016. The increase was primarily due to higher sales in the Americas and Europe regions. Reasons for the additional revenue in Americas included increased requirements of automobile manufacturers (OES customers). In Europe, business expanded particularly in Eastern Europe as well as in Southern and Western Europe. The higher revenue was primarily attributable to increased market coverage.

Cost of sales increased by 2.5 % to EUR 7,383 m (prior year: EUR 7,206 m) in 2016. In total, the Automotive division improved its gross profit by EUR 179 m or 6.5 % to EUR 2,950 m (prior year: EUR 2,771 m). The division's gross margin of 28.5 % was ahead of the prior year period (prior year: 27.8 %). The Automotive division has thus continued its profitable growth, more than offsetting cost increases, primarily due to collectively bargained wage and salary increases, and the adverse impact of foreign currency translation with the favorable impact of higher volumes and a better revenue mix as well as lower raw materials costs.

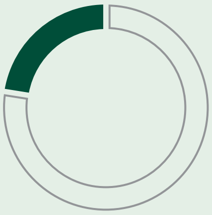
Functional costs increased 6.7 % to EUR 1,441 m (prior year: EUR 1,350 m), rising slightly to 13.9 % of revenue (prior year: 13.5 %). The main driver of this increase was the rise in research and development expenses by 14.4 % to EUR 613 m (prior year: EUR 536 m) or 5.9 % (prior year: 5.4 %) of revenue, reflecting increased activities in the field of electric mobility, which has already won several volume production orders. Selling and administrative expenses of EUR 828 m were slightly ahead of prior year (+1.7 %; prior year: EUR 814 m).

Automotive division EBIT grew by 21.9 % to EUR 1,383 m (prior year: EUR 1,135 m) during the reporting period, and its EBIT margin increased to 13.4 % (prior year: 11.4 %). In 2016, EBIT was adversely affected by EUR 108 m in special items (prior year: EUR 238 m), including EUR 82 m in special items for legal cases resulting from provisions for claims for damages in antitrust cases and other compliance cases. In addition, the division recognized EUR 13 m in restructuring expenses affecting the Automotive division as part of the second wave of the program "CORE" (consolidation of shared functions and plant structures). Streamlining the production portfolio resulted in other special items of EUR 13 m. Prior year EBIT had been adversely affected by a EUR 238 m provision for legal cases recognized for potential third party claims in connection with the EU antitrust proceedings finalized in March 2014. EBIT before special items increased by EUR 118 m to EUR 1,491 m (prior year: EUR 1,373 m), improving the division's EBIT margin by 0.6 percentage points to 14.4 % (prior year: 13.8 %). The increase in EBIT margin before special items was due to the favorable impact of higher volumes and a better revenue mix, partially offset mainly by higher research and development expenses and the adverse impact of currency translation.

Industrial division

Revenue EUR 3,005 m

22.5 %
of group revenue



EBIT margin before special items 7.0 %

Market environment remains strained // Revenue declined by 4.8 % at constant currency // Considerably lower demand in the Greater China region // Low demand, especially in the raw materials and rail sectors // Operating results still adversely affected by low sales volume // EBIT before special items at EUR 209 m // Efficiency and cost saving measures executed as planned // Second wave of program "CORE" initiated

Industrial division earnings No. 046

in € millions	2016	2015	Change in %
Revenue	**3,005**	**3,202**	**-6.2**
• at constant currency			-4.8
Revenue by region [1]			
Europe	1,773	1,816	-2.4
• at constant currency			-1.3
Americas	562	600	-6.3
• at constant currency			-4.6
Greater China	378	478	-20.9
• at constant currency			-18.8
Asia/Pacific	292	308	-5.2
• at constant currency			-4.1
Cost of sales	-2,169	-2,242	-3.3
Gross profit	**836**	**960**	**-12.9**
• in % of revenue	27.8	30.0	-
Research and development expenses	-138	-137	0.7
Selling and administrative expenses	-515	-513	0.4
EBIT	**173**	**267**	**-35.2**
• in % of revenue	5.8	8.3	-
Special items [2]	36	36	0.0
EBIT before special items	**209**	**303**	**-31.0**
• in % of revenue	7.0	9.5	-

Prior year information presented based on 2016 segment structure.
[1] Based on market (customer location).
[2] Please refer to page 48 for the definition of special items.

Industrial division earnings

Industrial division revenue decreased by 6.2 % to EUR 3,005 m (prior year: EUR 3,202 m) in 2016. Excluding the impact of currency translation, the division reported a revenue decline of 4.8 %.

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. Within the regions, the Industrial business is grouped into eight sectors: wind, raw materials, aerospace, rail, offroad, two wheelers, power transmission, and industrial automation. Sales to distributors (Industrial Distribution) round out the Industrial division's regional business.

The market environment of the Industrial division remained strained in 2016. Commodity and oil prices remained relatively low, weakening demand on the customer side and, in turn, adversely affecting the performance of the raw materials and power transmission sectors to a significant degree. Sharp revenue declines in the rail sector also had an adverse effect on the division's revenue trend. Although Industrial Distribution revenue recovered slightly over the course of 2016, it still lagged considerably behind the prior year for the reporting period as a whole. The offroad and industrial automation sectors also reported slightly lower revenue. However, revenue in the division's wind, two wheelers, and aerospace sectors increased.

Revenue in Schaeffler's **Europe region** fell by 2.4 % (-1.3 % at constant currency). Revenue trends varied widely across individual sectors. The raw materials sector business reported considerably lower revenue due to weak market conditions. The rail and power transmission sectors as well as Industrial Distribution similarly reported considerably lower revenue than in the prior year. The offroad and industrial automation sectors were nearly in line with prior year. However, revenue in the wind, two wheelers, and aerospace sectors generated considerable revenue increases. The wind and aerospace sectors generated double-digit growth rates excluding the impact of currency translation.

In the **Americas region**, revenue declined by 6.3 % (-4.6 % at constant currency). This trend was primarily driven by double-digit declines in revenue in the raw materials, rail, and power transmission sectors. These declines are related to the challenging situation in the U.S. markets for these sectors, particularly in the oil and gas industry. Despite recovering somewhat during the year, revenue for the industrial automation sector as well as for Industrial Distribution still fell short of its prior year level. Aerospace sector revenue at constant currency, on the other hand, was almost in line with prior year, and offroad sector revenue rose slightly, excluding the impact of currency translation. The wind and two wheelers sectors generated double-digit growth rates excluding the impact of currency translation.

The **Greater China region** reported a considerable drop in revenue of 20.9 % (-18.8 % at constant currency). Except for the wind sector, which reported only a minor decline in revenue, all significant sectors as well as Industrial Distribution saw double-digit declines in revenue due to weak market requirements, reduced investing activity, and the resulting pressure on market prices.

The decrease in revenue for the **Asia/Pacific region** by 5.2 % (-4.1 % at constant currency) was primarily attributable to Industrial Distribution and the raw materials sector. The aerospace, two wheelers, and industrial automation sectors, on the other hand, reported slightly higher revenue.

Industrial division cost of sales decreased by 3.3 % to EUR 2,169 m (prior year: EUR 2,242 m). Gross profit declined by EUR 124 m or 12.9 % to EUR 836 m (prior year: EUR 960 m) and, consequently, gross margin fell by 2.2 percentage points to 27.8 % (prior year: 30.0 %). The decrease was attributable to lower volumes, the resulting lower utilization of production capacities, and a less profitable revenue mix. However, lower raw materials prices had a positive effect on gross margin.

Functional costs of EUR 653 m (prior year: EUR 650 m) in 2016 were in line with prior year. The cost reduction measures of the program "CORE" approximately offset inflation-related increases in costs, particularly in personnel expenses. Functional costs as a percentage of revenue rose to 21.7 % (prior year: 20.3 %). Research and development expenses amounted to EUR 138 m (prior year: EUR 137 m), and selling and administrative expenses were EUR 515 m (prior year: EUR 513 m).

Industrial division EBIT declined to EUR 173 m (prior year: EUR 267 m) in 2016. The division's EBIT margin deteriorated to 5.8 % (prior year: 8.3 %). In 2016, the division's EBIT was adversely affected by EUR 36 m in special items (prior year: EUR 36 m), 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 recognized EUR 4 m in expenses for legal cases in 2016. This compares to EUR 36 m in restructuring expenses recognized in the prior year for the realignment of the Industrial division. The division's EBIT before special items amounted to EUR 209 m (prior year: EUR 303 m) in 2016, and its EBIT margin was 7.0 % (prior year: 9.5 %). The decrease in EBIT was primarily due to the adverse impact of lower volumes and a less favorable revenue mix.

Performance indicators and special items

EBIT, EBITDA, debt to EBITDA ratio, ROCE, and Schaeffler Value Added and the corresponding amounts before special items are indicators that are not defined in International Financial Reporting Standards (IFRS). Therefore, these indicators should be considered supplementary information.

The key indicators used in evaluating the company's operations are EBIT and the EBIT margin. In addition, the company calculates EBITDA, which represents EBIT before amortization of intangible assets, depreciation of property, plant and equipment, and impairment losses. EBITDA is primarily used to calculate the 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 return on capital employed (ROCE) as well as Schaeffler Value Added, which is closely linked to ROCE. ROCE corresponds to EBIT in relation to average capital employed. Average capital employed is 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. Schaeffler Value Added is calculated as EBIT less the cost of capital. 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.

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. 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 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.

In 2016, special items relate primarily to issues in the categories legal cases, restructuring, and other.

Reconciliation No. 047

	Total		Automotive		Industrial	
in € millions	2016	2015	2016	2015	2016	2015
EBIT	**1,556**	**1,402**	**1,383**	**1,135**	**173**	**267**
• in % of revenue	11.7	10.6	13.4	11.4	5.8	8.3
Special items	**144**	**274**	**108**	**238**	**36**	**36**
• Legal cases	86	238	82	238	4	0
• Restructuring	45	36	13	0	32	36
• Other	13	0	13	0	0	0
EBIT before special items	**1,700**	**1,676**	**1,491**	**1,373**	**209**	**303**
• in % of revenue	12.7	12.7	14.4	13.8	7.0	9.5
EBITDA	**2,293**	**2,096**				
Special items	**144**	**274**				
• Legal cases	86	238				
• Restructuring	45	36				
• Other	13	0				
EBITDA before special items	**2,437**	**2,370**				
Net income [1]	**859**	**591**				
Special items	**144**	**274**				
• Legal cases	86	238				
• Restructuring	45	36				
• Other	13	0				
– Tax effect [2]	-41	-80				
Net income before special items [1]	**962**	**785**				
Net financial debt	2,636	4,889				
/ EBITDA	2,293	2,096				
Debt to EBITDA ratio	**1.1**	**2.3**				
Net financial debt	2,636	4,889				
/ EBITDA before special items	2,437	2,370				
Debt to EBITDA ratio before special items	**1.1**	**2.1**				
EBIT	1,556	1,402				
/ Average capital employed	7,848	7,455				
ROCE (in %)	**19.8**	**18.8**				
EBIT before special items	1,700	1,676				
/ Average capital employed	7,848	7,455				
ROCE before special items (in %)	**21.7**	**22.5**				
EBIT	1,556	1,402				
– Cost of capital	785	745				
Schaeffler Value Added	**771**	**657**				
EBIT before special items	1,700	1,676				
– Cost of capital	785	745				
Schaeffler Value Added before special items	**915**	**931**				

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

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.

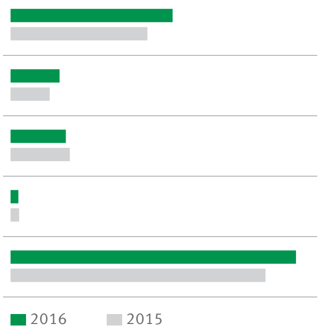
Cash flow No. 048

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.

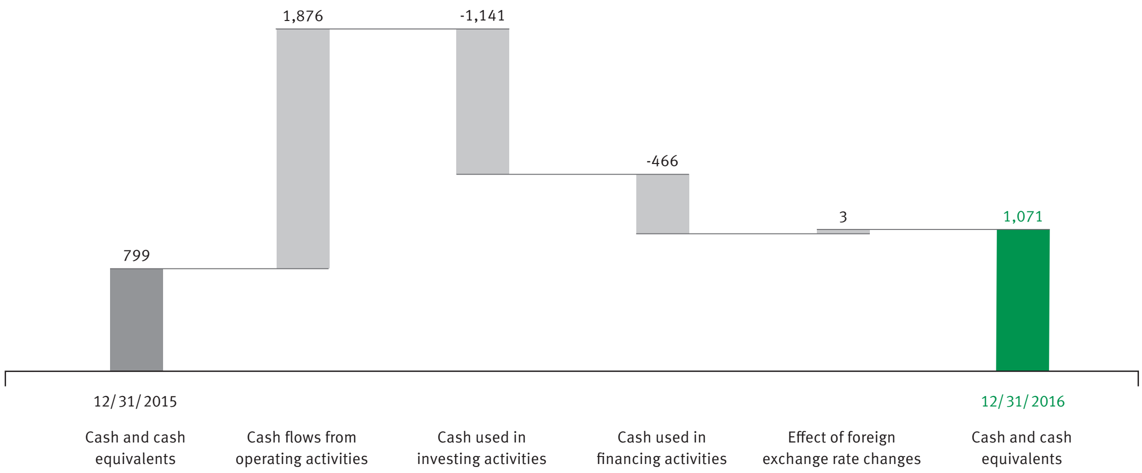
These developments resulted in free cash flow of EUR 735 m (prior year: EUR 370 m) for 2016.

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	Face value in millions 12/31/2016	Face value in millions 12/31/2015	Carrying amount in € millions 12/31/2016	Carrying amount in € millions 12/31/2015	Coupon 12/31/2016	Coupon 12/31/2015	Maturity
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 12/31/2016	Face value in millions 12/31/2015	Carrying amount in € millions 12/31/2016	Carrying amount in € millions 12/31/2015	Coupon	Maturity
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**		

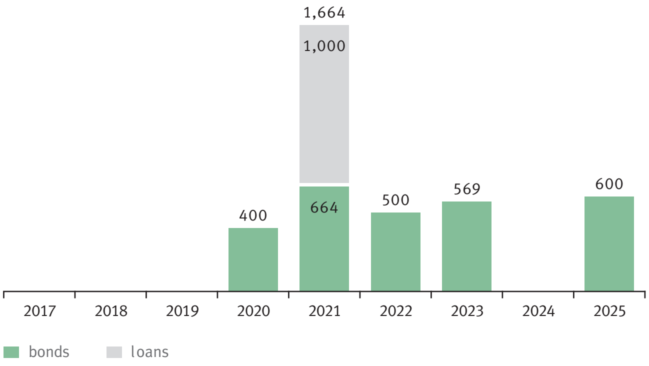
1) Redeemed in full on August 18, 2016.
2) Bonds are unsecured.
3) Redeemed in full on October 13, 2016.
4) Redeemed in full on October 07, 2016.

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:

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 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.

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.

Shareholders' equity including non-controlling interests rose by EUR 429 m to EUR 1,997 m as at December 31, 2016 (prior year: EUR 1,568 m). Net income of EUR 872 m increased shareholders' equity. The increase was partially offset by EUR 328 m in dividends paid to Schaeffler AG's shareholders. Shareholders' equity was also reduced by an increase in provisions for pensions and similar obligations due to the reduction in the average discount rate to 2.1 % (December 31, 2015: 2.6 %). The equity ratio was 17.3 % at December 31, 2016 (December 31, 2015: 12.6 %).

Non-current liabilities declined by EUR 1,783 m to EUR 6,361 m as at December 31, 2016 (prior year: EUR 8,144 m), largely due to the redemption in full of a USD bond series with a principal of USD 850 m and two EUR bond series with a principal of EUR 500 m each completed in October 2016. The redemptions were largely funded using the proceeds of the prepayment in full of a loan receivable from the company's shareholder IHO Verwaltungs GmbH as discussed above. Voluntary partial prepayments of institutional loan tranches during the first half of 2016 also reduced non-current financial debt. These decreases were partially offset by an increase in provisions for pensions and similar obligations by EUR 240 m, mainly as a result of lower discount rates.

Current liabilities increased by EUR 438 m to EUR 3,206 m as at December 31, 2016 (prior year: EUR 2,768 m). The increase was largely attributable to higher trade payables and higher other financial liabilities.

The Schaeffler Group's significant off-balance sheet commitments include obligations under operating rental and lease agreements and contingent liabilities. The Schaeffler Group's obligations under non-cancellable operating rental and lease agreements totaled EUR 123 m at December 31, 2016 (prior year: EUR 126 m); obligations under finance leases were insignificant.

2.6 Value management

Ensuring that the Schaeffler Group continues to meet its core business objective of growing profitably in the long-term necessitates a value-based approach to managing its business portfolio. The Schaeffler Group's key value-based performance indicator is return on capital employed (ROCE) as well as Schaeffler Value Added, which is closely linked to ROCE. Neither indicator is directly used in managing the Schaeffler Group's operations, although 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.

See section "Group strategy and management" – "Value-based management" for further detail.

Positive Schaeffler Value Added means that the Schaeffler Group's EBIT exceeds the cost of capital for the period and has added the corresponding amount in value. 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.

While Schaeffler Value Added is an absolute measure of the value added by the company, return on capital employed – the ratio of EBIT to capital employed – measures the Schaeffler Group's return on capital. Both indicators are determined before special items.

ROCE and Schaeffler Value Added — No. 056

	12/31/2016	12/31/2015
EBIT (in EUR m)	1,556	1,402
EBIT before special items (in € millions)	1,700	1,676
Capital employed (in € millions)	7,848	7,455
Cost of capital (in %)	10.0	10.0
Cost of capital (in € millions)	785	745
ROCE (in %)	19.8	18.8
ROCE before special items (in %)	**21.7**	**22.5**
Schaeffler Value Added (in € millions)	771	657
Schaeffler Value Added before special items (in € millions)	**915**	**931**

2.7 Overall assessment of the 2016 business year

The Board of Managing Directors looks back on a successful year 2016. Schaeffler achieved its targets for the three key performance indicators growth, EBIT margin, and free cash flow. The group's revenue growth excluding the impact of currency translation of 3.4 % was within the target corridor of 3 to 5 %. The EBIT margin before special items amounted to 12.7 %, reaching the top third of the targeted range of 12 to 13 %. Free cash flow of EUR 735 m considerably exceeded the target of approximately EUR 600 m.

This encouraging development of the key performance indicators was primarily driven by the strong performance of the Automotive division. This division benefitted from favorable overall conditions in the automotive industry which exceeded expectations, especially in China. In addition, revenue growth in the Automotive division of 6.0 % (at constant currency) outpaced growth in global automobile production. The Automotive EBIT margin before special items increased once again, reaching a very encouraging level of more than 14 %.

The Industrial division, on the other hand, continued to face a challenging market environment marked by declining demand in important sectors, particularly in China. Industrial division revenue declined by 4.8 % excluding the impact of currency translation in 2016. Its EBIT margin before special items declined as well, falling short of the division's plan for 2016 at 7.0 %. Achieving the targeted return for 2018 of 10 to 11 % will be challenging. In light of this, the Board of Managing Directors of Schaeffler AG decided in 2016 to step up its measures for revitalizing the Industrial division – in a second wave of the program "CORE" – in order to put the Industrial division, an integral component of the Schaeffler Group, back on course for long-term success. The measures to improve efficiency and reduce costs initiated in the first wave of the program "CORE" were executed as planned.

In addition, the Board of Managing Directors, cooperating closely with the Schaeffler Group's senior management and the Schaeffler AG Supervisory Board, finalized its strategy discussions and approved the strategy "Mobility for tomorrow" and the "Agenda 4 plus One" excellence program in October 2016. The strategy "Mobility for tomorrow" was backed with ambitious medium-term financial targets for 2020. Since the Schaeffler Group's strategy has been approved, the Board of Managing Directors views key fundamentals for profitable long-term growth and adding value to be in place.

2.8 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

Schaeffler AG earnings No. 057

in € millions	2016	2015	Change in %
Revenue	88	54	63.0
Cost of sales	-84	-51	64.7
Gross profit	**4**	**2**	**100**
General and administrative expenses	-71	-46	54.3
Net other operating income	118	30	> 100
Income from equity investments	600	1,119	-46.4
Interest result	-289	-408	-29.2
Income taxes	204	-122	-
Earnings after income tax	**566**	**575**	**-1.6**
Net income for the year	**566**	**575**	**-1.6**
Retained earnings brought forward	0	3,096	- 100
Retained earnings	**566**	**3,671**	**-84.6**

As Schaeffler AG is the ultimate parent company of the Schaeffler Group, it generates 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 71 m in general and administrative expenses.

The increase in revenue, cost of sales, and administrative expenses over the prior year was due to the transfer of certain employees with group-related responsibilities from a subsidiary to Schaeffler AG.

As part of its financing function, Schaeffler AG performs 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 the dividend from Schaeffler Technologies AG & Co. KG.

Interest result consists of the following:

Schaeffler AG interest result No. 058

in € millions	2016	2015
Interest expense on financial debt [1]	-329	-543
Fair value changes and compensation payments on derivatives	-10	-14
Interest income and expense on pensions and partial retirement obligations	0	-5
Other	50	154
Total	**-289**	**-408**

[1] Incl. transaction costs.

Interest expense on financial debt amounted to EUR 329 m in 2016 (prior year: EUR 543 m) and included interest paid and accrued on the company's institutional loans of EUR 25 m (prior year: EUR 79 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 169 m (prior year: EUR 216 m). The prepayment penalty of EUR 48 m (prior year: EUR 177 m) payable in connection with the early redemption of certain bonds was also transferred to Schaeffler AG. Interest expense further included EUR 18 m (prior year: EUR 15 m) in transaction costs and EUR 69 m (prior year: EUR 56 m) in other interest payments. Other included mainly interest income on a loan receivable from the company's shareholder IHO Verwaltungs GmbH.

Income taxes for 2016 amounted to EUR 204 m (prior year: expense of EUR 122 m). This income tax benefit consisted of current tax expense of EUR 109 m (prior year: EUR 58 m) and a deferred tax benefit of EUR 313 m (prior year: expense of EUR 64 m). The deferred tax expense benefit was largely the result of the reduction in deferred tax liabilities recognized on an investment in a partnership within the Schaeffler AG tax group.

Net income for the year amounts to EUR 566 m (prior year: EUR 575 m) in 2016, and equals retained earnings for 2016.

The Board of Managing Directors and the Supervisory Board will propose a dividend for 2016 of EUR 0.49 (prior year: EUR 0.34; special dividend EUR 0.15) per common share and EUR 0.50 (prior year: EUR 0.35; special dividend EUR 0.15) per common non-voting share to the annual general meeting.

Schaeffler AG financial position and net assets

Schaeffler AG financial position and net assets — No. 059

in € millions	12/31/2016	12/31/2015	Change in %
ASSETS			
Intangible assets	**0**	**0**	**0,0**
Property, plant and equipment	**0**	**0**	**0,0**
Shares in affiliated companies	14,109	14,109	
Loans receivable from affiliated companies	120	1,798	-93.3
Long-term financial assets	**14,229**	**15,907**	**-10.5**
Fixed assets	**14,229**	**15,907**	**-10.5**
Receivables from affiliated companies	11,506	11,100	3.7
Receivables from entities to which the company is linked by equity ownership	0	0	0.0
Other assets	98	178	-44.9
Receivables and other assets	**11,604**	**11,278**	**2.9**
Cash at banks	**635**	**449**	**41.4**
Current assets	**12,239**	**11,727**	**4.4**
Prepaid expenses and deferred charges	**0**	**0**	**0.0**
Excess of plan assets over post-employment benefit liability	**8**	**6**	**33.3**
Total assets	**26,476**	**27,640**	**-4.2**
SHAREHOLDERS EQUITY AND LIABILITIES			
Share capital	666	666	0.0
Capital reserves	2,359	2,359	0.0
Revenue reserves	3,343	0	-
Retained earnings	566	3,671	-84.6
Shareholders equity	**6,934**	**6,696**	**3.6**
Special reserve	**8**	**10**	**-20.0**
Provisions for pensions and similar obligations	38	23	65.2
Tax provisions	102	79	29.1
Other provisions	128	142	-9.9
Provisions	**268**	**244**	**9.8**
Bank debt	1,000	654	52.9
Trade payables	3	1	> 100
Amounts payable to affiliated companies	18,204	19,604	-7.1
Other liabilities	59	51	15.7
Liabilities	**19,266**	**20,310**	**-5.1**
Deferred income	**0**	**67**	**- 100**
Deferred tax liabilities	**0**	**313**	**- 100**
Total shareholders equity and liabilities	**26,476**	**27,640**	**-4.2**

Shares in affiliated companies consisted primarily of shares in Schaeffler Technologies AG & Co. KG.

Loans receivable from affiliated companies of EUR 120 m (prior year: EUR 1,798 m) declined significantly in 2016, as the company's shareholder IHO Verwaltungs GmbH prepaid a loan receivable of EUR 1.7 bn in full.

Receivables and other assets consisted of the following:

Schaeffler AG receivables and other assets No. 060

in € millions	12/31/2016 Due in up to 1 year	Due in 1 to 5 years	Due in more than 5 years	12/31/2015 Due in up to 1 year	Due in 1 to 5 years	Due in more than 5 years
Receivables from affiliated companies	11,506	0	0	11,100	0	0
• short-term loans	7,648	0	0	7,699	0	0
• other financial receivables	173	0	0	377	0	0
• trade receivables	82	0	0	24	0	0
• other receivables	3,603	0	0	3,000	0	0
Other assets	35	0	63	79	36	63

Short-term loans and other financial receivables relate 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 3,600 m (prior year: EUR 3,000 m) that had not yet been paid out to Schaeffler AG as at December 31, 2016.

Schaeffler AG managed the Schaeffler Group's cash pool and held bank balances of EUR 635 m (prior year: EUR 449 m) at the end of the reporting period.

On April 22, 2016, Schaeffler AG's annual general meeting passed a resolution to pay a dividend of EUR 328 m to shareholders and to add the remaining retained earnings of EUR 3,343 m to revenue reserves.

Provisions rose by EUR 24 m to EUR 268 m (prior year: EUR 244 m), primarily due to higher income tax provisions for expected income tax payments and higher provisions for pensions and similar obligations.

The signing of a new Facilities Agreement increased the company's bank debt by EUR 346 m to EUR 1,000 m (prior year: EUR 654 m) (see section "Financial debt" on page 50 et seq.).

Schaeffler AG liabilities No. 061

in € millions	12/31/2016 Due in up to 1 year	Due in 1 to 5 years	Due in more than 5 years	12/31/2015 Due in up to 1 year	Due in 1 to 5 years	Due in more than 5 years
Bank debt	0	1,000	0	0	654	0
Trade payables	3	0	0	1	0	0
Amounts payable to affiliated companies	15,471	1,063	1,670	14,558	2,043	3,003
• loans	14,246	1,063	1,670	13,927	2,043	3,003
• other financial debt	1,164	0	0	574	0	0
• trade payables	2	0	0	1	0	0
• other liabilities	59	0	0	56	0	0
Other liabilities	59	0	0	51	0	0

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 2,772 m (prior year: EUR 5,052 m) largely relating to the transfer of the proceeds from the bond issuances by Schaeffler Finance B.V. In October, Schaeffler Finance B.V. redeemed one USD-denominated bond series and two EUR-denominated bond series. The redemptions were largely funded using the proceeds of the prepayment in full of a loan receivable by Schaeffler AG from the company's shareholder IHO Verwaltungs GmbH. Schaeffler AG subsequently used the proceeds of the prepayment to reduce a loan payable to Schaeffler Finance B.V.

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".

2.9 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 289a HGB" beginning on page 74,
- "Governance structure" beginning on page 84,
- "Remuneration report" beginning on page 88, and
- "Governing bodies of the company" beginning on page 100.

Corporate governance report including the corporate governance declaration in accordance with section 289a HGB, which includes the declaration of conformity in accordance with section 161 AktG at: www.schaeffler.com/ir

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, 2016.

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) and free cash flow (financial position), depending on the risk category.

4.1 Risk management system

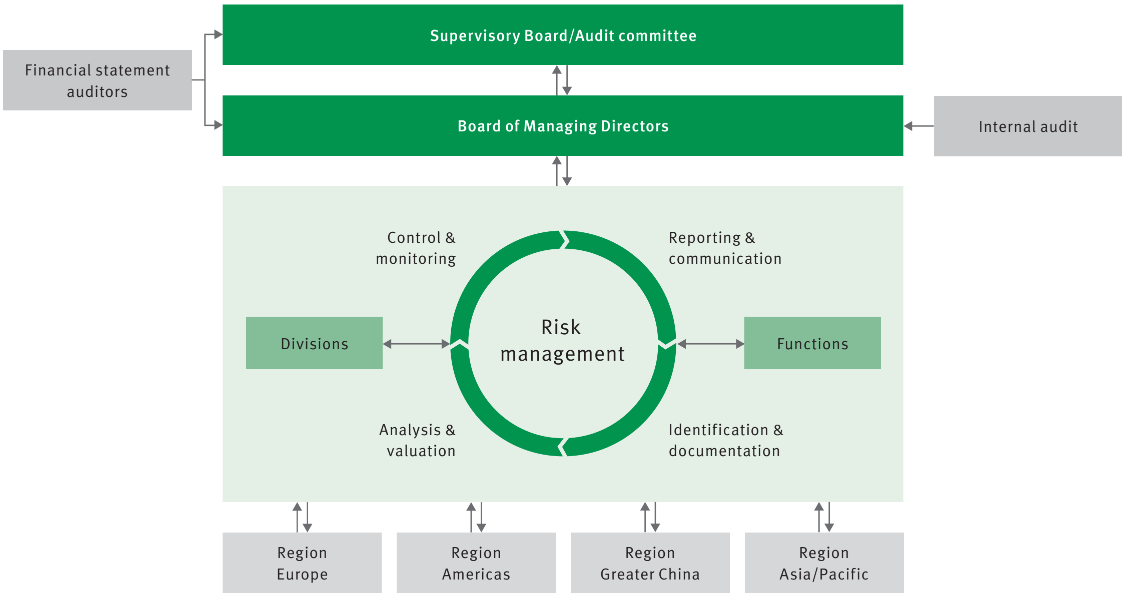
The Schaeffler Group intentionally takes risks in order to meet its corporate objectives. The objective of the risk management system is to identify these risks on a timely basis and to manage them in accordance with the company's risk appetite. This applies particularly to risks to the company's continued 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 various components of the COSO Framework can be found in the Schaeffler Group's risk management process described below.

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 Risk Management are binding on all individuals responsible for risk.

Structure of risk management system

No. 062



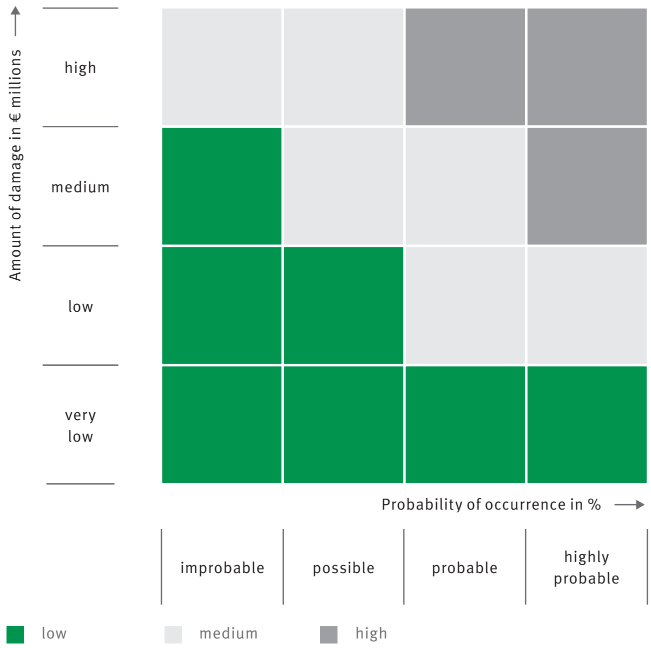
The risk management system consists of a multi-phase process spanning various levels and organizational units in order to appropriately reflect the matrix structure of the Schaeffler Group. In a bottom-up process, risks are identified and analyzed at the subsidiary level. Based on this analysis, the 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 pre-defined 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 2016, 44 of 153 Schaeffler Group entities were included, representing 94 % of revenue and 94 % 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 also classified in 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.
Risk classes are presented graphically using a risk matrix:

Risk matrix No. 063



Effect on net assets, financial position, and earnings

The assessment is made based on the following limits:

Impact assessment No. 064

Amont of damage in €		Probability of occurrence in %	
‹ 10 million	very low	‹ 25 %	improbable
› = 10 million - ‹ 25 million	low	25 % - ‹ 50 %	possible
› = 25 million - ‹ = 50 million	medium	50 % - 75 %	probable
› 50 million	high	› 75 %	highly probable

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.

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 the 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. Schaeffler 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 the corporate level ensure that the separate and consolidated financial statements of Schaeffler AG are compiled, prepared, and issued in accordance with IFRS, 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.

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 2016.

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 Schaeffler'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 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/applications will be replaced. The Schaeffler Group has established its electric mobility business field with the intention of creating a portfolio of products for this field 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.

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 on this issue early on. 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.

Strategic market risks

The markets for the products the Schaeffler Group offers 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 expiry of key patents.

The Schaeffler Groups 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, more focused and leaner competitors, especially in the emerging markets. The company is currently not passing these demands for extensive price reductions on to its own suppliers and cannot fully absorb them with its existing structure.

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.

Operating risks

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

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. Adverse trends in individual markets could have a medium impact on the Schaeffler Group's financial position and earnings.

Loss of market share

The Schaeffler Group operates in a highly competitive and technologically fast-paced environment. 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. Especially the automotive supply sector is characterized by a high level of capital expenditures, a high rate of technological change, constant progress in production technology and high pressure on pricing from OEMs. The Schaeffler Group's key customers include well-known OEMs and suppliers who are themselves subject to significant competitive pressure with respect to innovation and costs and, therefore, strive to obtain price reductions both during the bidding process and throughout the term of supply agreements. To prevent constant price adjustments from impairing margins, the Schaeffler Group is forced to continually improve its production process and reduce expenditures. 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. 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. Besides the price, another deciding factor in the Industrial division and in the Aftermarket business is the ability to deliver, which is constantly being enhanced by systematic improvements in production and delivery logistics.

Loss of market share could have a medium impact on the Schaeffler Group's earnings and financial position. Close cooperation with the Schaeffler Group's key customers on product development and strict product quality control measures reduce the likelihood of substitution and, at the same time, help maintain price levels.

Dependence on customers

The Schaeffler Group's key customers represent a substantial proportion of the Schaeffler Group's revenue. Despite this, the company's dependence on individual OEMs or suppliers is limited, since Schaeffler provides a large variety of products to various regions and applications. Thus, individual Schaeffler products may be substituted, but the probability that the customer will completely terminate the relationship is low and such a termination would require a longer period of time. Nevertheless, substitution of individual products can also have a medium 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 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 and are not quantified further within risk management system.

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.

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.

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. The consequences of such instances of non-compliance could have a negative impact on the Schaeffler Group's net assets, financial position, and earnings as well as on its reputation. The Schaeffler Group will cooperate with the authorities with respect to any current or future instances of non-compliance and will respond appropriately to weaknesses identified.

See chapter entitled "Governance structure" for a discussion of the company's compliance management system.

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.

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 adjustment to the tax base can 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 can 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 bonds 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 can 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 the year 2016 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 a revolving credit facility 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 can 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. 065

	Amount of damage in €	Probability of occurrence in %	Impact	Change from prior year
Strategic risks				
• Electric mobility	high	improbable	medium	new
• Digitalization	medium	possible	medium	new
• Strategic market risks	medium	possible	medium	→
Operating risks				
• Market developments	high	improbable	medium	new
• Loss of market share	high	improbable	medium	↗
• Dependence on customers	low	highly probable	medium	new
• Production risks	high	improbable	medium	→
• Warranty and liability risks	high	improbable	medium	→
• Product piracy risks	low	probable	medium	→
Legal risks				
• Antitrust proceedings	low	probable	medium	→
• Litigation	medium	possible	medium	↗
• Compliance risks	high	improbable	medium	new
Financial risks				
• Tax risks	high	highly probable	high	→
• Pension risks	high	possible	medium	→
• Currency risks	medium	possible	medium	↘
• Liquidity risks	high	improbable	medium	→

4.4 Opportunities

The responsibility for identifying and utilizing opportunities lies with operating management. Opportunities are discussed with the Board of Managing Directors during the regular Strategy Dialog and, based on these discussions, strategies are derived to determine the future direction of the Schaeffler Group.

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 OEMs and suppliers, generally providing an 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 OEMs 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 Electric Mobility Systems Division coordinates its wide range of activities relating to alternative types of drives, allowing the Schaeffler Group to benefit from comprehensive systems know-how.

Public mobility

The increasing number of people living in mega-cities 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 bogie 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 not only with respect to OEMs 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 actively doing research, but is also already operating successfully in the market. Continually expanding the existing expertise in these business fields offers additional future opportunities for growth.

OEM trends

In the last few years, OEMs have increasingly created global platforms aimed at standardizing components and vehicle systems in order to save costs by increasing efficiency. Consequently, OEMs are looking for suppliers who 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 the factory 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. This requires components which can identify and transmit condition-based information. Rolling bearings play a key role as they are responsible for guidance and positioning as well as supporting process forces and movements. To this end, sensors, actuators, control elements, and software components are being added to rolling bearings. The objectives range from continuous condition monitoring to independently locating solutions in response to error messages or active process control based on data from the bearing. The Schaeffler Group views its sensor-equipped bearings as an opportunity to benefit from this trend.

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 OEMs 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 OEMs 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, benefitting 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 OEM 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 instrument ratings to its outstanding bonds since January 2012. An improvement in the ratings published by Standard & Poor's and Moody's can provide the Schaeffler Group with more favorable financing conditions and open up new opportunities to obtain financing. In 2016, rating agency Moody's upgraded Schaeffler AG's company rating to Baa3 (investment grade) with a stable outlook. Rating agency Standard & Poor's upgraded the Schaeffler AG company rating to BB+ (sub-investment grade) with a stable outlook. The issuance ratings for secured bonds improved to Baa3 (Moody's) and BB+ (Standard & Poor's). The issuance rating of the unsecured bonds has been withdrawn since the unsecured bonds were redeemed in full on October 13, 2016.

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 outlook issued by the Schaeffler Group is not in jeopardy, including from the existing risks. In addition to the specific risks described in the management report, unexpected developments significantly damaging or harming the company's production process, customer relationship, or reputation can occur at any time.

The Schaeffler Group's situation with respect to risks has deteriorated slightly 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 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 (January 2017) currently expects the global economy to gather momentum somewhat in 2017, growing by 3.4 %. Oxford Economics (January 2017) is also forecasting a more dynamic economy with a growth rate of 3.3 %. In light of these forecasts, the Schaeffler Group anticipates global economic growth of a good 3 % in 2017.

The expected development of the global economy is subject to a number of uncertainties. The plans of the new U.S. administration include measures that could strengthen the U.S. economy while also stimulating the global economy. However, a full reversal of the U.S. trade policy could hamper growth in world trade. In Europe, the exit negotiations between the United Kingdom and the European Union are expected to start in the spring. In addition, a number of important elections will take place in 2017, including those in the Netherlands, France, and Germany. As a result, the rise of anti-European forces clearly demonstrated in the referendum in the United Kingdom poses a threat that the already extensive political uncertainty will be aggravated further. In addition, problems remain unsolved in the European Union banking sector, particularly in Italy. As well, China is still susceptible to an unexpected economic downturn. The massive increase in the volume of corporate debt in recent years is particularly critical in this regard, as it increases the risk of a sudden destabilization – in the form of a banking crisis and/or a considerable slump in growth.

Based on the forecasts of research institute IHS (February 2017), the Schaeffler Group expects to see global automobile production, measured in terms of the number of passenger cars and light commercial vehicles produced, increase by approximately 1.5 % in 2017. The Schaeffler Group's growth expectation for automobile production in the Europe region is approximately comparable, while automobile production in the Americas region is expected to decline by approximately 1 %. For the Greater China and Asia/Pacific regions, the Schaeffler Group expects growth of approximately 3 % and 2 %, respectively.

The Schaeffler Group anticipates slightly higher growth in industrial production in 2017 than in 2016 (Oxford Economics, December 2016).

5.2 Schaeffler Group outlook

Outlook 2017 No. 066

	Actual 2016	Outlook 2017
Revenue growth compared with prior year [1]	3.4 %	4 to 5 %
EBIT margin before special items	12.7 %	12 to 13 %
Free cash flow	EUR 735 m	~ EUR 600 m

[1] Excluding the impact of currency translation.

The Schaeffler Group expects its revenue to grow by 4 to 5 % excluding the impact of currency translation in 2017. This outlook is based on the assumption that global automobile production will expand by approximately 1.5 % and worldwide industrial production will grow slightly.

The Schaeffler Group expects its Automotive division to continue to grow faster than global automobile production of passenger cars and light commercial vehicles in 2017. Given the expanding global fleet of passenger vehicles, the Aftermarket business will also likely continue to grow.

In the Industrial division, sluggish order intake in the fourth quarter of 2016 and the still strained economic environment in certain sectors suggest 2017 revenue levels at par with 2016.

Based on these considerations, the company expects to generate an EBIT margin before special items [6] of 12 to 13 %.

The Schaeffler Group expects approximately EUR 600 m in free cash flow for 2017.

Herzogenaurach, February 20, 2017

The Board of Managing Directors

[6] Please refer to page 48 for the definition of special items.

Corporate Governance

* Included in the management report.

1. Corporate governance report including corporate governance declaration in accordance with section 289a 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 shareholders, business partners, and employees 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 289a HGB which is a separate component of the management report in accordance with section 315 (5) HGB. However, according to section 317 (2) sentence 4 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 the corporate governance declaration in accordance with section 289a HGB at: www.schaeffler.com/ir

1.1 Corporate governance principles

Managing the company with integrity and good corporate citizenship are integral components of the Schaeffler Group's long-standing corporate culture. The Schaeffler Group's manner of conducting business is based on integrity, fairness, and mutual respect. The Schaeffler Group wants to be a reliable partner to its business partners, employees, and shareholders. 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 updated Schaeffler Group Code of Conduct approved by the Board of Managing Directors provides guidance in this area. The Code of Conduct defines principles of acting with integrity and in compliance with the law. These principles apply equally to everyone – the Board of Managing Directors, management, and every single employee – and also represent a promise to the company's stakeholders. The Schaeffler Group lives up to its corporate responsibility and is laying the foundation for profitable growth and the company's long-term success. At the core of this success are top quality, outstanding technology, and exceptionally innovative spirit, in doing business with customers as well as in the group's internal processes. Being an innovation and technology leader with extensive expertise, the Schaeffler Group's products and solutions help make the mobility of tomorrow eco-friendly and energy-efficient.

Since the release of its last declaration of conformity in March 2016, Schaeffler AG complies with the recommendations of the “Governmental Commission German Corporate Governance Code” as amended on May 05, 2015 (“Code”) with the exceptions described below and will also comply with the recommendations in the future with the exception described under item 2 below:

1. The Code recommends in item 4.2.5 for the presentation of the remuneration of the Board of Managing Directors the use of template charts, which also provide for the presentation of comparative figures for the preceding year. As Schaeffler AG only has been converted into a stock corporation in October 2014 and the group management has only been transferred to the company at this point in time the remuneration report 2015 deviates from this recommendation. The remuneration report 2016 will show the comparative figures for the preceding year. Hence, Schaeffler AG will comply with the recommendation in item 4.2.5 in the future.

2. 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.

1.2 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. It 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 the company’s activities are in compliance with legal requirements and internal guidelines (“compliance”).

See chapter entitled “Governance structure” for further detail on compliance.

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 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 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.

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 at the two levels of management immediately below the Board of Managing Directors in accordance with sections 76 (4) and 111 (5) AktG.

See section “Act on Equal Access for Men and Women to Leadership Positions” for further detail on women in leadership positions.

Members may serve on the Board of Managing Directors until their 68th birthday.

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.

The members of the Board of Managing Directors, their areas of responsibility, and any positions they hold on supervisory boards of other companies are listed in the chapter entitled “Governing bodies of the company”.

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. 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. In addition, 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 appoints the members of the Board of Managing Directors and sets their remuneration.

See chapter entitled “Remuneration report” for further detail on the remuneration of the Board of Managing Directors.

In addition to considering the relevant technical qualifications, the Supervisory Board also strives for diversity when making appointments to 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. Under a resolution passed by the Supervisory Board on September 30, 2015, the Board of Managing Directors has to have at least one female member. The Board of Managing Directors meets the target set by the Supervisory Board, as it has had one female member since January 01, 2016.

Together with the members of the Board of Managing Directors, the Supervisory Board ensures that long-term succession planning is performed for appointments to the Board of Managing Directors.

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 such additional meetings.

As recommended by the German Corporate Governance Code, the Supervisory Board audits the efficiency of its activities at regular intervals. An efficiency audit was performed in 2016.

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. In addition, Schaeffler AG’s Supervisory Board has to consist of at least 30 % women and at least 30 % men (section 96 (2) AktG). This minimum quota is effective for new elections held on or after January 01, 2016, and applies to the Supervisory Board as a whole (joint compliance). 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 employer representative’s quota is currently at 10 %.

In addition to the above legal requirements and in accordance with item 5.4.1 of the German Corporate Governance Code, the Supervisory Board has set the following concrete targets for its composition, considering the company’s specific situation and 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:

- 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.

The current Supervisory Board meets these targets. 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. The members of the Supervisory Board ensure that they are able to devote sufficient time to the performance of their duties. The Supervisory Board also has several members experienced in international business or with other international ties. 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 2016. 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.

See section “Avoiding conflicts of interest” for further detail on conflicts of interest.

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.

Composition 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 is the committee’s chairman.

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) German Stock Corporations Act.

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 and the group 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 for preparing the Supervisory Board’s nomination of the auditors to be appointed by the annual general meeting.

The audit committee has the responsibility and authority to engage the auditors on behalf of the Supervisory Board, determine areas of focus for the audit, and agree 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 monitors the financial reporting process and the effectiveness of Internal Audit, the internal control system, and the risk management system, and addresses compliance within the company. It also regularly obtains information on the areas of focus for the audit as well as audit results from Internal Audit.

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 has to be independent and can neither be a former member of the Board of Managing Directors nor the Chairman of the Supervisory Board; he should 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 remaining members of the audit committee are Georg F. W. Schaeffler, Robin Stalker, Salvatore Vicari, Jürgen Worrich, and Dr. Reinold Mittag.

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 before the meeting. 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 and 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 2016.

Act on Equal Access for Men and Women to Leadership Positions

The Act on Equal Access for Men and Women to Leadership Positions in the Private and Public Sectors prescribes a fixed gender quota of 30 % for Schaeffler AG's Supervisory Board.

See "Supervisory Board" section for further detail on the gender quota of Schaeffler AG's Supervisory Board.

In addition, it requires the Supervisory Board to set a target for the proportion of women on the Board of Managing Directors and the Board of Managing Directors to set targets for the proportion of women at the two levels of management immediately below the Board of Managing Directors.

The target set by the Supervisory Board for the proportion of women on the Schaeffler AG Board of Managing Directors states that the Board of Managing Directors has to have at least one female member. The Board of Managing Directors meets this target set by the Supervisory Board, as it has had one female member since January 01, 2016.

In order to increase the proportion of women below the level of the Board of Managing Directors, the Board of Managing Directors has set targets for the proportion of women of 5 % at the first level of management and 12 % at the second level of management. These targets must be achieved by June 30, 2017.

1.3 Other information on corporate governance

Shares held by members of the Board of Managing Directors and the Supervisory Board, directors' dealings

Item 6.2 of the German Corporate Governance Code requires the ownership of shares in the company or related financial instruments by members of the Board of Managing Directors and the Supervisory Board to be disclosed if these directly or indirectly exceed 1 % of the shares issued by the company. On December 31, 2016, IHO Verwaltungs GmbH held a 75.1 % interest (500 million common shares) in Schaeffler AG. These shareholdings are attributable to Supervisory Board members Georg F. W. Schaeffler and Maria-Elisabeth Schaeffler-Thumann. The remaining members of the Supervisory Board and the Board of Managing Directors held less than 1 % of the common and common non-voting shares of the company as at that date.

Under article 19 of the Market Abuse Regulation, the members of the Board of Managing Directors and the Supervisory Board as well as persons closely associated with them are legally required to report any acquisition or disposal of shares in or bonds of Schaeffler AG or financial instruments linked thereto once the total amount of such transactions executed within a calendar year has reached EUR 5,000.

For further detail on securities transactions reported in 2016 is available at: www.schaeffler.com/ir

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

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 are prepared in accordance with the principles set out in International Financial Reporting Standards (IFRS) as adopted by the EU.

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 arising 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 10, 2016, the auditors have issued a binding independence letter for the year ended December 31, 2016.

1.4 Declaration of conformity pursuant to section 161 AktG

Since the release of its last declaration of conformity in March 2016, Schaeffler AG complies with the recommendations of the "Governmental Commission German Corporate Governance Code" as amended on May 05, 2015 ("Code") with the exceptions described below and will also comply with the recommendations in the future with the exception described under item 2 below:

1. The Code recommends in item 4.2.5 for the presentation of the remuneration of the Board of Managing Directors the use of template charts, which also provide for the presentation of comparative figures for the preceding year. As Schaeffler AG only has been converted into a stock corporation in October 2014 and the group management has only been transferred to the company at this point in time the remuneration report 2015 deviates from this recommendation. The remuneration report 2016 will show the comparative figures for the preceding year. Hence, Schaeffler AG will comply with the recommendation in item 4.2.5 in the future.

2. 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 2016

For the Supervisory Board	For the Board of Managing Directors
Georg F. W. Schaeffler Chairman of the Supervisory Board	Klaus Rosenfeld Chief Executive Officer

Georg F. W. Schaeffler

2. Report of the Supervisory Board

Ladies and Gentlemen,

The Supervisory Board has performed the duties mandated by law, the company's articles of association, and its internal rules of procedure in 2016. The Supervisory Board has provided advice to the Board of Managing Directors and supervised its activities. It was directly involved on a timely basis in all decisions that were of fundamental importance to the company. The Board of Managing Directors regularly informed the Supervisory Board in written and oral reports about the company's results of operations and about significant transactions as well as the related risks and opportunities. In addition, the Schaeffler Group's strategy was presented to and discussed with the Supervisory Board in detail by the Board of Managing Directors. The Board of Managing Directors continually updated the Supervisory Board in detail about the development of revenue and earnings of the group and the divisions as well as about the financial position. Short- and long-term planning and budgeting matters as well as compliance and risk management matters were also discussed. The Supervisory Board addressed developments in the capital markets and the trend in the price of Schaeffler AG's common non-voting shares, as well.

The members of the Supervisory Board were also available for consultation with the Board of Managing Directors between meetings. The Chairman of the Supervisory Board regularly kept in close 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.

Members of the Supervisory Board and its committees

The Supervisory Board and its committees remained unchanged in 2016. 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

The Supervisory Board continues to be of the opinion that it has a sufficient number of independent members (as defined in the German Corporate Governance Code).

There were no conflicts of interest related to members of the Board of Managing Directors or the Supervisory Board in 2016.

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), Dr. Ulrich Hauck, Oliver Jung, Prof. Dr. Peter Pleus, Corinna Schittenhelm, Dr. Stefan Spindler, and Matthias Zink (since January 01, 2017). On March 11, 2016, Matthias Zink was appointed to the Board of Managing Directors for a term of three years effective January 01, 2017. Also on that date, Prof. Dr. Peter Pleus was reappointed to the Board of Managing Directors for a further term of two years starting January 01, 2017. Norbert Indlekofer left the Board of Managing Directors effective December 31, 2016. The company and the Supervisory Board would like to express their gratitude to Norbert Indlekofer for his successful work over many years and wish him all the best for his retirement.

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, Dr. Ulrich Hauck 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.

Main activities

The Supervisory Board held four regular meetings, one strategy meeting, and two extraordinary meetings held via conference call in 2016. One resolution was passed in writing. All members of the Supervisory Board attended significantly more than half of the Supervisory Board meetings. The same applies to the attendance of members of the Supervisory Board at committee meetings.

At the extraordinary meeting held via telephone on February 17, 2016, attendees discussed the achievement of targets and objectives related to the remuneration of the Managing Directors and were provided with information on tort litigation against former Managing Directors.

At its first regular meeting on March 11, 2016, the Supervisory Board appointed Matthias Zink to the Board of Managing Directors, reappointed Prof. Dr. Pleus to the Board of Managing Directors, and addressed other personnel matters. The Supervisory Board also dealt with the Schaeffler Group's results of operations as well as with the 2015 separate and consolidated financial statements of the Schaeffler Group. In addition, it approved the report of the Supervisory Board to the annual general meeting, the Supervisory Board's proposed agenda items for the annual general meeting, and an amendment to the declaration of conformity pursuant to section 161 AktG.

At its second regular meeting on May 11, 2016, the Supervisory Board addressed personnel matters, the Schaeffler Group's results of operations, and the results of the first quarter of 2016. There was also a report on intellectual property.

In its extraordinary conference call on July 08, 2016, the Supervisory Board discussed financing measures which were subsequently approved by a resolution passed in writing dated July 15, 2016.

At its third regular meeting on October 06, 2016, the Supervisory Board heard a report on the latest results of operations and the results of the first half of 2016.

The third regular meeting of the Supervisory Board was immediately followed by a meeting at which the Schaeffler Group's future strategy was presented in detail. The Supervisory Board discussed the various aspects of the strategy with the Board of Managing Directors. The Board of Managing Directors included the Supervisory Board's suggestions in its strategy considerations.

At its fourth regular meeting on December 16, 2016, the Supervisory Board passed a resolution amending the employment contracts of the divisional CEOs and set the target amounts underlying the bonuses for the Managing Directors for 2017. The Supervisory Board also approved the declaration on the German Corporate Governance Code (section 161 AktG) and discussed the Schaeffler Group's results of operations and results of the third quarter of 2016. Also at this meeting, the Supervisory Board approved the budget for 2017 and the long-range plan for the years 2017 to 2021 (including the capital expenditure plan).

In October and November 2016, the Supervisory Board performed an internal efficiency audit of its activities. The audit found that the Supervisory Board performs its duties efficiently. Certain issues, such as monitoring the implementation of the Supervisory Board's decisions, need further development in the future.

The executive committee of the Supervisory Board held four regular meetings and four extraordinary meetings via telephone in 2016. One resolution was passed in writing. Preparing personnel decisions to be made by the Supervisory Board and preparing the meetings of the Supervisory Board were on the agenda of the regular meetings. A resolution dated September 01, 2016 to approve a Managing Director's external activity was passed in writing.

The extraordinary meetings held via telephone on January 08 and 12, 2016 and on November 04, 2016, dealt with tort litigation against former Managing Directors. The executive committee's extraordinary meeting held via telephone on December 07, 2016 dealt with two M&A projects and personnel matters.

The audit committee held four regular meetings in 2016. At these meetings, the audit committee addressed the separate and consolidated financial statements of the Schaeffler Group for 2015, and the interim reports as at March 31, 2016, June 30, 2016, and September 30, 2016. Compliance, internal audit, risk management, and the internal control system were reported on a regular basis at these meetings, as well. The audit committee also dealt with working capital management, issues related to international tax law, and non-audit services provided by the financial statement auditors. The audit committee recommended to the 2016 annual general meeting that it appoint KPMG AG auditors of the separate and consolidated financial statements and auditors for purposes of reviews of interim financial statements and financial information. The audit committee also engaged KPMG AG as auditors and determined areas of focus for the audit.

The nomination and mediation committees did not hold any meetings in 2016.

Separate and consolidated financial statements 2016

KPMG has audited the separate financial statements and the combined management report as at December 31, 2016 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.

KPMG 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, 2016 to December 31, 2016.

The consolidated financial statements of Schaeffler AG as at and for the year ended December 31, 2016 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 315a (1) German Commercial Code. The consolidated financial statements were also audited by KPMG.

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 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 audit committee discussed the financial statement documents, the dependency report, and the long-form audit reports with the Board of Managing Directors and the auditors on March 02, 2017. The audit committee scrutinized the development of earnings for 2016, the financial position and net assets as at the reporting date and, particularly, provisions for risks. The financial statement documents, the dependency report, and the long-form audit reports were also dealt with in the Supervisory Board meeting convened to approve the financial statements on March 03, 2017. 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 audit findings 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), 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 0.49 per common share and EUR 0.50 per common non-voting share in respect of 2016.

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 employees of Schaeffler AG and the group companies for their dedication and their constructive teamwork during another challenging year.

On behalf of the Supervisory Board

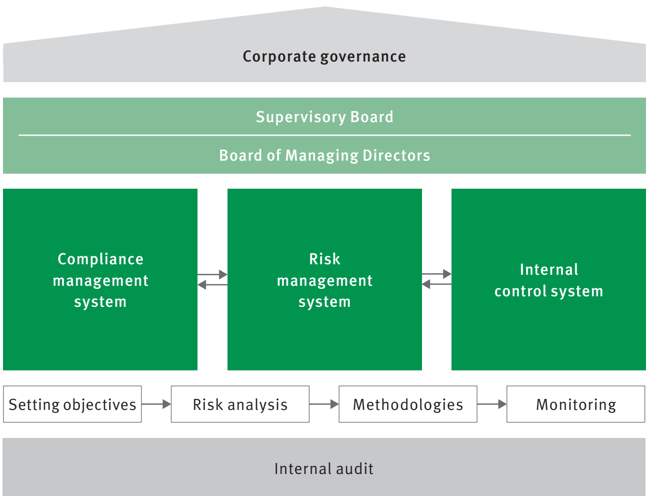
Georg F. W. Schaeffler
Chairman

Herzogenaurach, March 03, 2017

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. 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.

Schaeffler Group governance structure No. 067



The governance structure promotes transparency and supports the values of a global family business (sustainable, innovative, excellent, and passionate). The components of the governance structure support our business units in effectively identifying and managing risk.

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 Chief Compliance Officer. It consists of the heads of the subsystems and the heads of other risk and corporate functions. 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.

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.

Three lines of defense model No. 068

Lines of defense	Responsible unit or function	Area of responsibility
First line of defense	**Operating business units**	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.
Second line of defense	**Risk functions** (e. g. controlling, risk management, compliance, and legal)	The second tier defines global standards and controls, regularly monitors compliance with them, and reports on their effectiveness. It is also responsible for regular and independent risk assessment.
Third line of defense	**Internal Audit**	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.

The business units bear primary responsibility for the risks inherent in their business. 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. An anonymous whistleblowing system is available for this purpose where necessary.

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, a component of the "ONE Schaeffler" 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 PS 980 by an independent audit firm, the next step planned is a review of the implementation of the CMS by an independent audit firm.

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 estimates of the probability of occurrence and the size of the potential loss of pertinent risk scenarios from the interviewee that are 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, to issues regarding the location-specific design of Sales and Distribution.

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 which was expanded in 2016 and 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. Training sessions are continually refined and updated and adapted to the employees' areas of responsibility. For instance, case studies in the Risk Awareness training session are customized to the relevant business units in order to make the presentation of potential risks as specific and clear as possible. 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 2016. A new code of conduct applicable to all employees worldwide was introduced. In addition to requirements relating to general conduct, the principles and practices described 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 bribery or corruption in any way. The same applies to conduct violating competition or anti-trust laws. The Schaeffler Group stays away from any transactions that cannot be effected or continued without unacceptable conduct.

The company continued the implementation of a register of contacts with competitors as well as a groupwide business partner due diligence process. This underlines the standard the Schaeffler Group expects of its business partners with respect to acting with integrity and abiding by rules. In 2016, the compliance training program included training on risk awareness, the Schaeffler Code of Conduct, and security of information including classification of information. New training measures were introduced to protect against cybercrime and CEO fraud.

The company maintains a groupwide insider list in order to comply with capital markets regulations. The members of the Board of Managing Directors and the Supervisory Board as well as employees were informed of their obligations under capital markets laws and the consequences of the listing. In addition, there is an insider committee whose activities include maintaining the insider list, deciding on how to deal with potential insider information, and ensuring compliance with the requirements of capital markets laws.

For further detail on significant compliance-related risks see "Report on opportunities and risks".

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.

For further detail on the risk management system see "Report on opportunities and risks".

3.3 Internal control system

The second line of defense also comprises the Schaeffler Group's internal control system. The internal control system 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.

For further detail on the internal control system see "Report on opportunities and risks".

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. Organizationally, Internal Audit is assigned to the Chief Executive Officer of Schaeffler AG.

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 CEO/Board of Managing Directors/audit committee;
- audit planning and significant changes therein have to be approved by the Board of Managing Directors and documented appropriately.

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 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.

Internal Audit performs systems and effectiveness audits. Systems audits involve auditing selected areas (e.g. Procurement) and documenting and analyzing the actual processes in place. Any findings documented during such systems audits are assigned to one of three assessment areas ("orderliness", "internal monitoring system", "business processes"). Effectiveness audits involve testing the effectiveness of the risk management system or the internal control system within the Schaeffler Group. Compliance risks are covered in the "orderliness" assessment area.

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, its recommendations for mitigating risk, and the persons responsible for implementation, with whom they agree binding implementation dates. In a monitoring and follow-up process, Internal Audit monitors implementation of its recommendations for remediating 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 in effect since the listing

As stipulated in the German Corporate Governance Code (GCGC) and section 87 AktG, the Supervisory Board sets the total remuneration, reviews the remuneration scheme on a regular basis, and reviews the appropriateness of the remuneration of the Board of Managing Directors on a regular basis. 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).

In preparation for the listing, Schaeffler AG's Supervisory Board approved the enhancement of the remuneration system for the members of the Board of Managing Directors on September 08, 2015. This remuneration system became effective retroactively as at January 01, 2015 on the date of the listing, October 09, 2015, and is effective for all members of the Board of Managing Directors in office in 2016.

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. 069

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 (in 2015 also for the divisional CEOs): Free cash flow (FCF Group) and Schaeffler Value Added (SVA Group) of the Schaeffler Group (weighted equally). For the divisional CEOs: Free cash flow (FCF Group) and Schaeffler Value Added (SVA Group) of the Schaeffler Group, Schaeffler Value Added (SVA Division) and working capital (WC Division) of the division (weighted equally) 1)	0 % – 150 % (target bonus = 100 %)	Meeting annual performance targets	Annually
Long-term bonus	Share price trend underlying performance share units (PSUs) granted 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

1) Starting in 2017, cash flow of the division will replace working capital of the division for purposes of measuring the performance of the divisional CEOs.

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 2016.

Performance-based components

Short-term variable component – short-term bonus

All members of the Board of Managing Directors in office in 2016 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 on an annual basis. The 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 (in 2015 also to the divisional CEOs) 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 (FCF Group) of the Schaeffler Group and Schaeffler Value Added (SVA Group) of the Schaeffler Group and of Schaeffler Value Added (SVA Division) of the division and working capital (WC Division) of the division, again weighted equally. [7]

[7] Starting in 2017, cash flow of the division will replace working capital of the division for purposes of measuring the performance of the divisional CEOs.

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 Working Capital Division performance target is calculated as the ratio of the division's working capital to divisional revenue.

The Supervisory Board can set other strategic targets in addition to the FCF, SVA, and WC performance targets. The short-term bonus may lapse in its entirety if the minimum targets are not met. Furthermore, the Supervisory Board can establish a multiplier ranging from 0.8 to 1.2 to reflect a Managing Director's individual performance. In any event, 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. Based on relevant agreements, all current Managing Directors are eligible for the PSUP.

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 performance targets 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 cannot increase.

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. [8]
- 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.

The 2015 and 2016 tranches of PSUs subject to FCF- and TSR-based performance targets vest based on the following target tiers.

PSUP performance targets for FCF No. 070

Cumulative free cash flow 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 FCFF ‹ ~ 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 for TSR No. 071

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.

[8] Taking into account the rules applicable to leavers.

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 No. 072

	Target amount (in € thousands)	Number of PSUs granted on January 01, 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
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
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
Total	**7,350**	**504,117**	**-**	**6,376**

[1] Equals the number of PSUs outstanding as at December 31, 2016.
[2] Norbert Indlekofer left the Board of Managing Directors of Schaeffler AG as at December 31, 2016.

The underlying share price of the 2015 tranche is EUR 13.15. The PSUs granted to each individual and the related fair values in 2015 are as follows:

PSUs granted in 2015 [1] No. 073

	Target amount (in € thousands)	Number of PSUs granted on October 09, 2015 [2]	Grant date fair value per PSU (in €)	Grant date fair value (in € thousands)
Klaus Rosenfeld (CEO)	1,300			
Base number of PSUs		49,429	11.58	572
FCF PSUs		24,715	11.58	286
TSR PSUs		24,715	6.96	172
Prof. Dr. Peter Gutzmer	950			
Base number of PSUs		36,121	11.58	418
FCF PSUs		18,061	11.58	209
TSR PSUs		18,061	6.96	126
Dr. Ulrich Hauck	600			
Base number of PSUs		22,813	11.58	264
FCF PSUs		11,407	11.58	132
TSR PSUs		11,407	6.96	79
Norbert Indlekofer [3]	950			
Base number of PSUs		36,121	11.58	418
FCF PSUs		18,061	11.58	209
TSR PSUs		18,061	6.96	126
Oliver Jung	950			
Base number of PSUs		36,121	11.58	418
FCF PSUs		18,061	11.58	209
TSR PSUs		18,061	6.96	126
Prof. Dr. Peter Pleus	950			
Base number of PSUs		36,121	11.58	418
FCF PSUs		18,061	11.58	209
TSR PSUs		18,061	6.96	126
Dr. Stefan Spindler	533			
Base number of PSUs		20,278	11.58	235
FCF PSUs		10,140	11.58	117
TSR PSUs		10,140	6.96	71
Total	**6,233**	**474,016**	**-**	**4,940**

[1] Kurt Mirlach and Robert Schullan left the Board of Managing Directors of Schaeffler AG as at December 31 and April 30, 2015, respectively. They were not granted any PSUs for 2015.
[2] Equals the number of PSUs outstanding as at December 31, 2016.
[3] 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 2016 tranche (prior year: 2015 tranche) reflects the following input parameters:

- risk-free interest rate for the remaining performance period of 0.15 % (prior year: 0.2 %),
- expected dividend yield of Schaeffler AG common non-voting shares over the performance period of 2.15 % (prior year: 2.66 %),
- expected volatility of Schaeffler AG common non-voting shares of 33.02 % (prior year: 33.34 %),
- expected volatility of the benchmark index of 19.56 % (prior year: 18.97 %),
- expected correlation coefficient between the benchmark index and Schaeffler AG common non-voting shares of 0.43 (prior year: 0.34).

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, 2016, calculated in accordance with IAS 19 and based on the beneficiary's current age and years of service.

Service cost for 2016 and defined benefit obligations as at December 31, 2016 in accordance with IAS 19 No. 074

in € thousands	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
Norbert Indlekofer [1]	2016	194	5,049
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
Total		**3,295**	**30,910**

1) Norbert Indlekofer left the Board of Managing Directors of Schaeffler AG as at December 31, 2016.

Service cost for 2015 and defined benefit obligations as at December 31, 2015 in accordance with IAS 19 No. 075

in € thousands	Year	Service cost	Defined benefit obligation
Klaus Rosenfeld (CEO)	2015	1,240	7,875
Prof. Dr. Peter Gutzmer	2015	273	4,178
Dr. Ulrich Hauck	2015	337	345
Norbert Indlekofer [1]	2015	205	5,300
Oliver Jung	2015	288	2,166
Prof. Dr. Peter Pleus	2015	380	5,282
Dr. Stefan Spindler	2015	164	168
Members who left the Board of Managing Directors in 2015 (remuneration under remuneration system in effect prior to listing)			
Kurt Mirlach [2]	2015	266	4,391
Robert Schullan [3]	2015	130	3,824
Total		**3,283**	**33,529**

1) Norbert Indlekofer left the Board of Managing Directors of Schaeffler AG as at December 31, 2016.
2) Kurt Mirlach left the Board of Managing Directors of Schaeffler AG as at December 31, 2015.
3) Robert Schullan left the Board of Managing Directors of Schaeffler AG as at April 30, 2015. His employment contract continued until December 31, 2015.

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 EUR 300 thousand each for 2017 and 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 the long-term bonuses granted in 2017, 2018, and 2019.

Moreover, in 2015, certain members of the Board of Managing Directors received additional payments in connection with the change in the remuneration system and adjustment of their fixed remuneration. These payments, EUR 525 thousand in total, were offset in full against amounts payable by the company in 2016.

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 noncompetition clause for a period of two 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 twelve 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 Corinna Schittenhelm, who was appointed to the Board of Managing Directors in 2016, and Dr. Ulrich Hauck and Dr. Stefan Spindler, who were appointed to the Board of Managing Directors in 2015, include post-contract non-competition clauses calling for corresponding compensation.

Robert Schullan left Schaeffler AG's Board of Managing Directors early at his own request effective April 30, 2015. He was entitled to receive non-performance-based remuneration including all fringe benefits until December 31, 2015, a total of EUR 301 thousand.

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 obtained the assistance of an independent remuneration expert for purposes of reviewing whether the remuneration of the Board of Managing Directors is appropriate.

4.2 Main features of the remuneration system for and amounts of remuneration of the Board of Managing Directors in effect prior to the listing

The remuneration system in effect prior to the listing remained applicable to the two members of the Board of Managing Directors who left the company, Kurt Mirlach (left effective December 31, 2015) and Robert Schullan (left effective April 30, 2015), without change in 2015 and consisted of fixed and variable remuneration components. The total remuneration of each member of the Board of Managing Directors was capped ("hard cap"). The fixed component of remuneration was based on the duties and responsibilities of each member of the Board of Managing Directors. In addition to the fixed component, each member of the Board of Managing Directors also received a performance-based bonus, which was calculated based on the following factors:

- operating earnings compared to minimum return on revenue,
- actual working capital compared to budgeted working capital, and
- individual performance factor.

In addition, the members of the Board of Managing Directors received fringe benefits which included the use of a company car for private purposes, insurance benefits, D&O insurance, and pension benefits.

The previous remuneration system was based on individual contractual arrangements entered into prior to the company's listing on the capital markets. On the date of the listing, the new remuneration system meeting the requirements for remuneration systems of listed companies became effective retroactively as at January 01, 2015.

4.3 Amounts of remuneration of the Board of Managing Directors

The fixed and variable components of remuneration are disclosed below. The following tables show the remuneration granted for and paid in 2016 and in 2015.

Remuneration for 2016

	Klaus Rosenfeld				Prof. Dr. Peter Gutzmer				Dr. Ulrich Hauck			
	Chief Executive Officer				Deputy Chief Executive Officer and Chief Technology Officer				Chief Financial Officer			
	since October 24, 2014				since October 24, 2014				since April 01, 2015			
in € thousands	**2015**	**2016**	**2016 (floor)**	**2016 (ceiling)**	**2015**	**2016**	**2016 (floor)**	**2016 (ceiling)**	**2015**	**2016**	**2016 (floor)**	**2016 (ceiling)**
Fixed remuneration	1,200	1,200	1,200	1,200	600	600	600	600	450	600	600	600
Sign-on bonus	1,200	-	-	-	600	-	-	-	600	-	-	-
Fringe benefits	27	27	27	27	28	28	28	28	20	28	28	28
Total	**2,427**	**1,227**	**1,227**	**1,227**	**1,228**	**628**	**628**	**628**	**1,070**	**628**	**628**	**628**
One-year variable remuneration	1,200	1,200	0	1,800	900	900	0	1,350	563	750	0	1,125
Multi-year variable remuneration												
• Long-term bonus: PSUP (4 years) – 2015 tranche	1,031	-	-	-	753	-	-	-	476	-	-	-
• Long-term bonus: PSUP (4 years) – 2016 tranche	-	1,128	0	2,600	-	824	0	1,900	-	694	0	1,600
Total	**4,658**	**3,555**	**1,227**	**5,627**	**2,881**	**2,352**	**628**	**3,878**	**2,109**	**2,072**	**628**	**3,353**
Pension cost	1,240	1,158	1,158	1,158	273	287	287	287	337	458	458	458
Total remuneration	**5,898**	**4,713**	**2,385**	**6,785**	**3,154**	**2,639**	**915**	**4,165**	**2,446**	**2,530**	**1,086**	**3,811**

Payments for 2016

	Klaus Rosenfeld		Prof. Dr. Peter Gutzmer		Dr. Ulrich Hauck	
	Chief Executive Officer		Deputy Chief Executive Officer and Chief Technology Officer		Chief Financial Officer	
	since October 24, 2014		since October 24, 2014		since April 01, 2015	
in € thousands	**2016**	**2015**	**2016**	**2015**	**2016**	**2015**
Fixed remuneration	1,200	1,200	600	600	600	450
Sign-on bonus	600	600	300	300	300	300
Fringe benefits	27	27	28	28	28	20
Total	**1,827**	**1,827**	**928**	**928**	**928**	**770**
One-year variable remuneration	1,199	953	899	715	749	447
Multi-year variable remuneration						
• Long-term bonus: PSUP (4 years) – 2015 tranche	0	0	0	0	0	0
• Long-term bonus: PSUP (4 years) – 2016 tranche	0	0	0	0	0	0
Total	**3,026**	**2,780**	**1,827**	**1,643**	**1,677**	**1,217**
Pension cost	1,158	1,240	287	273	458	337
Total remuneration	**4,184**	**4,020**	**2,114**	**1,916**	**2,135**	**1,554**

No. 076

Norbert Indlekofer				Oliver Jung				Prof. Dr. Peter Pleus				Corinna Schittenhelm				Dr. Stefan Spindler			
CEO Automotive				Chief Operating Officer				CEO Automotive				Chief Human Resources Officer				CEO Industrial			
from October 24, 2014 to December 31, 2016				since October 24, 2014				since October 24, 2014				since January 01, 2016				since May 01, 2015			
2015	2016	2016 (floor)	2016 (ceiling)	2015	2016	2016 (floor)	2016 (ceiling)	2015	2016	2016 (floor)	2016 (ceiling)	2015	2016	2016 (floor)	2016 (ceiling)	2015	2016	2016 (floor)	2016 (ceiling)
600	600	600	600	600	600	600	600	600	600	600	600	-	600	600	600	400	600	600	600
600	-	-	-	600	-	-	-	600	-	-	-	-	-	-	-	600	-	-	-
27	25	25	25	28	28	28	28	41	41	41	41	-	23	23	23	13	23	23	23
1,227	**625**	**625**	**625**	**1,228**	**628**	**628**	**628**	**1,241**	**641**	**641**	**641**	**-**	**623**	**623**	**623**	**1,013**	**623**	**623**	**623**
900	900	0	1,350	900	900	0	1,350	900	900	0	1,350	-	600	0	900	500	750	0	1,125
753	-	-	-	753	-	-	-	753	-	-	-	-	-	-	-	423	-	-	-
-	824	0	1,900	-	824	0	1,900	-	824	0	1,900	-	564	0	1,300	-	694	0	1,600
2,880	**2,349**	**625**	**3,875**	**2,881**	**2,352**	**628**	**3,878**	**2,894**	**2,365**	**641**	**3,891**	**-**	**1,787**	**623**	**2,823**	**1,936**	**2,067**	**623**	**3,348**
205	194	194	194	288	272	272	272	380	357	357	357	-	319	319	319	164	250	250	250
3,085	**2,543**	**819**	**4,069**	**3,169**	**2,624**	**900**	**4,150**	**3,274**	**2,722**	**998**	**4,248**	**-**	**2,106**	**942**	**3,142**	**2,100**	**2,317**	**873**	**3,598**

No. 077

Norbert Indlekofer		Oliver Jung		Prof. Dr. Peter Pleus		Corinna Schittenhelm		Dr. Stefan Spindler	
CEO Automotive		Chief Operating Officer		CEO Automotive		Chief Human Resources Officer		CEO Industrial	
from October 24, 2014 to December 31, 2016		since October 24, 2014		since October 24, 2014		since January 01, 2016		since May 01, 2015	
2016	2015	2016	2015	2016	2015	2016	2015	2016	2015
600	600	600	600	600	600	600	-	600	400
300	300	300	300	300	300	-	-	300	300
25	27	28	28	41	41	23	-	23	13
925	**927**	**928**	**928**	**941**	**941**	**623**	**-**	**923**	**713**
862	715	899	715	862	715	599	-	522	397
0	0	0	0	0	0	0	-	0	0
0	0	0	0	0	0	0	-	0	0
1,787	**1,642**	**1,827**	**1,643**	**1,803**	**1,656**	**1,222**	**-**	**1,445**	**1,110**
194	205	272	288	357	380	319	-	250	164
1,981	**1,847**	**2,099**	**1,931**	**2,160**	**2,036**	**1,541**	**-**	**1,695**	**1,274**

Remuneration for 2016 –
Managing Directors who left the company in 2015

No. 078

	Kurt Mirlach				Robert Schullan			
	Chief Human Resources Officer				CEO Industrial			
	from October 24, 2014 to December 31, 2015				from October 24, 2014 to April 30, 2015			
in € thousands	2015	2016	2016 (floor)	2016 (ceiling)	2015	2016	2016 (floor)	2016 (ceiling)
Fixed remuneration	450	-	-	-	142	-	-	-
Sign-On Bonus	-	-	-	-	-	-	-	-
Fringe benefits	22	-	-	-	9	-	-	-
Total	**472**	**-**	**-**	**-**	**151**	**-**	**-**	**-**
One-year variable remuneration	960	-	-	-	572	-	-	-
Multi-year variable remuneration								
• Long-term bonus: PSUP (4 years) – 2015 tranche	-	-	-	-	-	-	-	-
• Long-term bonus: PSUP (4 years) – 2016 tranche	-	-	-	-	-	-	-	-
Total	**1,432**	**-**	**-**	**-**	**723**	**-**	**-**	**-**
Pension cost	266	-	-	-	130	-	-	-
Total remuneration	**1,698**	**-**	**-**	**-**	**853**	**-**	**-**	**-**

Payments for 2016 –
Managing Directors who left the company in 2015

No. 079

	Kurt Mirlach		Robert Schullan	
	Chief Human Resources Officer		CEO Industrial	
	from October 24, 2014 to December 31, 2015		from October 24, 2014 to April 30, 2015	
in € thousands	2016	2015	2016	2015
Fixed remuneration	-	450	-	142
Sign-On Bonus	-	-	-	-
Fringe benefits	-	22	-	9
Total	**-**	**472**	**-**	**151**
One-year variable remuneration	-	1,003	-	579
Multi-year variable remuneration				
• Long-term bonus: PSUP (4 years) – 2015 tranche	-	-	-	-
• Long-term bonus: PSUP (4 years) – 2016 tranche	-	-	-	-
Total	**-**	**1,475**	**-**	**730**
Pension cost	-	266	-	130
Total remuneration	**-**	**1,741**	**-**	**860**

The total remuneration for 2016 and 2015 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 2016 by individual No. 080

	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
Norbert Indlekofer [2]	625	862	824	2,311
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
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.

Total remuneration (HGB) for 2015 by individual No. 081

	Remuneration components			
in € thousands	fixed	variable, short-term	variable, long-term [1]	Total remuneration
Klaus Rosenfeld (CEO)	2,427	953	1,031	4,411
Prof. Dr. Peter Gutzmer	1,228	715	753	2,696
Dr. Ulrich Hauck	1,070	447	476	1,993
Norbert Indlekofer [2]	1,227	715	753	2,695
Oliver Jung	1,228	715	753	2,696
Prof. Dr. Peter Pleus	1,241	715	753	2,709
Dr. Stefan Spindler	1,013	397	423	1,833
Managing Directors who left the company in 2015 (Remuneration under remuneration in effect prior to listing)				
Kurt Mirlach (until December 31, 2015)	472	1,003	0	1,475
Robert Schullan (until April 30, 2015)	151	579	0	730
Total	**10,057**	**6,239**	**4,942**	**21,238**

[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 2016 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. 082

in € thousands	Expenses (IFRS)
Klaus Rosenfeld (CEO)	402
Prof. Dr. Peter Gutzmer	293
Dr. Ulrich Hauck	213
Norbert Indlekofer [1]	948
Oliver Jung	293
Prof. Dr. Peter Pleus	184
Corinna Schittenhelm	88
Dr. Stefan Spindler	201
Total	**2,622**

[1] Norbert Indlekofer left the Board of Managing Directors of Schaeffler AG as at December 31, 2016.

The total expenses resulting from the PSUP for 2015 are broken down by individual in accordance with section 314 (1) (6a) (8) HGB in connection with IFRS 2.51a below.

PSUP expenses in 2015 No. 083

in € thousands	Expenses (IFRS)
Klaus Rosenfeld (CEO)	92
Prof. Dr. Peter Gutzmer	67
Dr. Ulrich Hauck (since April 01, 2015)	42
Norbert Indlekofer [1]	176
Oliver Jung	67
Prof. Dr. Peter Pleus	176
Dr. Stefan Spindler (since May 01, 2015)	38
Managing Directors who left the company in 2015 (Remuneration under remuneration in effect prior to listing)	
Kurt Mirlach (until December 31, 2015)	-
Robert Schullan (until April 30, 2015)	-
Total	**658**

[1] Norbert Indlekofer left the Board of Managing Directors of Schaeffler AG as at December 31, 2016.

4.4 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. Remuneration is pro-rated for changes in the Supervisory Board or its committees.

Remuneration for committee membership for any one financial year is conditional on the relevant committee actually having met to fulfill its responsibilities during the period.

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.

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.

The company has obtained director's and officers' liability insurance (D&O insurance) for all members of the Supervisory Board; the policy's deductible provision is in accordance with the German Stock Corporations Act and the GCGC.

No advances or loans were granted to members of the Supervisory Board in 2016 or 2015. The following tables summarize the amount of remuneration of each member of the Supervisory Board.

Supervisory Board remuneration for 2016 1) No. 084

in € thousands	Fixed remuneration	Remuneration for committee membership	Attendance fees	Total remuneration
Bullinger, Prof. Dr. Hans-Jörg	60		7	67
Engelmann, Dr. Holger	60		7	67
Gottschalk, Prof. Dr. Bernd	60		7	67
Lenhard, Norbert 2)	60	24	12	96
Luther, Dr. Siegfried	60	48	16	124
Mittag, Dr. Reinold 2)	60	24	16	100
Münch, Yvonne 2)	60		9	69
Resch, Barbara 2)	60	24	14	98
Schaeffler, Georg F. W.	119	48	14	181
Schaeffler-Thumann, Maria-Elisabeth	89	24	7	120
Schmidt, Stefanie 2)	60		7	67
Spindler, Dirk	60		9	69
Stalker, Robin	60	24	14	98
Stolz, Jürgen 2)	60		9	69
Vicari, Salvatore 2)	60	24	14	98
Wechsler, Jürgen 2)	89	24	12	125
Wiesheu, Dr. Otto	60		7	67
Wolf, Prof. KR Ing. Siegfried	60	24	9	93
Worrich, Jürgen 2)	60	24	16	100
Zhang, Prof. Dr.-Ing. Tong	60		9	69
Total	**1,317**	**312**	**215**	**1,844**

1) All amounts shown include value-added tax on remuneration where applicable. The positions held by the Supervisory Board members are listed in section 5 "Governing bodies of the company".
2) 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 2015 1) No. 085

in € thousands	Fixed remuneration	Remuneration for committee membership	Attendance fees	Total remuneration
Bänsch, Jürgen (until November 19, 2015) 2)	53	21	16	90
Bullinger, Prof. Dr. Hans-Jörg	60		7	67
Engelmann, Dr. Holger	60		7	67
Gottschalk, Prof. Dr. Bernd	60		7	67
Lenhard, Norbert 2)	60	24	16	100
Luther, Dr. Siegfried	60	48	12	120
Mittag, Dr. Reinold 2)	60	24	18	102
Mölkner, Thomas (until November 19, 2015) 2)	53		9	62
Münch, Yvonne (since November 19, 2015) 2)	7		2	9
Resch, Barbara (since November 19, 2015) 2)	7	1	4	12
Schaeffler, Georg F. W.	119	48	23	190
Schaeffler-Thumann, Maria-Elisabeth	89	24	12	125
Schmidt, Stefanie 2)	60		7	67
Spindler, Dirk	60		9	69
Stalker, Robin	60	24	16	100
Stolz, Jürgen 2)	60		9	69
Vicari, Salvatore 2)	60	24	18	102
Wechsler, Jürgen 2)	89	24	16	129
Wiesheu, Dr. Otto	60		9	69
Wolf, Prof. KR Ing. Siegfried	60	24	9	93
Worrich, Jürgen 2)	60	24	18	102
Zhang, Prof. Dr.-Ing. Tong	60		5	65
Total	**1,317**	**310**	**249**	**1,876**

1) All amounts shown include value-added tax on remuneration where applicable. The positions held by the Supervisory Board members are listed in section 5 "Governing bodies of the company".
2) These employee representatives have stated 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 2016 or 2015.

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 TÜV SÜD AG, Munich; deputy chairman of the supervisory board of WILO SE, Dortmund

Dr. Holger Engelmann

Chief Executive Officer of Webasto SE

Appointed: December 01, 2014
Committee memberships: Member of the nomination committee
Seats on supervisory and similar boards: Member of the supervisory board of Webasto Roof Systems China Ltd., Hong Kong, China (until October 18, 2016); chairman of the supervisory board of Webasto Thermo & Comfort SE, Gilching

* Employee representative on the Supervisory Board.

Prof. Dr. Bernd Gottschalk
Acting Partner of AutoValue GmbH

Appointed: December 01, 2014
Committee memberships: Member of the nomination committee
Seats on supervisory and similar boards: Member 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

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: Member of the supervisory board of Evonik Industries AG, Essen; member of the board of directors of Sparkasse Gütersloh, Gütersloh

Dr. Reinold Mittag*
Trade Union Secretary of IG Metall

Appointed: November 19, 2015
Committee memberships: Member of the audit committee

Yvonne Münch*
Manager Plant Purchase and Logistics

Appointed: November 19, 2015

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
Chief Financial Officer of adidas AG, Herzogenaurach

Appointed: December 01, 2014
Committee memberships: Member of the audit committee

Jürgen Stolz*
Chairman of the Works Council at the Bühl plant

Appointed: November 19, 2015

Salvatore Vicari*
Chairman of the Works Council at Homburg/Saar plant

Appointed: November 19, 2015
Committee memberships: Member of the audit committee

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: Chairman 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 (since June 24, 2016)

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

* Employee representative on the Supervisory Board.

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 eight members: the Chief Executive Officer (CEO), the CEOs of the two divisions Automotive and Industrial, 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; MOVE, Communications & Marketing; Investor Relations; Legal; Internal Audit; Corporate 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 supervisory board of FAG Bearings India Ltd., Mumbai, India

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

Responsible for: Corporate R&D Management; Corporate Innovation; R&D Processes, Methods & Tools; R&D Competence & Services; Intellectual Property & Rights; Surface Technology; Information Technology; 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

Dr. Ulrich Hauck
Chief Financial Officer

Responsible for: Finance Strategy, Processes & Infrastructure; Corporate Accounting; Corporate Controlling; Corporate Treasury; Corporate Taxes; Divisional Controlling Automotive; Divisional Controlling Industrial; Corporate Insurance
Appointed: April 01, 2015
Term of office ends: March 31, 2018
Seats on supervisory and similar boards: Member of the supervisory board of mutares AG, Munich

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 Operations
Appointed: October 24, 2014
Term of office ends: September 30, 2018
Seats on supervisory and similar boards: Member of the supervisory board of SupplyOn AG, Munich

Prof. Dr. Peter Pleus
CEO Automotive

Responsible for: Engine Systems and Chassis Systems business divisions; Global Key Account Management Automotive division; Business Development Automotive
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

* Employee representative on the Supervisory Board.

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; HR Functions; HR Automotive; HR Industrial
Appointed: January 01, 2016
Term of office ends: December 31, 2018

Dr. Stefan Spindler
CEO Industrial

Responsible for: Strategic Planning Sectors & Customers; Global Sales Industrial; Research & Development and Application Engineering; Operations and Supply Chain Management; Program "CORE"
Appointed: May 01, 2015
Term of office ends: April 30, 2018
Seats on supervisory and similar boards: Deputy Chairman of the supervisory board of Schaeffler Austria GmbH, Berndorf-St. Veit, Austria

Matthias Zink (since January 01, 2017)
CEO Automotive

Responsible for: Transmission Systems and Automotive Aftermarket business divisions; Research & Development Automotive division
Appointed: January 01, 2017
Term of office ends: December 31, 2019

The following member left the Board of Managing Directors in 2016

Norbert Indlekofer (until December 31, 2016)
CEO Automotive

Responsible for: Transmission Systems and Automotive Aftermarket business divisions; Research & Development Automotive division
Appointed: October 24, 2014
Term of office ended: December 31, 2016
Seats on supervisory and similar boards: Member of the supervisory board of Gienanth GmbH, Eisenberg

* Employee representative on the Supervisory Board.

Consolidated financial statements

1. Consolidated income statement

No. 086

in € millions	Note	2016	2015	Change in %
Revenue	3.1	13,338	13,179	1.2
Cost of sales		-9,552	-9,448	1.1
Gross profit		**3,786**	**3,731**	**1.5**
Research and development expenses		-751	-673	11.6
Selling expenses		-915	-920	-0.5
Administrative expenses		-428	-407	5.2
Other income	3.2	41	57	-28.1
Other expenses	3.3	-177	-386	-54.1
Earnings before financial result and income taxes (EBIT)		**1,556**	**1,402**	**11.0**
Financial income	3.5	220	327	-32.7
Financial expenses	3.5	-561	-874	-35.8
Financial result	**3.5**	**-341**	**-547**	**-37.7**
Earnings before income taxes		**1,215**	**855**	**42.1**
Income taxes	3.6	-343	-250	37.2
Net income		**872**	**605**	**44.1**
Attributable to shareholders of the parent company		859	591	45.3
Attributable to non-controlling interests		13	14	-7.1
Earnings per common share (basic/diluted, in €)	3.7	1.29	0.88	46.6
Earnings per common non-voting share (basic/diluted, in €)	3.7	1.30	1.28	1.6

2. Consolidated statement of comprehensive income

No. 087

in € millions	2016 before taxes	2016 taxes	2016 after taxes	2015 before taxes	2015 taxes	2015 after taxes
Net income	**1,215**	**-343**	**872**	**855**	**-250**	**605**
Foreign currency translation differences for foreign operations	59	0	59	103	0	103
Net change from hedges of net investments in foreign operations	-10	3	-7	-96	27	-69
Effective portion of changes in fair value of cash flow hedges [1)]	-9	3	-6	62	-16	46
Net change in fair value of available-for-sale financial assets	0	0	0	-1	0	-1
Total other comprehensive income (loss) that may be reclassified subsequently to profit or loss	**40**	**6**	**46**	**68**	**11**	**79**
Remeasurement of net defined benefit liability	-223	63	-160	87	-24	63
Total other comprehensive income (loss) that will not be reclassified to profit or loss	**-223**	**63**	**-160**	**87**	**-24**	**63**
Total other comprehensive income (loss)	**-183**	**69**	**-114**	**155**	**-13**	**142**
Total comprehensive income (loss) for the period	**1,032**	**-274**	**758**	**1,010**	**-263**	**747**
Total comprehensive income (loss) attributable to shareholders of the parent company	1,012	-267	745	985	-256	729
Total comprehensive income (loss) attributable to non-controlling interests	20	-7	13	25	-7	18

1) Including income of EUR 54 m (prior year: income of EUR 12 m) reclassified to profit and loss.

See Notes 4.11 and 4.14 to the consolidated financial statements for further detail.

3. Consolidated statement of financial position

No. 088

in € millions	Note	12/31/2016	12/31/2015	Change in %
ASSETS				
Intangible assets	4.1	632	589	7.3
Property, plant and equipment	4.2	4,507	4,180	7.8
Other financial assets	4.6	217	2,123	-89.8
Other assets	4.6	51	57	-10.5
Income tax receivables	4.3	0	4	- 100
Deferred tax assets	4.3	572	485	17.9
Total non-current assets		**5,979**	**7,438**	**-19.6**
Inventories	4.4	1,905	1,812	5.1
Trade receivables	4.5	2,218	2,023	9.6
Other financial assets	4.6	55	123	-55.3
Other assets	4.6	218	211	3.3
Income tax receivables	4.3	93	74	25.7
Cash and cash equivalents	4.7	1,071	799	34.0
Assets held for sale	4.8	25	0	-
Total current assets		**5,585**	**5,042**	**10.8**
Total assets		**11,564**	**12,480**	**-7.3**
SHAREHOLDERS' EQUITY AND LIABILITIES				
Share capital		666	666	0.0
Capital reserves		2,348	2,348	0.0
Other reserves		-404	-935	-56.8
Accumulated other comprehensive income (loss)		-713	-599	19.0
Equity attributable to shareholders of the parent company		**1,897**	**1,480**	**28.2**
Non-controlling interests		100	88	13.6
Total shareholders' equity	**4.9**	**1,997**	**1,568**	**27.4**
Provisions for pensions and similar obligations	4.11	2,182	1,942	12.4
Provisions	4.12	96	182	-47.3
Financial debt	4.10	3,704	5,685	-34.8
Income tax payables	4.3	163	210	-22.4
Other financial liabilities	4.13	86	12	› 100
Other liabilities	4.13	6	6	0.0
Deferred tax liabilities	4.3	124	107	15.9
Total non-current liabilities		**6,361**	**8,144**	**-21.9**
Provisions	4.12	354	431	-17.9
Financial debt	4.10	3	3	0.0
Trade payables	4.14	1,625	1,405	15.7
Income tax payables	4.3	176	112	57.1
Other financial liabilities	4.13	696	512	35.9
Other liabilities	4.13	344	305	12.8
Liabilities held for sale	4.8	8	0	-
Total current liabilities		**3,206**	**2,768**	**15.8**
Total shareholders' equity and liabilities		**11,564**	**12,480**	**-7.3**

4. Consolidated statement of cash flows

No. 089

in € millions	2016	2015	Change in %
Operating activities			
EBIT	1,556	1,402	11.0
Interest paid	-279	-508	-45.1
Interest received	98	43	› 100
Income taxes paid	-327	-358	-8.7
Depreciation, amortization and impairments	737	694	6.2
(Gains) losses on disposal of assets	4	-18	-
Changes in:			
• Inventories	-88	-75	17.3
• Trade receivables	-205	-79	› 100
• Trade payables	271	38	› 100
• Provisions for pensions and similar obligations	-29	-9	› 100
• Other assets, liabilities and provisions	138	242	-43.0
Cash flows from operating activities [1)]	**1,876**	**1,372**	**36.7**
Investing activities			
Proceeds from disposals of property, plant and equipment	4	26	-84.6
Capital expenditures on intangible assets	-29	-48	-39.6
Capital expenditures on property, plant and equipment	-1,117	-977	14.3
Other investing activities [2)]	1	-3	-
Cash used in investing activities	**-1,141**	**-1,002**	**13.9**
Financing activities			
Dividends paid to shareholders and non-controlling interests	-329	-251	31.1
Proceeds from issuing shares	0	810	
Receipts from loans	1,000	207	› 100
Repayments of loans	-2,910	-1,175	› 100
Other financing activities	1,773	197	› 100
Cash used in financing activities	**-466**	**-212**	**› 100**
Net increase (decrease) 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 as at end of period	**1,071**	**799**	**34.0**

[1)] Excluding interest payments, cash flows from operating activities for the period from January 01 to December 31, 2016 amount to EUR 2,155 m (prior year: EUR 1,880 m).
[2)] Including EUR 2 m of cash and cash equivalents acquired in the purchase of Compact Dynamics GmbH.

5. Consolidated statement of changes in equity

No. 090

in € millions	Share capital	Capital Reserves	Other Reserves	Accumulated other comprehensive income (loss)				Subtotal	Non-controlling interests	Total
				Translation reserve	Hedging reserve	Fair value reserve	Defined benefit plan remeasure-ment reserve			
Balance as at January 01, 2015	**600**	**1,600**	**-1,276**	**-109**	**-75**	**1**	**-554**	**187**	**71**	**258**
Net income			591					591	14	605
Other comprehensive income (loss)				30	46	-1	63	138	4	142
Total comprehensive income (loss) for the period	**0**	**0**	**591**	**30**	**46**	**-1**	**63**	**729**	**18**	**747**
Issuance of new shares	66	748						814		814
Dividends			-250					-250	-1	-251
Total amount of transactions with shareholders	**66**	**748**	**-250**					**564**	**-1**	**563**
Balance as at December 31, 2015	**666**	**2,348**	**-935**	**-79**	**-29**	**0**	**-491**	**1,480**	**88**	**1,568**
Balance as at January 01, 2016	**666**	**2,348**	**-935**	**-79**	**-29**	**0**	**-491**	**1,480**	**88**	**1,568**
Net income			859					859	13	872
Other comprehensive income (loss)				52	-6	0	-160	-114	0	-114
Total comprehensive income (loss) for the period	**0**	**0**	**859**	**52**	**-6**	**0**	**-160**	**745**	**13**	**758**
Dividends			-328					-328	-1	-329
Total amount of transactions with shareholders	**0**	**0**	**-328**					**-328**	**-1**	**-329**
Balance as at December 31, 2016	**666**	**2,348**	**-404**	**-27**	**-35**	**0**	**-651**	**1,897**	**100**	**1,997**

See Note 4.9 to the consolidated financial statements for further detail.

6. Consolidated segment information

(Part of the notes to the consolidated financial statements)

No. 091

	Automotive		Industrial		Total	
	01/01-12/31		01/01-12/31		01/01-12/31	
in € millions	**2016**	**2015**	**2016**	**2015**	**2016**	**2015**
Revenue	10,333	9,977	3,005	3,202	13,338	13,179
Cost of sales	-7,383	-7,206	-2,169	-2,242	-9,552	-9,448
Gross profit	2,950	2,771	836	960	3,786	3,731
EBIT	1,383	1,135	173	267	1,556	1,402
• in % of revenue	13.4	11.4	5.8	8.3	11.7	10.6
Depreciation, amortization and impairments	-544	-498	-193	-196	-737	-694
Inventories [1)]	1,228	1,164	677	648	1,905	1,812
Trade receivables [1)]	1,730	1,556	488	467	2,218	2,023
Property, plant and equipment [1)]	3,430	3,115	1,077	1,065	4,507	4,180
Additions to intangible assets and property, plant and equipment	902	880	213	238	1,115	1,118

Prior year information presented based on 2016 segment structure.
[1)] Amounts as at December 31.

See Note 5.4 to the consolidated financial statements for further detail.

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, 2016 comprise Schaeffler AG and its subsidiaries, investments in associated companies, and joint ventures (together referred to as "Schaeffler" or "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 Electronic Federal Gazette (Bundesanzeiger Verlag GmbH, Cologne) and published in the Electronic Federal Gazette.

1.2 Basis of preparation

In accordance with section 315a (1) HGB, the consolidated financial statements of the Schaeffler Group for the year ended December 31, 2016 have been compiled in accordance with International Financial Reporting Standards (IFRS) 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 non-current/current distinction.

In the past, customer payments for development services were presented in the consolidated income statement as service revenue. Starting in 2016, these customer payments are netted against the related development costs and reported under research and development expenses in the consolidated income statement. Figures for the comparison period for revenue (decrease of EUR 47 m) and research and development expenses (decrease of EUR 47 m) were adjusted retrospectively. The change was made to provide better financial information and to bring the presentation into line with common industry practice.

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,
- determination of valuation allowances on inventories,
- identification of cash-generating units and determination of recoverable amounts for purposes of impairment tests of goodwill and non-current assets,
- accounting for post-employment employee benefits, especially selecting actuarial assumptions,
- recognition and measurement of provisions,
- determination of fair values of financial debt and derivatives,
- assessment of the recoverability of deferred tax assets, and
- share-based payment.

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 2016. The discount rate used to measure defined benefit pension obligations was reduced to reflect lower 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 have been consolidated in the company's consolidated financial statements. Subsidiaries are entities directly or indirectly controlled by Schaeffler AG. Subsidiaries are consolidated in the consolidated financial statements from the date Schaeffler 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

Selected foreign exchange rates No. 092

Currencies		Closing rates		Average rates	
1 € in		12/31/2016	12/31/2015	2016	2015
CNY	China	7.32	7.06	7.35	6.97
INR	India	71.45	72.02	74.38	71.18
KRW	South Korea	1,270.57	1,280.78	1,284.51	1,255.73
MXN	Mexico	21.79	18.92	20.66	17.60
USD	U.S.A.	1.05	1.09	1.11	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 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 Schaeffler,
- the costs associated with the transaction can be measured reliably,
- Schaeffler 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.

Newly issued shares are reflected in the calculation of the average number of shares outstanding on a pro rata temporis basis from the date they were entered in the Commercial Register. However, as these new shares are entitled to profits for the full year, consolidated net income attributable to the new shares was included in full. In addition, the average number of shares outstanding and, hence, earnings per share for all periods presented were adjusted retrospectively for the share split and the conversion of common shares to common non-voting shares.

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. Recoverable amount is determined using the discounted cash flow method and is the higher of fair value less costs of disposal and value in use of the cash-generating unit. 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 time frame. 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 additions to intangible assets and property, plant and equipment. Please refer to the report on expected developments in the group management report for further detail. 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. Schaeffler'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 recoverable amount under the value in use concept using the discounted cash flow method. If value in use does not exceed the carrying amount of the cash-generating unit, 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.

Schaeffler 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 delinquency 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.

Cash and cash equivalents are accounted for at cost.

Financial liabilities

Except for derivative financial instruments, Schaeffler 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 included 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 12 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.

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 interest rates of 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 Schaeffler 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. Interest expense on provisions for pensions and similar obligations and the return on plan assets are considered separately for each plan and presented in financial result on a net basis.

For defined contribution plans, Schaeffler 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 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 generally accepted financial valuation models. The fair value is recognized as personnel expense over the relevant vesting period.

1.4 New accounting pronouncements

The new Standards and amendments of Standards initially effective starting in 2016 have not had a significant 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 2016, and none were adopted early.

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. Earlier application is permitted, but Schaeffler does not plan to apply the standard early.

IFRS 9 introduces a uniform approach to the classification and measurement of financial assets. The classification criteria are the cash flow characteristics and the business model for managing the financial assets. IFRS 9 also introduces a new impairment model for financial assets including trade receivables.

The standard replaces the current incurred loss model with the expected loss model. The hedge accounting requirements were revised to allow financial statements to better reflect the company's risk management strategy. The standard also requires additional quantitative and qualitative note disclosures. Detailed statements regarding the extent of the impact on the Schaeffler Group's consolidated financial statements are currently not yet possible, as the analysis of the implementation of the new standard has not yet been completed.

In May 2014, the IASB issued the new revenue recognition standard IFRS 15 Revenue from Contracts with Customers, merging its existing revenue recognition guidance, which was previously contained in several standards (IAS 18 Revenue and IAS 11 Construction contracts) and interpretations (IFRIC 13, IFRIC 15, IFRIC 18, and SIC 31), into one comprehensive standard. In addition, the IASB issued Clarifications to IFRS 15 in April 2016, which addressed initial implementation issues (including identification of separate performance obligations) and provided additional practical expedients to the transition requirements. The standard is effective for annual reporting periods beginning on or after January 01, 2018. Earlier application is permitted. 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 the date of initial application, January 01, 2018.

IFRS 15 is applicable to all contracts, as defined in the standard, with customers for the sale of goods or the rendering of services, and includes a uniform five-step model that is applicable to all industries and is used to determine the amount of revenue and the timing of revenue recognition. The core principle of the new standard is that an entity recognizes revenue in an amount that reflects the consideration to which the entity expects to be entitled in exchange for transferring goods or services to a customer. Revenue is recognized when the customer obtains control of the goods or services.

In 2016, the Schaeffler Group initiated a project to implement IFRS 15. The initial project stage consisted of analyzing the impact of the requirements of IFRS 15 at the level of the group's identified homogeneous business models. The company currently expects only limited changes in the total amount of revenue recognized for a contract with a customer. However, depending on the contractual features of customer contracts (which may need to be combined), the timing of revenue recognition may change. As a result, depending on the features of contractual cancellation clauses and on the degree to which the goods or services sold are specific to the customer, which may result in a lack of alternative use of individual products, it may be necessary to recognize revenue over a period of time, which is not required under the current requirements. In addition, for certain types of contracts, separating performance obligations as required under certain conditions and the resulting allocation of the transaction price may result in earlier revenue recognition for activities occurring prior to volume production (especially Tool Shop). Also, it is possible that variable components of consideration and the identification of additional separate performance obligations may lead to shifts in the timing of revenue recognition. Apart from the issues described above, the Schaeffler Group expects changes in the presentation of its statement of financial position, especially regarding the separate line items for contract assets and contract liabilities required by IFRS 15. The standard also requires additional quantitative and qualitative note disclosures.

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. 093

Standard/Interpretation		Effective date	Subject of Standard/Interpretation or amendment	Expected impact on the Schaeffler Group
Annual Improvements 2014-2016		01/01/2017/ 01/01/2018	Various improvements to IFRS 1, IFRS 12 and IAS 28	none
Amendments to IAS 7	Statement of Cash Flows	01/01/2017	Improved disclosures about an entity's debt	Scope of disclosures related to statement of cash flows
Amendments to IAS 12	Recognition of Deferred Tax Assets	01/01/2017	Clarification that decreases below cost in the carrying amount of debt instruments measured at fair value resulting from a change in market interest rates give rise to deductible temporary differences	none
Amendments to IFRS 2	Share-based Payments	01/01/2018	Changes regarding arrangements with a net settlement feature and modifications that change classification	Under examination [1]
Clarification to IFRS 15	Revenue from Contracts with Customers	01/01/2018	Clarifications regarding several issues	Under examination [1]
IFRS 16	Leases	01/01/2019	Capitalization of all leasing arrangements with few exceptions	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 2016, the consolidated financial statements of Schaeffler AG cover, in addition to Schaeffler AG, 152 (prior year: 153) subsidiaries; 51 (prior year: 51) entities are domiciled in Germany and 101 (prior year: 102) in other countries.

SIA "Schaeffler Baltic", Riga, Latvia (until December 31, 2016: NACO Technologies SIA) and Compact Dynamics GmbH, Starnberg, were consolidated for the first time in 2016. A disposal (Schaeffler Motorenelemente AG & Co. KG, Herzogenaurach) and two internal mergers have reduced the scope of consolidation.

In the consolidated financial statements as at December 31, 2016, five (prior year: five) investments (including two joint ventures; prior year: two) are accounted for at equity.

Please refer to Note 5.9 for further detail on the Schaeffler Group's companies.

2.2 Acquisitions and disposals of companies and business operations

Acquisition of companies

On December 20, 2016, Schaeffler Technologies AG & Co. KG acquired 51 % of the shares and voting interests in Compact Dynamics GmbH, Starnberg, from SEMIKRON International GmbH. The acquiree engages in the development and batch production of electric drive systems. For simplification purposes, the company was consolidated beginning on December 31, 2016. Had the company been consolidated effective January 01, 2016, consolidated revenue would have increased by EUR 9 m and consolidated net income by EUR 1 m.

In determining net income, the company did not assume that the excess of fair values over carrying amounts capitalized in the purchase price allocation as at the acquisition date would have been the same had the business combination occurred on January 01, 2016. The company was assigned to the Automotive division and, therefore, to the Automotive segment.

The consideration transferred had a fair value of EUR 45 m at the acquisition date. This resulted in a liability of EUR 23 m (payable in cash) for the 51 % interest acquired and a contingent purchase price payable of EUR 22 m for the shares remaining with SEMIKRON International GmbH for the time being. The contingent purchase price payable was measured at fair value and results from a combined symmetric put/call option for the remaining shares. The fair value of the contingent purchase price payable was determined based on the contractual exercise price and the expected exercise date. As the symmetric options with largely identical conditions represent a forward contract when viewed in combination, in substance, the Schaeffler Group has present ownership of the shares underlying the options. Therefore, the company has anticipated the exercise of the option and recognized a financial liability rather than a non-controlling interest.

The allocation of the purchase price resulted in EUR 41 m in goodwill and a minor amount of intangible assets (carrying amount as at December 31, 2016: EUR 0 m, fair value as at December 31, 2016: EUR 1 m). The goodwill, which is not deductible for tax purposes, represents factors that are not separable and, therefore, cannot be separately recognized under IFRS; these factors are, in particular, the know-how of the workforce of Compact Dynamics GmbH and expected income from synergies in development and manufacturing, the main reasons behind the transaction.

Receivables assumed in the transaction had a carrying amount of EUR 1 m as at December 31, 2016, which was equal to fair value. The carrying amounts of the remaining assets and liabilities assumed are equal to their fair value. Total identifiable net assets amounted to EUR 4 m as at December 31, 2016.

The transaction did not have any further impact on the Schaeffler Group's net assets, financial position and earnings as at December 31, 2016.

Disposals of companies and business operations

In a contract signed on December 21, 2016, the Schaeffler Group agreed to sell its interest and voting interest in Schaeffler Motorenelemente AG & Co. KG to the Weber Group effective December 31, 2016. The company specializes in the mechanical processing of cylinder heads and other complex housings, which are not an integral part of the Schaeffler Group's core business. The disposal transaction resulted in a loss of EUR 13 m, which is included in other expenses, and eliminated EUR 18 m in assets and EUR 5 m in liabilities from the statement of financial position.

Further, Schaeffler Schweiz GmbH plans to sell its fine blanking activities to Swiss Güntensperger Group in an asset deal. The sale agreement was signed in November 2016, but is subject to several conditions. The transaction is expected to close in the second quarter of 2017. Since the company is committed to the sale and the sale is highly probable to occur within twelve months, the assets and liabilities concerned are classified as assets held for sale in accordance with IFRS 5 as at December 31, 2016.

3. Notes to the consolidated income statement

3.1 Revenue

Revenue No. 094

in € millions	2016	2015
Revenue from the sale of goods	13,193	13,044
Other revenue	145	135
Total	**13,338**	**13,179**

Other revenue primarily includes EUR 96 m (prior year: EUR 86 m) in revenue from the sale of tools and machines constructed by the company as well as EUR 38 m (prior year: EUR 45 m) from services.

3.2 Other income

Other income No. 095

in € millions	2016	2015
Gains on disposal of assets	1	23
Miscellaneous income	40	34
Total	**41**	**57**

3.3 Other expenses

Other expenses No. 096

in € millions	2016	2015
Exchange losses	9	40
Miscellaneous expenses	168	346
Total	**177**	**386**

Foreign exchange losses consisted largely of exchange losses from operations and exchange losses related to forward exchange contracts. In 2016, netting foreign exchange gains and losses resulted in a net exchange loss of EUR 9 m (prior year: EUR 40 m).

Miscellaneous other expenses include EUR 45 m (prior year: EUR 36 m) in expenses related to the stepped-up efficiency measures aimed at revitalizing the Industrial division under the second wave of the program “CORE”. Another EUR 86 m in expenses were attributable to potential third party claims in connection with antitrust proceedings and other compliance cases. The prior year included EUR 238 m related to a provision for legal risks recognized for potential third party claims in connection with the EU antitrust proceedings finalized in March 2014.

3.4 Personnel expense and headcount

Average number of employees by region No. 097

	2016	2015
Europe	59,609	58,496
Americas	12,563	12,662
Greater China	10,778	10,037
Asia/Pacific	2,783	2,735
Total	**85,733**	**83,930**

The number of employees at December 31, 2016 was 86,662, 2.9 % above the prior year level of 84,198.

The Schaeffler Group's personnel expense can be analyzed as follows:

Personnel expense No. 098

in € millions	2016	2015
Wages and salaries	3,388	3,253
Social security contributions	665	621
Other personnel expense	114	116
Total	**4,167**	**3,990**

The increase in personnel expense in 2016 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 110 m (prior year: EUR 109 m) in retirement benefit expenses.

3.5 Financial result

Schaeffler Group financial result No. 099

in € millions	2016	2015
Interest expense on financial debt [1]	-286	-513
Interest income on shareholder loans	49	72
Foreign exchange gains and losses	-12	-224
Fair value changes and compensation payments on derivatives	-21	234
Fair value changes on embedded derivatives	-30	-79
Interest income and expense on pensions and partial retirement obligations	-45	-42
Other	4	5
Total	**-341**	**-547**

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

Interest expense on financial debt amounted to EUR 286 m in 2016 (prior year: EUR 513 m) and includes EUR 48 m in prepayment penalties and EUR 31 m in deferred transaction costs derecognized. Please refer to the chapter entitled "Current and non-current financial debt" for further detail. The prior year amount included prepayment penalties of EUR 173 m and EUR 23 m in deferred transaction costs derecognized in connection with the early redemption of bonds.

Interest income on shareholder loans earned on a loan receivable from IHO Verwaltungs GmbH (until September 27, 2016: Schaeffler Verwaltung Zwei GmbH), was EUR 49 m (prior year: EUR 72 m).

Net **foreign exchange** losses on financial assets and liabilities amounted to EUR 12 m (prior year: losses of EUR 224 m) and resulted primarily from translating financing instruments denominated in U.S. Dollar to Euro. The company has hedged these instruments using cross-currency derivatives and reports the resulting losses of EUR 21 m (prior year: gains of EUR 234 m) under **fair value changes and compensation payments on derivatives**. The losses largely relate to the early termination of cross-currency derivatives.

Fair value changes on embedded derivatives, primarily prepayment options for external financing instruments, resulted in net losses of EUR 30 m (prior year: EUR 79 m), comprising EUR 79 m in losses related to prepayment options written off in connection with the refinancing transactions in 2016, partially offset by EUR 49 m in gains resulting from changes in the fair value of the remaining prepayment options.

3.6 Income taxes

Income taxes — No. 100

in € millions	2016	2015
Current income taxes	345	287
Deferred income taxes	-2	-37
Income taxes	**343**	**250**

As a corporation, Schaeffler AG was subject to German corporation and trade taxes during the reporting period 2016.

The average domestic tax rate was 28.6 % in 2016 (prior year: 28.4 %). 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: 12.5 %).

The current income tax benefit related to prior years amounted to EUR 13 m (prior year: EUR 24 m) in 2016. Schaeffler incurred EUR 6 m in deferred tax expense related to prior years (prior year: EUR 17 m) in 2016.

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 2016 is based on the Schaeffler Group's 28.6 % (prior year: 28.4 %) effective combined trade and corporation tax rate including solidarity surcharge.

Tax rate reconciliation — No. 101

in € millions	2016	2015
Earnings before income taxes	1,215	855
Expected tax expense	**348**	**243**
Addition/reduction due to deviating local tax bases	5	7
Foreign/domestic tax rate differences	-19	-14
Change in tax rate and law	-2	-1
Non-recognition of deferred tax assets	4	-1
Tax credits and other tax benefits	-11	-6
Non-deductible expenses	32	26
Taxes for previous years	-7	-7
Other	-7	3
Reported tax expense	**343**	**250**

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 tax-free income includes non-deductible operating expenses and deferred tax liabilities on dividends expected to be paid by subsidiaries.

3.7 Earnings per share

Earnings per share — No. 102

in € millions	2016	2015
Net income	872	605
Net income attributable to shareholders of the parent company	859	591
Earnings attributable to common shares (basic/diluted)	644	442
Earnings attributable to common non-voting shares (basic/diluted)	215	149
Average number of common shares issued in millions	500	500
Average number of common non-voting shares issued in millions	166	116
Earnings per common share (basic/diluted, in €)	**1.29**	**0.88**
Earnings per common non-voting share (basic/diluted, in €)	**1.30**	**1.28**

There were no dilutive items at December 31, 2016 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 amounted to EUR 319 m (prior year: EUR 275 m) for the Automotive segment and EUR 208 m (prior year: EUR 208 m) for the Industrial segment. The addition of EUR 44 m in the Automotive segment resulted from the acquisition of Compact Dynamics GmbH.

For purposes of determining recoverable amount, cash flows beyond the detailed forecasting horizon of 2019 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, Schaeffler uses an assumed pre-tax interest rate of 12.6 % (prior year: 13.3 %) as the weighted average cost of capital for the Automotive segment and 12.6 % (prior year: 13.5 %) for the Industrial segment. This corresponds to a post-tax interest rate of 8.9 % for the Automotive segment (prior year: 9.4 %) and 8.9 % for the Industrial segment (prior year: 9.4 %).

As the value in use of each of the cash-generating units exceeded their carrying amount both for 2016 and the prior year, they were not impaired.

Internally generated intangible assets consist largely of development costs of EUR 47 m (prior year: EUR 37 m), including EUR 22 m (prior year: EUR 5 m) in assets not yet available for use that were not yet subject to amortization.

Amortization of intangible assets totaled EUR 31 m (prior year: EUR 31 m) and was recognized in the following line items in the consolidated income statement: Cost of sales EUR 8 m (prior year: EUR 5 m), research and development expenses EUR 5 m (prior year: EUR 4 m), selling expenses EUR 0 m (prior year: EUR 2 m), and administrative expenses EUR 18 m (prior year: EUR 20 m).

Intangible assets

No. 103

in € millions	Goodwill	Purchased intangible assets	Internally generated intangible assets	Total
Historical cost				
Balance as at January 01, 2015	**483**	**1,029**	**275**	**1,787**
Additions from initial consolidation of subsidiaries	0	0	0	0
Additions	0	47	23	70
Disposals	0	-9	-12	-21
Transfers	0	2	6	8
Foreign currency translation	0	3	1	4
Balance as at December 31, 2015	**483**	**1,072**	**293**	**1,848**
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**
Accumulated amortization and impairment losses				
Balance as at January 01, 2015	**0**	**1,001**	**231**	**1,232**
Additions from initial consolidation of subsidiaries	0	0	0	0
Amortization	0	16	15	31
Impairments	0	0	0	0
Impairment reversals	0	0	0	0
Disposals	0	-7	0	-7
Transfers	0	0	0	0
Foreign currency translation	0	3	0	3
Balance as at December 31, 2015	**0**	**1,013**	**246**	**1,259**
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
Impairments	0	0	0	0
Impairment reversals	0	0	0	0
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**
Net carrying amounts				
As at January 01, 2015	**483**	**28**	**44**	**555**
As at December 31, 2015	**483**	**59**	**47**	**589**
As at January 01, 2016	**483**	**59**	**47**	**589**
As at December 31, 2016	**527**	**54**	**51**	**632**

4.2 Property, plant and equipment

Property, plant and equipment No. 104

in € millions	Land, land rights and buildings	Technical equipment and machinery	Other equipment	Assets under construction	Total
Historical cost					
Balance as at January 01, 2015	**2,336**	**7,254**	**970**	**543**	**11,103**
Additions from initial consolidation of subsidiaries	0	0	0	0	0
Disposals of subsidiaries	0	0	0	0	0
Additions	43	391	83	531	1,048
Disposals	-15	-185	-44	-2	-246
Transfers	56	322	32	-418	-8
Reclassification to IFRS 5	0	0	0	0	0
Foreign currency translation	28	54	9	9	100
Balance as at December 31, 2015	**2,448**	**7,836**	**1,050**	**663**	**11,997**
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**
Accumulated depreciation and impairment losses					
Balance as at January 01, 2015	**1,209**	**5,373**	**768**	**5**	**7,355**
Additions from initial consolidation of subsidiaries	0	0	0	0	0
Disposals of subsidiaries	0	0	0	0	0
Depreciation	79	510	74	0	663
Impairments	0	0	0	0	0
Disposals	-9	-178	-43	-1	-231
Transfers	0	0	0	0	0
Reclassification to IFRS 5	0	0	0	0	0
Foreign currency translation	11	14	6	-1	30
Balance as at December 31, 2015	**1,290**	**5,719**	**805**	**3**	**7,817**
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
Impairments	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**
Net carrying amounts					
As at January 01, 2015	**1,127**	**1,881**	**202**	**538**	**3,748**
As at December 31, 2015	**1,158**	**2,117**	**245**	**660**	**4,180**
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**

At December 31, 2016, the Schaeffler Group had open commitments under fixed contracts to purchase property, plant and equipment of EUR 320 m (prior year: EUR 352 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. 105

in € millions	12/31/2016 Deferred tax assets	12/31/2016 Deferred tax liabilities	12/31/2015 Deferred tax assets	12/31/2015 Deferred tax liabilities
Intangible assets	3	-22	4	-22
Property, plant and equipment	98	-175	94	-156
Financial assets	2	-13	1	-15
Inventories	110	-4	98	-6
Trade receivables and other assets	64	-108	51	-146
Provisions for pensions and similar obligations	406	-35	328	-30
Other provisions and other liabilities	189	-82	219	-87
Interest- and loss carryforwards	15	0	45	0
Deferred taxes (gross)	**887**	**-439**	**840**	**-462**
Netting	-315	315	-355	355
Deferred taxes (net)	**572**	**-124**	**485**	**-107**

The group had gross carryforwards under the interest deduction cap of EUR 10 m (prior year: EUR 103 m) at the end of the reporting period. The company has recognized deferred tax assets on all interest carryforwards.

At December 31, 2016, the Schaeffler Group had gross loss carryforwards of EUR 115 m (prior year: EUR 115 m) for corporation tax and EUR 9 m (prior year: EUR 6 m) for trade tax, including EUR 92 m (prior year: EUR 66 m) in corporation tax losses and EUR 9 m (prior year: EUR 6 m) in trade tax losses for which no deferred taxes have been recognized.

The majority of the unrecognized loss carryforwards can be carried forward for a limited period. The remaining interest carryforwards can be utilized indefinitely.

No deferred tax assets were recognized on EUR 7 m (prior year: EUR 8 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 1,694 m (prior year: EUR 1,717 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 1 m (prior year: EUR 18 m). Recovery of these deferred tax assets is considered probable since sufficient taxable profits are expected in the future.

At December 31, 2016, the amount of deferred taxes recognized in accumulated other comprehensive income was EUR 328 m (prior year: EUR 259 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, 2016, income tax receivables amounted to EUR 93 m (prior year: EUR 78 m) and did not include any non-current balances (prior year: EUR 4 m).

At December 31, 2016, income tax payables amounted to EUR 339 m (prior year: EUR 322 m), including non-current balances of EUR 163 m (prior year: EUR 210 m). The reduction in non-current income tax payables compared to the prior year is mainly the result of a reclassification between non-current and current income tax payables.

4.4 Inventories

Inventories No. 106

in € millions	12/31/2016	12/31/2015
Raw materials and supplies	358	343
Work in progress	468	452
Finished goods and merchandise	1,078	1,015
Advance payments	1	2
Total	**1,905**	**1,812**

EUR 9,413 m (prior year: EUR 9,319 m) in inventories used were expensed as cost of sales in the consolidated income statement in 2016.

The impairment allowance on inventories amounted to EUR 260 m (prior year: EUR 234 m) as at December 31, 2016.

4.5 Trade receivables

Trade receivables No. 107

in € millions	12/31/2016	12/31/2015
Trade receivables (gross)	**2,243**	**2,051**
Impairment allowances	-25	-28
Trade receivables (net)	**2,218**	**2,023**

Movements in impairment allowances on these trade receivables can be reconciled as follows:

Impairment allowances on trade receivables No. 108

in € millions	2016	2015
Impairment allowances as at January 01	**-28**	**-24**
Additions	-3	-9
Allowances used to cover write-offs	3	2
Reversals	3	3
Impairment allowances as at December 31	**-25**	**-28**

Trade receivables of EUR 2,079 m (prior year: EUR 1,884 m) were neither past due nor impaired as at December 31, 2016.

Also as at December 31, 2016, trade receivables of EUR 113 m (prior year: EUR 117 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 51 m (prior year: EUR 50 m), and the related impairment allowance was EUR -25 m (prior year: EUR -28 m).

Trade receivables pledged as security under loan and bond agreements were released from such pledges under a security release agreement dated August 18, 2016. The company still had receivables of EUR 201 m (prior year: EUR 999 m) that were pledged as security as at December 31, 2016.

The Schaeffler Group's exposure to counterparty, currency and liquidity risk related to trade receivables is disclosed in Note 4.14.

4.6 Other financial assets and other assets

Other financial assets (non-current/current) No. 109

	12/31/2016			12/31/2015		
in € millions	Non-current	Current	Total	Non-current	Current	Total
Loans receivable and financial receivables	3	0	3	1,775	0	1,775
Derivative financial assets	175	29	204	309	53	362
Miscellaneous other financial assets	39	26	65	39	70	109
Total	**217**	**55**	**272**	**2,123**	**123**	**2,246**

The EUR 1,773 m loan receivable from IHO Verwaltungs GmbH as at December 31, 2015 was fully repaid in 2016. Please refer to Note 5.5 for further detail.

At December 31, 2016, **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.

Other financial assets pledged as security under loan and bond agreements in the prior year were released in full from such pledges under a security release agreement dated August 18, 2016 (prior year: EUR 2,081 m).

The Schaeffler Group's exposure to currency and liquidity risk related to other financial assets is disclosed in Note 4.14 on financial instruments.

Other assets (non-current/current) No. 110

	12/31/2016			12/31/2015		
in € millions	Non-current	Current	Total	Non-current	Current	Total
Pension asset	21	0	21	34	0	34
Tax receivables	1	171	172	1	175	176
Miscellaneous other assets	29	47	76	22	36	58
Total	**51**	**218**	**269**	**57**	**211**	**268**

Tax receivables consisted predominantly of value-added tax refunds receivable.

The majority of **miscellaneous other assets** represented the current and non-current portions of prepaid assets and deferred charges.

Other assets pledged as security under loan and bond agreements in the prior year were released in full from such pledges under a security release agreement dated August 18, 2016 (prior year: EUR 1 m).

4.7 Cash and cash equivalents

At December 31, 2016, cash and cash equivalents consisted primarily of bank balances.

At the end of the reporting period, cash and cash equivalents include EUR 325 m (prior year: EUR 198 m) held by subsidiaries in Argentina, Brazil, Chile, China, Colombia, India, Peru, the Philippines, South Korea, South Africa, Taiwan, Thailand, Venezuela, and 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.

Cash and cash equivalents pledged as security under loan and bond agreements in the prior year were released in full from such pledges under a security release agreement dated August 18, 2016 (prior year: EUR 449 m).

4.8 Assets held for sale and liabilities associated with assets held for sale

Assets and liabilities held for sale are related to the planned sale of the fine blanking activities of Schaeffler Schweiz GmbH, which is scheduled to close in the second quarter of 2017.

The company has written the disposal group down to the lower of its carrying amount and fair value less costs to sell, resulting in an impairment loss of EUR 4 m which has been recognized in other expenses. The impairment loss has reduced the carrying amount of the non-current assets included in the disposal group.

The disposal group related to the fine blanking activities of Schaeffler Schweiz GmbH is largely part of the Automotive segment and includes assets held for sale of EUR 25 m; EUR 14 m of these assets are non-current while EUR 11 m are current. The associated liabilities held for sale of EUR 8 m consist of EUR 3 m in non-current and EUR 5 m in current payables and provisions.

Other comprehensive income includes accumulated losses of EUR 2 m related to the disposal group.

The disposal group was measured at fair value on a non-recurring basis; this measurement was classified as a Level 1 measurement of fair value, based on the inputs of the valuation techniques used.

4.9 Shareholders' equity

Shareholders' equity No. 111

in € millions	12/31/2016	12/31/2015
Share capital	666	666
Capital reserves	2,348	2,348
Other reserves	-404	-935
Accumulated other comprehensive income (loss)	-713	-599
Equity attributable to shareholders of the parent company	**1,897**	**1,480**
Non-controlling interests	100	88
Total shareholders' equity	**1,997**	**1,568**

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, 2016.

Capital reserves remain unchanged at EUR 2,348 m as at December 31, 2016.

The change in **other reserves** in 2016 was 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 2016, a dividend of EUR 328 m will be proposed to the Schaeffler AG annual general meeting. EUR 83 m of this dividend relates to the common non-voting shares. This represents a total dividend of EUR 0.50 (prior year: EUR 0.35; special dividend EUR 0.15) per common non-voting share and EUR 0.49 (prior year: EUR 0.34; special dividend EUR 0.15) 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 mainly consisted of the impact of currency translation, changes in the fair value of financial instruments designated as hedging instruments and of available-for-sale financial assets, as well as remeasurements of pensions and similar obligations.

At December 31, 2016, **non-controlling interests** related primarily to third-party interests in the equity of FAG Bearings India Ltd., India, which do not convey control to the holder.

4.10 Current and non-current financial debt

Financial debt (non-current/current) No. 112

in € millions	12/31/2016 Total	Due in up to 1 year	Due in more than 1 year	12/31/2015 Total	Due in up to 1 year	Due in more than 1 year
Bonds	2,719	0	2,719	5,048	0	5,048
Facilities Agreement	982	0	982	632	0	632
Other financial debt	6	3	3	8	3	5
Financial debt	**3,707**	**3**	**3,704**	**5,688**	**3**	**5,685**

The decrease in financial debt compared to December 31, 2015 was primarily attributable to repayments, redemptions, and refinancing transactions. These were partially offset by the impact of currency translation on financial debt denominated in U.S. Dollar.

In May 2016, Schaeffler AG voluntarily prepaid approximately EUR 229 m of its institutional loan tranches. The company paid off EUR 85 m of its Senior Term Loan B EUR and USD 160 m of its Senior Term Loan B USD.

In July 2016, Schaeffler AG refinanced its institutional loan tranches. The new Facilities Agreement consists of a EUR 1.0 bn term loan and a EUR 1.3 bn revolving credit facility. The funds were used to repay the existing loan tranches totaling approximately EUR 418 m. The company paid off EUR 165 m of its Senior Term Loan B EUR and USD 280 m of its Senior Term Loan B USD. A further portion of the funds was used to redeem EUR bonds with a principal of EUR 600 m on August 18, 2016.

On October 07, 2016, the Schaeffler Group fully redeemed USD bonds with a principal of USD 850 m, and on October 13, 2016, it redeemed two EUR bonds with a principal of EUR 500 m each. The bond redemptions were largely funded using the proceeds of the prepayment of a loan receivable from the company's shareholder IHO Verwaltungs GmbH in September 2016.

At December 31, 2016, the group's debt consisted of a loan tranche with a principal of EUR 1.0 bn, five bond series totaling the equivalent of approximately EUR 2,733 m and a revolving line of credit with a principal of EUR 1.3 bn.

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 Schaeffler Group's Facilities Agreement consisted of the following loan tranches at December 31, 2016:

Facilities Agreement Schaeffler Group No. 113

Tranche	Currency	Face value in millions 12/31/2016	12/31/2015	Carrying amount in € millions 12/31/2016	12/31/2015	Coupon 12/31/2016	12/31/2015	Maturity
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.

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. 114

ISIN	Currency	Face value in millions 12/31/2016	12/31/2015	Carrying amount in € millions 12/31/2016	12/31/2015	Coupon	Maturity
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 differences between face value 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 27 m (prior year: EUR 39 m) in interest accrued on the bonds up to December 31, 2016 are reported in other financial liabilities (see Note 4.13).

Both the Facilities Agreement and the bond agreements contain certain constraints including a requirement to meet certain financial covenants. The financial covenant relevant to the Facilities Agreement is a leverage covenant. The creditors are entitled to call the debt prior to maturity under certain circumstances, including if the covenant is not met, which would result in the debt becoming due immediately.

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 defined contribution plans. While defined contribution plans generally entail no further obligation beyond the regular contributions included in personnel expense, defined benefit pension 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 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 benefits in the form of pension units largely result from Schaeffler's Company Pension Scheme ("Schaeffler Versorgungsordnung") and similar schemes that base the amount of the pension unit 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. 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, Schaeffler 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 pension 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 2016, approximately 74 % (prior year: 73 %) of pension obligations in the U.S. and approximately 104 % (prior year: 113 %) 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 obligation

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, 2016:

Amounts recognized in the statement of financial position for pensions and similar obligations No. 115

	12/31/2016					12/31/2015				
in € millions	Germany	U.S.A.	United Kingdom	Other countries	Total	Germany	U.S.A.	United Kingdom	Other countries	Total
Provisions for pensions (liabilities net of related plan assets)	-2,029	-58	-4	-91	-2,182	-1,778	-59	-1	-104	-1,942
Pension asset (plan assets net of related liabilities)	7	0	12	2	21	7	0	26	1	34
Net defined benefit liability	**-2,022**	**-58**	**8**	**-89**	**-2,161**	**-1,771**	**-59**	**25**	**-103**	**-1,908**

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. 116

	12/31/2016					12/31/2015				
in € millions	Germany	U.S.A.	United Kingdom	Other countries	Total	Germany	U.S.A.	United Kingdom	Other countries	Total
Present value of defined benefit obligations (active members)	-1,224	-84	0	-204	-1,512	-1,005	-84	0	-218	-1,307
Present value of defined benefit obligations (deferred members)	-141	-27	-166	-4	-338	-108	-27	-134	-4	-273
Present value of defined benefit obligations (pensioners)	-825	-115	-65	-26	-1,031	-806	-112	-70	-26	-1,014
Present value of defined benefit obligations (total)	**-2,190**	**-226**	**-231**	**-234**	**-2,881**	**-1,919**	**-223**	**-204**	**-248**	**-2,594**
Fair value of plan assets	168	168	239	145	720	148	164	229	145	686
Net defined benefit liability	**-2,022**	**-58**	**8**	**-89**	**-2,161**	**-1,771**	**-59**	**25**	**-103**	**-1,908**

Movements in the net defined pension benefit liability in 2016 can be reconciled as follows:

Reconciliation of net defined benefit liability/asset January 01/December 31 No. 117

					2016					2015
in € millions	Germany	U.S.A.	United Kingdom	Other countries	Total	Germany	U.S.A.	United Kingdom	Other countries	Total
Net defined benefit liability (-)/ asset (+) as at January 01	**-1,771**	**-59**	**25**	**-103**	**-1,908**	**-1,793**	**-63**	**3**	**-95**	**-1,948**
Benefits paid	58	1	0	9	68	59	0	0	6	65
Service cost	-56	0	0	-19	-75	-56	-1	0	-20	-77
Net interest on net defined benefit liability	-42	-2	1	-2	-45	-38	-2	1	-2	-41
Employer contributions	12	0	0	12	24	-4	9	0	10	15
Employee contributions	1	0	0	0	1	0	0	0	0	0
Transfers in/out	0	-2	0	0	-2	-17	-1	17	0	-1
Remeasurement of net defined benefit liability	-224	6	-15	10	-223	76	5	5	1	87
Business combinations/disposals	0	0	0	2	2	0	0	0	0	0
Changes in foreign exchange rates	0	-2	-3	2	-3	2	-6	-1	-3	-8
Net defined benefit liability (-)/ asset (+) as at December 31	**-2,022**	**-58**	**8**	**-89**	**-2,161**	**-1,771**	**-59**	**25**	**-103**	**-1,908**

The slight decrease in **service cost** to EUR 75 m (prior year: EUR 77 m) in 2016 was mainly driven by the increase in the discount rate for Germany as at December 31, 2015 to 2.3 % from 2.1 % as at the end of 2014. The reason is as follows: The increase in the discount rate decreases the settlement amount of the defined benefit plans, resulting in lower service cost than in the prior year.

Movements in defined benefit obligation

The opening and closing balances of the present value of the defined benefit obligation 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. 118

					2016					2015
in € millions	Germany	U.S.A.	United Kingdom	Other Countries	Total	Germany	U.S.A.	United Kingdom	Other Countries	Total
Present value of defined benefit obligations as at January 01	**-1,919**	**-223**	**-204**	**-248**	**-2,594**	**-1,972**	**-222**	**-188**	**-286**	**-2,668**
Benefits paid	61	11	10	18	100	63	10	18	16	107
Current service cost	-56	0	0	-18	-74	-56	-2	0	-17	-75
Past service cost	0	0	0	-1	-1	0	0	0	-5	-5
Interest cost	-45	-9	-7	-6	-67	-41	-9	-8	-8	-66
Employee contributions	-8	-1	0	-1	-10	-10	-1	0	-1	-12
Transfers in/out	0	0	0	0	0	28	0	-28	0	0
Settlements paid	0	0	0	0	0	0	9	0	55	64
Gains (+) / losses (-) on settlements	0	0	0	0	0	0	1	0	2	3
Gains (+) / losses (-) – changes in financial assumptions	-235	0	-58	4	-289	72	8	7	5	92
Gains (+) / losses (-) – changes in demographic assumptions	0	4	0	-1	3	0	4	7	0	11
Gains (+) / losses (-) – experience adjustments	12	-1	0	2	13	-1	4	-1	-5	-3
Business combinations/disposals	0	0	0	20	20	0	0	0	0	0
Changes in foreign exchange rates	0	-7	28	-3	18	-2	-25	-11	-4	-42
Present value of defined benefit obligations as at December 31	**-2,190**	**-226**	**-231**	**-234**	**-2,881**	**-1,919**	**-223**	**-204**	**-248**	**-2,594**

The portion of the defined benefit obligation and the plan assets subject to the planned disposal of the fine blanking activities in Switzerland have been classified as held for sale; as a result, the net amount of the defined benefit obligation and the plan assets to be disposed of is shown separately in the statement of financial position. Please refer to Note 4.8 for further detail on the planned disposal.

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. 119

	2016					2015				
in € millions	Germany	U.S.A.	United Kingdom	Other countries	Total	Germany	U.S.A.	United Kingdom	Other countries	Total
Fair value of plan assets as at January 01	**148**	**164**	**229**	**145**	**686**	**179**	**159**	**191**	**191**	**720**
Benefits paid	-3	-10	-10	-9	-32	-4	-10	-18	-10	-42
Interest income on plan assets	3	7	8	4	22	3	7	9	6	25
Employee contributions	9	1	0	1	11	10	1	0	1	12
Employer contributions	12	0	0	12	24	-4	9	0	10	15
Transfers in/out	0	-2	0	0	-2	-45	-1	45	0	-1
Settlements paid	0	0	0	0	0	0	-9	0	-55	-64
Return on plan assets excluding interest income	-1	3	43	5	50	5	-11	-8	1	-13
Business combinations/disposals	0	0	0	-18	-18	0	0	0	0	0
Changes in foreign exchange rates	0	5	-31	5	-21	4	19	10	1	34
Fair value of plan assets as at December 31	**168**	**168**	**239**	**145**	**720**	**148**	**164**	**229**	**145**	**686**

The Schaeffler Group plans to contribute EUR 11 m to plan assets in 2017.

Negative employer contributions in the prior year represent refunds of additional contributions made in the past to cover temporary shortfalls.

Plan assets consisted of the following:

Classes of plan assets No. 120

	12/31/2016					12/31/2015				
in € millions	Germany	U.S.A.	United Kingdom	Other Countries	Total	Germany	U.S.A.	United Kingdom	Other Countries	Total
Equity instruments	84	68	64	17	233	79	66	62	18	225
Debt instruments	28	99	47	112	286	24	97	49	106	276
Real estate	0	0	23	8	31	0	0	26	14	40
Cash	32	1	2	1	36	20	1	2	1	24
(Reimbursement) insurance policies	24	0	0	7	31	25	0	0	6	31
Mixed funds	0	0	103	0	103	0	0	90	0	90
Total	**168**	**168**	**239**	**145**	**720**	**148**	**164**	**229**	**145**	**686**

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. 121

					2016					2015
in € millions	Germany	U.S.A.	United Kingdom	Other countries	Total	Germany	U.S.A.	United Kingdom	Other countries	Total
Current service cost	56	0	0	18	74	56	2	0	17	75
Past service cost	0	0	0	1	1	0	0	0	5	5
• plan amendments	0	0	0	1	1	0	0	0	5	5
Gains (-)/losses (+) on settlements	0	0	0	0	0	0	-1	0	-2	-3
Service cost	**56**	**0**	**0**	**19**	**75**	**56**	**1**	**0**	**20**	**77**
Interest cost	45	9	7	6	67	41	9	8	8	66
Interest income	-3	-7	-8	-4	-22	-3	-7	-9	-6	-25
Net interest on net defined benefit liability/asset	**42**	**2**	**-1**	**2**	**45**	**38**	**2**	**-1**	**2**	**41**
Gains (-)/losses (+) – changes in financial assumptions	235	0	58	-4	289	-72	-8	-7	-5	-92
Gains (-)/losses (+) – changes in demographic assumptions	0	-4	0	1	-3	0	-4	-7	0	-11
Gains (-)/losses (+) – experience adjustments	-12	1	0	-2	-13	1	-4	1	5	3
Return on plan assets excluding interest income	1	-3	-43	-5	-50	-5	11	8	-1	13
Remeasurements of net defined benefit liability/asset	**224**	**-6**	**15**	**-10**	**223**	**-76**	**-5**	**-5**	**-1**	**-87**
Total comprehensive income (loss) on defined benefit obligations	**322**	**-4**	**14**	**11**	**343**	**18**	**-2**	**-6**	**21**	**31**

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. 122

	2016					2015				
in € millions	Germany	U.S.A.	United Kingdom	Other countries	Total	Germany	U.S.A.	United Kingdom	Other countries	Total
Cost of sales	33	0	0	12	45	31	-1	0	16	46
Research and development expenses	11	0	0	1	12	10	0	0	1	11
Selling expenses	4	0	0	3	7	4	0	0	2	6
Administrative expenses	8	0	0	2	10	11	2	0	1	14
Included in EBIT	**56**	**0**	**0**	**18**	**74**	**56**	**1**	**0**	**20**	**77**
Interest expense	45	9	7	6	67	41	9	8	8	66
Interest income on plan assets	-3	-7	-8	-4	-22	-3	-7	-9	-6	-25
Included in financial result	**42**	**2**	**-1**	**2**	**45**	**38**	**2**	**-1**	**2**	**41**
Total	**98**	**2**	**-1**	**20**	**119**	**94**	**3**	**-1**	**22**	**118**

Duration

The weighted average duration of defined benefit obligations is 19.3 years (prior year: 18.1 years) at year-end. In the most significant countries Germany, the U.S., and the United Kingdom, the duration averages 20.3 years (prior year: 18.6 years), 11.9 years (prior year: 12.1 years), and 24.0 years (prior year: 24.9 years), respectively.

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. 123

	2016					2015				
	Germany	U.S.A.	United Kingdom	Other countries	Total	Germany	U.S.A.	United Kingdom	Other countries	Total
Discount rate as at December 31	1.7 %	4.2 %	2.8 %	2.6 %	2.1 %	2.3 %	4.2 %	4.1 %	2.6 %	2.6 %
Future salary increases	3.3 %	n.a. [1]	n.a. [1]	3.2 %	3.3 %	3.3 %	n.a. [1]	n.a. [1]	3.2 %	3.3 %
Future pension increases	1.8 %	2.5 %	3.3 %	0.1 %	1.9 %	1.8 %	2.5 %	3.2 %	0.3 %	1.9 %

[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.

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. 124

						2016					2015
in € millions		Germany	U.S.A.	United Kingdom	Other countries	Total	Germany	U.S.A.	United Kingdom	Other countries	Total
Discount rate	Plus 1.0 %	-382	-25	-46	-25	-478	-296	-25	-42	-29	-392
	Minus 1.0 %	508	30	63	30	631	408	30	58	35	531
Future salary increases	Plus 1.0 %	50	n.a. [1]	n.a. [1]	17	67	41	n.a. [1]	n.a. [1]	19	60
	Minus 1.0 %	-44	n.a. [1]	n.a. [1]	-15	-59	-36	n.a. [1]	n.a. [1]	-17	-53
Future pension increases	Plus 1.0 %	230	0	30	2	262	199	0	25	5	229
	Minus 1.0 %	-190	0	-25	-1	-216	-166	0	-21	-2	-189

[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 106 m (prior year: EUR 90 m) in Germany, EUR 6 m (prior year: EUR 6 m) in the U.S., and EUR 9 m (prior year: EUR 7 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 pension plans

In 2016, Schaeffler incurred EUR 20 m (prior year: EUR 18 m) in expenses related to defined contribution plans. At EUR 13 m (prior year: EUR 12 m), the majority of this amount relates to plans in the U.S.

4.12 Provisions

Provisions No. 125

in € millions	Employee benefits	Restruc-turing	Warranties	Other taxes	Other	Total
Balance as at January 01, 2016	**103**	**42**	**83**	**22**	**363**	**613**
Additions	42	41	53	3	116	255
Utilization	-50	-13	-42	-3	-271	-379
Reversals	-5	-12	-24	0	-5	-46
Interest expense	3	0	0	0	0	3
Foreign currency translation	1	0	0	0	3	4
Balance as at December 31, 2016	**94**	**58**	**70**	**22**	**206**	**450**

Provisions consisted of the following current and non-current portions. Non-current provisions are due in one to five years.

Provisions (non-current/current) No. 126

			12/31/2016			12/31/2015
in € millions	Non-current	Current	Total	Non-current	Current	Total
Employee benefits	39	55	94	43	60	103
Restructuring	14	44	58	28	14	42
Warranties	0	70	70	0	83	83
Other taxes	0	22	22	0	22	22
Other	43	163	206	111	252	363
Total	**96**	**354**	**450**	**182**	**431**	**613**

Provisions for employee benefits consisted primarily of EUR 60 m (prior year: EUR 54 m) in provisions for long-time service awards and partial retirement programs.

Restructuring provisions mainly included provisions of EUR 10 m (prior year: EUR 36 m) related to the realignment of the Industrial division (program “CORE”). An additional restructuring provision of EUR 41 m was recognized for a second wave of measures in the fourth quarter of 2016.

Other provisions include, inter alia, provisions for potential third party claims in connection with antitrust proceedings and other compliance cases of EUR 103 m. EUR 75 m of these provisions were recognized in the fourth quarter of 2016. 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 217 m.

Other non-current provisions declined by EUR 68 m to EUR 43 m (prior year: EUR 111 m). The decline is largely attributable to the reclassification of provisions from non-current to current to reflect their settlement dates.

Other current provisions decreased by EUR 89 m to EUR 163 m (prior year: EUR 252 m). The impact of the reclassifications described above was more than offset by the utilization of the provision for potential third party claims in connection with the EU antitrust proceedings finalized in March 2014 as also described above.

4.13 Other financial liabilities and other liabilities

Other financial liabilities (non-current/current) No. 127

			12/31/2016			12/31/2015
in € millions	Non-current	Current	Total	Non-current	Current	Total
Amounts payable to staff	0	262	262	0	227	227
Derivative financial liabilities	5	70	75	3	46	49
Miscellaneous other financial liabilities	81	364	445	9	239	248
Total	**86**	**696**	**782**	**12**	**512**	**524**

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 reduction in market value.

The increase in **miscellaneous other financial liabilities** mainly reflects the changed presentation of third party claims in connection with the EU antitrust proceedings finalized in March 2014, which were previously included in other provisions. The consideration payable in connection with the acquisition of Compact Dynamics GmbH is also included in miscellaneous other financial liabilities, as are accrued selling costs (customer bonuses, rebates, early-payment discounts) and accrued bond interest.

The Schaeffler Group's exposure to currency and liquidity risk related to other financial liabilities is disclosed in Note 4.14.

Other liabilities (non-current/current) No. 128

			12/31/2016			12/31/2015
in € millions	Non-current	Current	Total	Non-current	Current	Total
Social security contributions payable	2	40	42	2	38	40
Advance payments received	0	25	25	0	29	29
Other tax payables	0	121	121	0	102	102
Miscellaneous other liabilities	4	158	162	4	136	140
Total	**6**	**344**	**350**	**6**	**305**	**311**

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.

Miscellaneous other current liabilities primarily contained accrued vacation and overtime accounts.

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. 129

		12/31/2016		12/31/2015	
in € millions	Category per IFRS 7.8	Carrying amount	Fair value	Carrying amount	Fair value
Financial assets, by class					
Trade receivables	LaR	2,218	2,218	2,023	2,023
Other financial assets					
• Investments in associates [1]	n.a.	3	-	3	-
• Other investments [2]	AfS	14	-	17	-
• Marketable securities	AfS	17	17	14	14
• Derivatives designated as hedging instruments	n.a.	63	63	127	127
• Derivatives not designated as hedging instruments	HfT	141	141	235	235
• Miscellaneous other financial assets	LaR	34	34	1,850	1,856
Cash and cash equivalents	LaR	1,071	1,071	799	799
Financial liabilities, by class					
Financial debt	FLAC	3,707	3,820	5,688	5,793
Trade payables	FLAC	1,625	1,625	1,405	1,405
Other financial liabilities					
• Derivatives designated as hedging instruments	n.a.	40	40	16	16
• Derivatives not designated as hedging instruments	HfT	35	35	33	33
• Miscellaneous other financial liabilities	FLAC	707	707	475	475
Summary by category					
Available-for-sale financial assets (AfS)		31	-	31	-
Financial assets held for trading (HfT)		141	-	235	-
Loans and receivables (LaR)		3,323	-	4,672	-
Financial liabilities at amortized cost (FLAC)		6,039	-	7,568	-
Financial liabilities held for trading (HfT)		35	-	33	-

[1] Equity-accounted investees.
[2] Investments accounted for at cost.

The carrying amounts of trade receivables, miscellaneous other financial assets and 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 2016, 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. 130

in € millions	Level 1	Level 2	Total
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	0	40	40
Derivatives not designated as hedging instruments	0	35	35
Total financial liabilities	**2,813**	**1,082**	**3,895**
December 31, 2015			
Marketable securities	14	-	14
Derivatives designated as hedging instruments	-	127	127
Derivatives not designated as hedging instruments	-	235	235
Other financial assets	-	1,779	1,779
Total financial assets	**14**	**2,141**	**2,155**
Financial debt	5,069	724	5,793
Derivatives designated as hedging instruments	-	16	16
Derivatives not designated as hedging instruments	-	33	33
Total financial liabilities	**5,069**	**773**	**5,842**

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. 131

	Subsequent measurement				Net income (loss)	
in € millions	Interest and dividends	at fair value	Impairment loss	Foreign currency translation	2016	2015
Available-for-sale financial assets	-	0	-	-	0	2
Financial assets and liabilities held for trading	104	-113	-	-	-9	84
Loans and receivables	54	-	3	-13	44	116
Financial liabilities at amortized cost	-289	-	-	-54	-343	-755
Total	**-131**	**-113**	**3**	**-67**	**-308**	**-553**

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 9 m (prior year: net gain of EUR 84 m) relates entirely to derivatives. EUR 4 m (prior year: EUR 168 m) of this net loss is included in financial result. Fair value changes on bifurcated embedded derivatives resulted in losses of EUR 30 m (prior year: EUR 79 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 organization 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 Schaeffler'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 the Schaeffler Group's 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 risk).

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 Schaeffler's reputation.

Liquidity risk is monitored and managed using a rolling liquidity budget with a forecasting period of up to 12 months. Both liquidity status and liquidity forecast are reported regularly to the Chief Financial Officer.

The Schaeffler Group uses equity, cash pooling arrangements, intercompany loans 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 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. 132

in € millions	Carrying amount	Contractual cash flows	Up to 1 year	1-5 years	More than 5 years
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**
December 31, 2015					
Non-derivative financial liabilities	**7,568**	**8,895**	**2,117**	**3,480**	**3,298**
• Financial debt	5,688	7,014	236	3,480	3,298
• Trade payables	1,405	1,405	1,405	0	0
• Other non-derivative financial liabilities	475	476	476	0	0
Derivative financial liabilities	**49**	**49**	**46**	**3**	**0**
Total	**7,617**	**8,944**	**2,163**	**3,483**	**3,298**

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 their payment obligations in full. 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 provisions, 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 OEMs (see Note 5.4). Receivables from ten OEMs make up 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.

Schaeffler's financial debt can be summarized by type of interest as follows:

Variable and fixed interest financial debt No. 133

	Carrying amount	
in € millions	12/31/2016	12/31/2015
Variable interest instruments	**983**	**635**
• Financial debt	983	635
Fixed interest instruments	**2,724**	**5,053**
• Financial debt	2,724	5,053

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, 2016 would affect (increase/decrease) net income and shareholders' equity as follows:

Sensitivity analysis: Shift in yield curve No. 134

	Net income (loss)		Shareholders' equity	
in € millions	Plus 100 Bp	Minus 100 Bp	Plus 100 Bp	Minus 100 Bp
As at December 31, 2016				
Variable interest instruments	-7	0	0	0
Interest rate derivatives designated as hedging instruments	0	0	-2	2
Interest rate derivatives not designated as hedging instruments	-22	6	0	0
Total	**-29**	**6**	**-2**	**2**
As at December 31, 2015				
Variable interest instruments	-3	0	0	0
Interest rate derivatives designated as hedging instruments	0	0	-4	4
Interest rate derivatives not designated as hedging instruments	-10	51	0	0
Total	**-13**	**51**	**-4**	**4**

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, 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. 135

in € millions	USD	CNY	RON	PLN
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**
December 31, 2015				
Estimated currency risk from operations	740	491	-211	150
Forward exchange contracts	-622	-336	156	-95
Remaining currency risk from operations	**118**	**155**	**-55**	**55**

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 organization. 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 organization. The most significant currency risk exposure in these countries arises on the U.S. Dollar and amounts to an estimated EUR 76 m (prior year: EUR 36 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, 2016, 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. 136

	12/31/2016		12/31/2015	
in € millions	Net income (loss)	Share-holders' equity	Net income (loss)	Share-holders' equity
USD	15	-67	16	-67
CNY	19	-39	14	-25
HUF	6	10	1	9
PLN	0	-12	-1	9

Conversely, a 10 % rise in the Euro against the significant foreign currencies as at December 31, 2016 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 800 m (prior year: USD 1,800 m). Changes in the fair value of those cross-currency swaps not subject to hedge accounting (notional amount of USD 400 m; prior year: USD 800 m) were recognized directly in profit or loss in 2016.

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, 2016. 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. 137

	12/31/2016		12/31/2015	
in € millions	Net income (loss)	Share-holders' equity	Net income (loss)	Share-holders' equity
Foreign exchange gains and losses on financial debt	-76	-47	-165	-72
Foreign exchange gains and losses on derivatives	80	7	170	16
Total	**4**	**-40**	**5**	**-56**

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 risk

Other price risk 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. 138

	12/31/2016		12/31/2015	
in € millions	Nominal value	Fair value	Nominal value	Fair value
Financial assets				
Currency hedging				
Forward exchange contracts	1,458	32	2,050	53
• thereof: hedge accounting	439	6	599	18
Cross-currency swaps	759	108	1,653	214
• thereof: hedge accounting	380	57	919	108
Financial liabilities				
Currency hedging				
Forward exchange contracts	2,106	75	2,187	49
• thereof: hedge accounting	1,166	40	797	16
Cross-currency swaps	57	0	0	0
• thereof: hedge accounting	57	0	0	0

Cash flow hedges

A portion of Schaeffler'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. 139

in € millions	2016	2015
Balance as at January 01	**3**	**-45**
Additions	-34	3
Reclassified to income statement		
• to other income	-3	0
• to other expense	0	45
Balance as at December 31	**-34**	**3**

The Schaeffler Group also applies cash flow hedge accounting to the foreign currency hedge of its bonds issued in U.S. Dollar using cross-currency swaps with a nominal value of USD 400 m (prior year: USD 1,000 m). As a result, accumulated gains of EUR 27 m (prior year: gains of EUR 14 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, 2016. There was no ineffectiveness. The foreign exchange effects hedged will be recognized in profit or loss in the years 2017 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. 140

in € millions	2016	2015
Balance as at January 01	**-42**	**-56**
Additions	-51	75
Reclassified to income statement		
• to financial income	0	-61
• to financial expense	78	0
Balance as at December 31	**-15**	**-42**

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 (principal of USD 500 m; prior year: USD 790 m) under a net investment hedge. This mitigates the group's translation risk on the U.S. subsidiaries. As a result, foreign exchange losses of EUR 10 m (prior year: losses of EUR 95 m) on designated financial debt were recognized in other comprehensive income and reported in accumulated other comprehensive income (translation reserve) as at December 31, 2016. 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 Associations (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 are as follows:

Offsetting financial assets and financial liabilities No. 141

in € millions	12/31/2016	12/31/2015
Financial assets		
Gross amount of financial assets	204	362
Amounts offset in accordance with IAS 32.42	0	0
Net amount of financial assets	204	362
Amounts subject to master netting arrangements		
• Derivatives	-62	-47
Net amount of financial assets	142	315
Financial liabilities		
Gross amount of financial liabilities	75	49
Amounts offset in accordance with IAS 32.42	0	0
Net amount of financial liabilities	75	49
Amounts subject to master netting arrangements		
• Derivatives	-62	-47
Net amount of financial liabilities	13	2

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.

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 vesting, 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 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, 2016 amounted to EUR 3.5 m (prior year: EUR 0.7 m) and were included in non-current provisions. Net expenses arising from the PSUP for 2016 totaled EUR 2.8 m (prior year: EUR 0.7 m). There were 1,310,594 PSUs (prior year: 474,016 PSUs) in total as at December 31, 2016. All PSUs granted in 2016 were still outstanding as at December 31, 2016.

The average fair value of a PSU granted was EUR 11.31 as at December 31, 2016 (prior year: EUR 13.18). 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. 142

	12/31/2016	12/31/2015
Average risk-free interest rate for the remaining performance period	-0.35 %	0.11 %
Expected dividend yield of Schaeffler AG common non-voting shares	2.49 %	2.15 %
Expected volatility of Schaeffler AG common non-voting shares	34.27 %	33.02 %
Expected volatility of the benchmark index	18.75 %	19.53 %
Expected correlation between the benchmark index and Schaeffler AG common non-voting shares	0.61	0.43

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 long-term strategy of pursuing profitable 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 debt to equity (gearing ratio). 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 is in 2020.

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 2016, the Schaeffler Group obtained ratings from rating agencies Standard & Poor's and Moody's. As a basis for executing its growth strategies, 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 certain financial covenants (see Note 4.10). Compliance with these financial covenants is continually monitored at group level. The inputs to the calculation of the financial covenants are defined in detail in the debt agreements and cannot be derived directly from amounts in the consolidated financial statements.

As in the prior year, the company has complied with the financial covenants in 2016 as stipulated in the debt agreements. Based on its forecast, the Schaeffler Group also expects to comply with these covenants in subsequent years.

In addition to the financial covenants contained in the debt agreements, the Schaeffler Group regularly calculates further financial indicators. One such further indicator is the ratio of net debt to EBITDA (earnings before financial result, income taxes, depreciation, amortization, and impairment losses), which is determined as follows:

Net financial debt to EBITDA ratio No. 143

in € millions	12/31/2016	12/31/2015
Current financial debt	3	3
Non-current financial debt	3,704	5,685
Total financial debt	**3,707**	**5,688**
Cash and cash equivalents	1,071	799
Total net financial debt	**2,636**	**4,889**
Earnings before financial result, income taxes, depreciation and amortization and impairment losses (EBITDA) [1]	**2,293**	**2,096**
Net financial debt to EBITDA ratio [2]	**1.1**	**2.3**

[1] EBITDA incl. EUR 144 m (prior year: EUR 274 m) in special items.
[2] Debt to EBITDA ratio incl. special items (footnote 1).

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

5. Other disclosures

5.1 Leases

Future minimum lease payments under non-cancellable operating rental and lease agreements are due as follows:

Leases No. 144

in € millions	12/31/2016	12/31/2015
Less than one year	58	56
Between one and five years	60	64
More than five years	5	6
Total	**123**	**126**

The obligations consisted primarily of rental agreements for real estate and lease agreements relating to company vehicles and IT and logistics.

In 2016, the Schaeffler Group recognized EUR 85 m in expenses related to operating rental and lease agreements in profit or loss (prior year: EUR 84 m).

5.2 Contingent liabilities

At December 31, 2016, the Schaeffler Group had contingent liabilities of EUR 46 m (prior year: EUR 23 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.

5.3 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 its institutional loan tranches, Schaeffler AG also terminated a portion of the cross-currency swaps designed to hedge the USD tranche against currency fluctuations before maturity. Termination involved an exchange of principal and resulted in cash inflows of EUR 96 m due to exchange rate changes. These cash inflows from the hedging instrument as well as the cash inflows from the hedged item are presented under repayments of loans.

The disposal of Schaeffler Motorenelemente AG & Co. KG and the planned sale of the fine blanking activities of Schaeffler Schweiz GmbH have not affected the statement of cash flows as no payments were made for these transactions in 2016. The purchase price for the acquisition of Compact Dynamics GmbH has also not been paid yet. The inflow of the EUR 2 m in cash held by Compact Dynamics GmbH is reflected in other investing activities.

Other financing activities include EUR 1,773 m in cash provided by the prepayment in full of a loan that was receivable by Schaeffler AG from IHO Verwaltungs GmbH.

5.4 Segment reporting

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 impairments are reported based on the current allocation of customers to divisions. The allocation of customers to divisions is reviewed at least once every year and adjusted where necessary. To ensure that segment information is comparable, prior year information is also presented using the current year's customer structure. Revenue related to transactions between operating segments is not included.

Since January 01, 2016, the Industrial division segment is primarily managed based on regions due to its broad customer and business structure. 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. Within the regions, the Industrial business is grouped into eight sectors: wind, raw materials, aerospace, rail, offroad, two wheelers, power transmission, and industrial automation.

Sales to distributors (Industrial Distribution) round out the Industrial division's regional business.

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). Products range from wheel bearings as well as chassis and steering components through transmission systems and developments to engine components and valve control systems.

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. This segment's key products are rolling and plain bearings, linear guidance systems, and direct drives.

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. 145

in € millions	2016	2015
EBIT Automotive [1]	1,383	1,135
EBIT Industrial [1]	173	267
EBIT	**1,556**	**1,402**
Financial result	-341	-547
Earnings before income taxes	**1,215**	**855**

[1] Prior year information presented based on 2016 segment structure.

In 2016, the Schaeffler Group generated revenue of EUR 1,462 m (prior year: EUR 1,528 m) from one key customer, representing approximately 11.0 % (prior year: 11.6 %) of total group revenue and approximately 14.1 % (prior year: 15.3 %) of Automotive segment revenue.

In addition to the divisions and functions, the Schaeffler Group's multi-dimensional 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 2016:

Information about geographical areas No. 146

	Revenue [1]		Non-current assets [2]	
in € millions	2016	2015	12/31/2016	12/31/2015
Europe	7,077	7,027	3,039	2,843
Americas	2,800	2,901	818	706
Greater China	2,053	1,898	932	879
Asia/Pacific	1,408	1,353	350	341
Total	**13,338**	**13,179**	**5,139**	**4,769**

[1] Revenue by market (customer locations); Prior year information presented based on 2016 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 2,790 m (prior year: EUR 2,928 m), EUR 1,986 m (prior year: EUR 1,806 m), and EUR 1,827 m (prior year: EUR 1,870 m) as well as non-current assets of EUR 1,757 m (prior year: EUR 1,634 m), EUR 931 m (prior year: EUR 878 m), and EUR 476 m (prior year: EUR 399 m), respectively.

5.5 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 according to IAS24 for 2016 totaled EUR 19 m (prior year: EUR 21 m), including EUR 12 m (prior year: EUR 16 m) in short-term benefits. Expenses of EUR 3 m (prior year: EUR 3 m) were recognized for post-employment benefits. Termination benefits amounted to EUR 0 m (prior year: EUR 0.3 m), and share-based payments totaled EUR 2.6 m (prior year: EUR 0.7 m).

Total remuneration of the Board of Managing Directors in accordance with section 314 (1) (6a) (1 - 3) HGB amounted to EUR 19 m (prior year: EUR 21 m) in 2016.

The following share-based remuneration was granted to members of the Board of Managing Directors in 2016 under the Performance Share Unit Plan (PSUP) implemented in 2015: 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).

The following share-based remuneration was granted to members of the Board of Managing Directors in the prior year: 237,004 Performance Share Units (PSU) subject to a service condition (fair value per PSU at grant date of EUR 11.58), 118,506 PSUs subject to an FCF-based performance target (fair value per PSU at grant date of EUR 11.58) and 118,506 PSUs with a TSR-based performance target (fair value per PSU at grant date of EUR 6.96). Please refer to the remuneration report for a detailed discussion of the PSUP.

Certain members of the Board of Managing Directors have received advances on their variable short-term remuneration in connection with the change in the remuneration system and adjustment of their fixed remuneration. Advances paid in 2015 amounted to EUR 525 thousand and were repaid in 2016.

Short-term benefits paid to members of Schaeffler AG's Supervisory Board, which became operational in early December 2014, amounted to EUR 1.8 m (prior year: EUR 1.9 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 2.9 m in 2016 (prior year: EUR 0.3 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 11 m at December 31, 2016 (prior year: EUR 8 m).

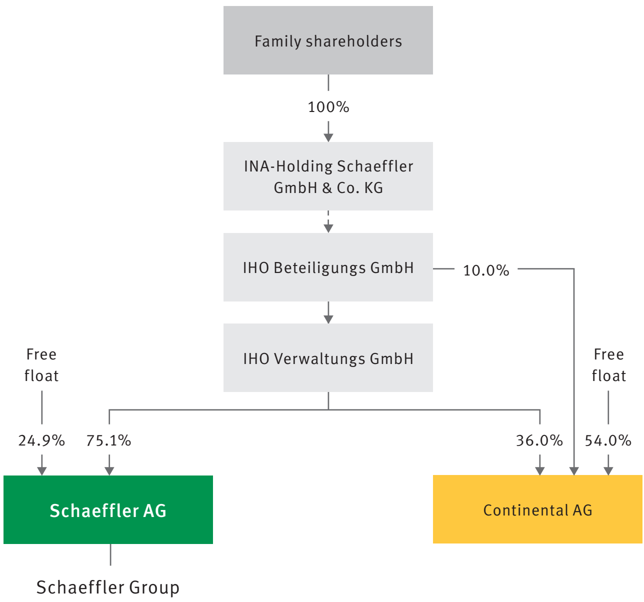
In the prior year, members of the Board of Managing Directors and the Supervisory Board of Schaeffler AG as well as close members of their family acquired bonds issued by Schaeffler Finance B.V. totaling EUR 1 m. Additionally, bonds issued in prior years with a value of EUR 3 m (prior year: EUR 1 m) held by key management personnel and close members of their family were redeemed. At December 31, 2016, 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 0.8 m (prior year: EUR 6 m). Key management personnel and close members of their family received interest of EUR 0.1 m (prior year: EUR 0.2 m) on these bonds.

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 GmbH & Co. KG has significant influence.

Simplified ownership structure No. 147

as at December 31, 2016



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 2016.

In 2016 and 2015, Schaeffler Group companies had various business relationships with the group's related entities.

On April 22, 2016, the Schaeffler AG annual general meeting declared a total dividend of EUR 328 m in respect of 2015, including EUR 245 m on the common shares held by IHO Verwaltungs GmbH.

The EUR 1,773 m loan receivable from IHO Verwaltungs GmbH as at December 31, 2015 was fully repaid in two partial payments made in May and September of 2016. Interest income earned on this loan in 2016 amounted to EUR 49 m (prior year: EUR 72 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 Continental 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. 148

	Receivables		Payables	
in € millions	12/31/2016	12/31/2015	12/31/2016	12/31/2015
Related entities	22	1,787	12	8

Expenses and income from transactions with related entities No. 149

	Expenses		Income	
in € millions	2016	2015	2016	2015
Related entities	84	78	168	176

Receivables from transactions with related entities include EUR 22 m (prior year: EUR 14 m) in trade receivables.

5.6 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. 150

	KPMG		thereof KPMG AG	
in € millions	**2016**	**2015**	**2016**	**2015**
Financial statement audit services	6.4	6.5	3.7	3.6
Other attestation services	0.1	0.3	0.1	0.3
Tax advisory services	1.3	1.0	1.0	0.8
Other services	0.5	1.4	0.4	1.3
Total	**8.3**	**9.2**	**5.2**	**6.0**

The amounts required to be disclosed under section 314 (1)(9) HGB were determined in accordance with the revised version of IDW RS HFA 36 dated September 08, 2016. Prior year information was adjusted accordingly. Global fees were determined in line with these requirements.

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.

5.7 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 required by section 161 AktG in December 2016 and have made it publicly available on the Schaeffler Group's website (www.schaeffler.com/ir).

5.8 Events after the reporting period

No material events expected to have a significant impact on the results of operations, financial position, or net assets of the Schaeffler Group occurred after December 31, 2016.

5.9 List of shareholdings required by section 313 (2) HGB

The parent company is Schaeffler AG, which is based in Herzogenaurach.

List of shareholdings No. 151

Entity	Location	Country code	Group ownership interest in %
A. Entities fully consolidated **I. Germany (51)**			
AS Auslandsholding GmbH [2]	Buehl	DE	100.00
CBF Europe GmbH	Wuppertal	DE	100.00
Compact Dynamics GmbH [3]	Starnberg	DE	51.00
CVT Beteiligungsverwaltungs GmbH	Buehl	DE	100.00
CVT Verwaltungs GmbH & Co. Patentverwertungs KG [1] [5]	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] [5]	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] [5]	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 ASG GmbH	Buehl	DE	100.00
LuK Auslandsholding GmbH [2]	Buehl	DE	100.00
LuK Beteiligungsgesellschaft mbH [2]	Buehl	DE	100.00
LuK GmbH & Co. KG [1] [5]	Buehl	DE	100.00
LuK Management GmbH	Buehl	DE	100.00
LuK Truckparts GmbH & Co. KG [1] [5]	Kaltennordheim	DE	100.00
LuK Unna GmbH & Co. KG [1] [5]	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] [5]	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] [5]	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] [5]	Herzogenaurach	DE	100.00
Schaeffler Technologies AG & Co. KG [1] [5]	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] [5]	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 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
INA Lanskroun, s.r.o.	Lanskroun	CZ	100.00
Schaeffler CZ s.r.o.	Prague	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
Schaeffler Trading (UK) Limited	Sutton Coldfield	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.	Halandri	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
FAG Bearings India Ltd.	Mumbai	IN	51.33
INA Bearings India Private Limited	Pune	IN	100.00
LuK India Private Limited	Hosur	IN	100.00
FAG Railway Products G.e.i.e.	Mailand	IT	75.00
INA Invest S.r.l.	Momo	IT	100.00
Schaeffler 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
NACO Technologies SIA (since January 01, 2017: 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. [6]	Bangkok	TH	49.00
Schaeffler Holding (Thailand) Co., Ltd. [6]	Bangkok	TH	49.00
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
Roland Corporate Housing LLC	Cheraw	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 [5]	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			
Foreign (1)			
Schaeffler (Xiangtan) Co., Ltd. [4]	Xiangtan	CN	100.00

[1] Exemption under section 264b HGB.
[2] Exemption under section 264 (3) HGB.
[3] The company is consolidated as if it were wholly owned, since the parties hold matching call and put options on the remaining shares.
[4] The company is insignificant to the results of operations, financial position, and net assets of Schaeffler AG as at the reporting date.
[5] Schaeffler AG or another consolidated entity is the general partner.
[6] The company is consolidated based on a majority of the voting rights.

5.10 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, Norbert Lenhard*,
Dr. Siegfried Luther, Dr. Reinold Mittag*, Yvonne Münch*,
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

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 Chief Executive Officer and Chief Technology Officer),
Dr. Ulrich Hauck (Chief Financial Officer),
Oliver Jung (Chief Operating Officer),
Prof. Dr. Peter Pleus (CEO Automotive),
Corinna Schittenhelm (Chief Human Resources Officer),
Dr. Stefan Spindler (CEO Industrial),
Matthias Zink (CEO Automotive; since January 01, 2017)

The following member left the Board of Managing Directors in 2016

Norbert Indlekofer (CEO Automotive; until December 31, 2016)

* Employee representative.

5.11 Preparation of consolidated financial statements

The Board of Managing Directors of Schaeffler AG prepared the consolidated financial statements on February 20, 2017 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 20, 2017

Schaeffler Aktiengesellschaft
The Board of Managing Directors

Klaus Rosenfeld
Chief Executive Officer

Prof. Dr.-Ing. Peter Gutzmer

Dr. Ulrich Hauck

Oliver Jung

Prof. Dr. Peter Pleus

Corinna Schittenhelm

Dr. Stefan Spindler

Matthias Zink

Independent auditors' report

This auditors' report, prepared in accordance with § 322 HGB [Handelsgesetzbuch: „German Commercial Code"], refers to the complete consolidated financial statements, comprising the consolidated income statement, the consolidated statement of comprehensive income, the consolidated statement of financial position, the consolidated statement of cash flows, the consolidated statement of changes in shareholders' equity and the notes to the consolidated financial statements, together with its report of the position of the company and the group for the business year from January 1, 2016 to December 31, 2016. The above-mentioned auditors' report and consolidated financial statements are both translations of the respective German-language documents.

We have audited the consolidated financial statements prepared by the Schaeffler AG, Herzogenaurach, comprising the consolidated income statement, the consolidated statement of comprehensive income, the consolidated statement of financial position, the consolidated statement of cash flows, the consolidated statement of changes in shareholders' equity and the notes to the consolidated financial statements, together with its report of the position of the company and the group for the business year from January 1, 2016 to December 31, 2016. The preparation of the consolidated financial statements and the report of the position of the company and the group in accordance with IFRSs, as adopted by the EU, and the additional requirements of German commercial law pursuant to § 315a Abs. 1 HGB [Handelsgesetzbuch: „German Commercial Code"] are the responsibility of the parent company's management. Our responsibility is to express an opinion on the consolidated financial statements and on the report on the position of the company and the group report based on our audit.

We conducted our audit of the consolidated financial statements in accordance with § 317 HGB [Handelsgesetzbuch: „German Commercial Code"] and German generally accepted standards for the audit of financial statements promulgated by the Institut der Wirtschaftsprüfer [Institute of Public Auditors in Germany] (IDW). Those standards require that we plan and perform the audit such that misstatements materially affecting the presentation of the net assets, financial position and results of operations in the consolidated financial statements in accordance with the applicable financial reporting framework and its report of the position of the company and the group are detected with reasonable assurance. Knowledge of the business activities and the economic and legal environment of the Group and expectations as to possible misstatements are taken into account in the determination of audit procedures. The effectiveness of the accounting-related internal control system and the evidence supporting the disclosures in the consolidated financial statements and the report of the position of the company and the group are examined primarily on a test basis within the framework of the audit. The audit includes assessing the annual financial statements of those entities included in consolidation, the determination of entities to be included in consolidation, the accounting and consolidation principles used and significant estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements and its report of the position of the company and the group. We believe that our audit provides a reasonable basis for our opinion.

Our audit has not led to any reservations.

In our opinion, based on the findings of our audit, the consolidated financial statements comply with IFRSs, as adopted by the EU, the additional requirements of German commercial law pursuant to § 315a Abs. 1 HGB and give a true and fair view of the net assets, financial position and results of operations of the Group in accordance with these requirements. The report on the position of the company and the group is consistent with the consolidated financial statements, complies with the German statutory requirements, and as a whole provides a suitable view of the Group's position and suitably presents the opportunities and risks of future development.

Munich, February 21, 2017

KPMG AG
Wirtschaftsprüfungsgesellschaft

Alt-Scherer Wirtschaftsprüferin	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 20, 2017

Schaeffler Aktiengesellschaft
The Board of Managing Directors

Klaus Rosenfeld
Chief Executive Officer

Prof. Dr.-Ing. Peter Gutzmer

Dr. Ulrich Hauck

Oliver Jung

Prof. Dr. Peter Pleus

Corinna Schittenhelm

Dr. Stefan Spindler

Matthias Zink

Additional information

Glossary

A

Active roll control: Newly developed mechatronic component used in passenger cars to minimize or completely eliminate the vehicle's rolling motion when taking corners and on poor roads. This significantly improves safety and comfort while also increasing the vehicle's agility.

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. 16 Strategic Initiatives that have significance worldwide and have been selected from a variety of initiatives are in turn assigned to these categories.

Automotive: As a reliable partner to nearly all automobile manufacturers and major suppliers, the Schaeffler Group's Automotive division offers expertise for the entire drive train: For engines, transmissions, chassis, and accessory units in passenger cars and commercial vehicles. The Automotive Aftermarket sector is represented worldwide in the spare parts business.

B

Bearing & Components Technologies (BCT): Functionally coordinated department of the Schaeffler Group that acts as an integrated internal supplier.

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. Used to assess an entity's financial strength.

CEEMEA: Central and Eastern Europe & Middle East and Africa.

CE officer: Person responsible for the conformity assessment of the Schaeffler Group's products required for access to the European market.

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.

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 as part of the One Schaeffler portfolio.

Content per Car: Proportion of product per vehicle.

CORE: 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.

Corruption Perception Index: Describes the degree of perceived corruption in a country's public sector.

COSO model: Internal control model to help document, evaluate and design internal control systems.

Cost of capital: The cost of capital is derived from the return investors require for providing capital to the entity.

Covenants: Also called "financial covenants" or "financial ratios"; used to monitor compliance with loan agreements. If the agreed upon financial ratios are not met, creditors can call the corresponding loans.

D

DAX: Abbreviation of "Deutscher Aktien Index" ("German Share Index"): Leading share index of Deutsche Börse.

Debt to EBITDA ratio: Ratio of net financial debt to EBITDA.

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 is complying with the German Corporate Governance Code and which recommendations were 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 (e.g. index, share or bond).

Digital Agenda: Initiative under the "Agenda 4 plus One" excellence program 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 the Schaeffler Board of Managing Directors or Supervisory Board or persons related to them.

Diversity: Diversity with respect to aspects including gender, ethnic origin, age, disability sexual orientation, religion, life style.

Dual-mass flywheel: Component of the drive train of modern vehicles (passenger cars, buses, commercial vehicles) that helps reduce torsional vibration.

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.

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.

EMAS: EU environmental audit regulation under which Schaeffler Group locations have been validated.

EnEHS: Energy, environment, health and safety.

Equity ratio: Shareholders' equity as a percentage of total capital.

Euribor: Abbreviation of "Euro Interbank Offered Rate": Interest rate that European banks charge each other on unsecured loans denominated in Euro.

EURO MTF (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.

E-Wheel Drive: Electric wheel hub drive developed by the Schaeffler Group in which all components required for drive, deceleration, and driving safety – such as the electric motor, power electronics, controller, brake, and cooling system – are contained within the wheel rim.

F

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 covenants: Agreements 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.

G

Gearing ratio: Ratio of net financial debt to shareholders' equity.

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.

Gross margin: Gross profit as a percentage of revenue.

Group Compliance and Risk Committee: 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".

House of Governance: Model summarizing the key elements of corporate governance (compliance management, risk management, internal control system and internal audit).

I

IAS: Abbreviation of "International Accounting Standards".

IASB: Abbreviation of "International Accounting Standards Board".

IATF 16949: International standard for quality management systems of companies in the automotive sector.

IFRIC: Abbreviation of "International Financial Reporting Standards Interpretation".

IFRS: Abbreviation of “International Financial Reporting Standards”.

IHO Holding: A group of holding companies held indirectly by the Schaeffler family.

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.

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.

ISO TS 16949:2009: Replaced by IATF 16949 on October 01, 2016.

ISO 9001:2015: International standard for quality management systems.

ISO 14001: Established international standard for environmental management systems.

ISO 50001: International standard for energy management systems.

iTraxx: Indicator of credit risk and the cost of credit in the European high yield market.

L

LaR: Abbreviation of “Loans and receivables”.

M

M&A: Abbreviation of Mergers & Acquisitions = mergers of companies and acquisition 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.

MEA: Middle East and Africa.

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 16 Strategic Initiatives, and the Schaeffler Group’s Financial Ambitions 2020.

MOVE: Internal program used by Schaeffler to review processes and activities regarding their contribution to value added.

N

Net financial debt: Total of current and non-current financial debt net of cash and cash equivalents.

Net Promoter Score: Ratio measuring customer satisfaction.

NGO: Abbreviation of non-governmental organization.

Non-controlling interest: Interest in the company’s shareholders’ equity held by third parties that does not give the holder control.

O

OEM: Original equipment manufacturer = manufacturer of a branded product.

OES: Original equipment supplier = supplier manufacturing spare parts for distribution by the OEM under its own brand.

OHSAS 18001: OHSAS is the abbreviation of “Occupational Health and Safety Assessment Series”. OHSAS 18001 is a standard for occupational safety management systems.

One Schaeffler: Transformation program consisting of 21 initiatives aimed at improving the company’s structures and processes, drive forward higher-level business issues, and strengthen inter-departmental cooperation within the Schaeffler Group. The program was completed successfully on December 31, 2015.

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

Payout ratio: Percentage of the Schaeffler Group's net income before special items that is paid out to shareholders in dividends.

Pick-up sheet method: Method commonly used in the industry to coordinate the flow of goods.

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.

Power steering pump: The power steering pump supplies hydraulic oil to the steering gear.

Predictive Maintenance 4.0: Technology that expands conventional maintenance systems and provides the customer with new options for increasing efficiency and reducing the total cost of ownership.

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 expenditures as a percentage of revenue.

Rating: Assessment of a company's creditworthiness by rating agencies.

RCOI: Abbreviation of "Reasonable Country of Origin Inquiries" = inquiries into the country of origin of raw materials or minerals to ensure that mining of these raw materials does not contribute to financing wars.

Revolving credit facility: Contractually agreed credit facility that can be utilized repeatedly.

Roadmap 2020: Strategic Initiative for operationalizing the strategic concept "Mobility for tomorrow".

ROCE (return on capital employed): Ratio of EBIT to average capital employed. Average capital employed is 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.

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.

Schaeffler Cloud: Digital platform used to operate all data-based services of the Schaeffler Group.

Schaeffler System 48 V: Concept car developed by Schaeffler based on an Audi TT with a 48 V electric motor mounted on the rear axle as an "electric axle", complementing the front-wheel drive internal combustion engine.

Schaeffler Value Added: Key performance indicator used in value-based management; compares earnings before interest and taxes to the cost of capital.

Scope of consolidation: Total of all companies included in the consolidated financial statements.

Sensotect: Thin-layer technology developed by the Schaeffler Group; can be used to produce multi-functional surfaces that can directly record forces or torques inside components.

SHARE: 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.

SIC: Abbreviation of the former "Standing Interpretations Committee".

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.

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. This innovative module is key to reducing fuel consumption and CO_2 emissions by up to 4 %.

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.

Torque vectoring: Torque vectoring offers an additional possibility for steering the wheels of an automobile by selectively distributing the drive forces to specific wheels.

Transparency International: Politically independent organization dealing with the worldwide problem of corruption.

Tribology: The science and technology of interacting surfaces in relative motion.

W

Working capital: Inventories plus trade receivables less trade payables (excluding accrued payables).

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Contact details/imprint

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'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 does not intend or assume any obligation to update any forward-looking statements to reflect events or circumstances after the date of this report.

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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.

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.

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Summary – 1st quarter 2015 to 4th quarter 2016

	2015				2016			
Income statement (in € millions)	1st quarter	2nd quarter	3rd quarter	4th quarter	1st quarter	2nd quarter	3rd quarter	4th quarter
Revenue	3,339	3,382	3,237	3,221	3,343	3,369	3,265	3,361
EBIT	434	384	433	151	421	438	417	280
• in % of revenue	13.0	11.4	13.4	4.7	12.6	13.0	12.8	8.3
EBIT before special items [1]	441	384	433	418	421	438	417	424
• in % of revenue	13.2	11.4	13.4	13.0	12.6	13.0	12.8	12.6
Net income [2]	167	142	212	70	253	241	178	187
Earnings per common non-voting share (basic/diluted, in €) [3]	0.42	0.36	0.53	0.11	0.38	0.37	0.27	0.28
Statement of financial position (in € millions)								
Total assets	12,844	12,221	12,450	12,480	12,607	12,554	12,862	11,564
Shareholders' equity [4]	418	532	631	1,568	1,609	1,425	1,554	1,997
• in % of total assets	3.3	4.4	5.1	12.6	12.8	11.4	12.1	17.3
Net financial debt	6,190	6,245	5,950	4,889	4,909	4,874	2,876	2,636
• Net financial debt to EBITDA ratio before special items [1] [5]	2.7	2.7	2.6	2.1	2.1	2.0	1.2	1.1
• Gearing ratio (Net financial debt to shareholders' equity, in %)	1,480.9	1,173.9	942.9	311.8	305.1	342.0	185.1	132.0
Statement of cash flows (in € millions)								
EBITDA	604	557	604	331	598	619	600	476
• in % of revenue	18.1	16.5	18.7	10.3	17.9	18.4	18.4	14.2
EBITDA before special items [1]	611	557	604	598	598	619	600	620
• in % of revenue	18.3	16.5	18.7	18.6	17.9	18.4	18.4	18.4
Cash flows from operating activities	184	238	490	460	206	571	528	571
Capital expenditures (capex) [6]	244	257	242	282	318	243	268	317
• in % of revenue (capex ratio)	7.3	7.6	7.5	8.8	9.5	7.2	8.2	9.4
Free cash flow	-60	-12	264	178	-112	328	263	256
Value added								
ROCE before special items (in %) [1] [5]	22.8	22.2	21.9	22.5	22.1	22.5	21.9	21.7
Schaeffler Value Added before special items (in € millions) [1] [5]	896	878	870	931	906	951	920	915
Employees								
Headcount (at end of reporting period)	83,331	83,774	84,414	84,198	85,016	85,225	86,029	86,662

[1] EBIT before special items, please refer to page 48.
[2] Attributable to shareholders of the parent company.
[3] Earnings per share were calculated in accordance with IAS 33.
[4] Including non-controlling interests.
[5] EBIT/EBITDA based on the last twelve months.
[6] Capital expenditures on intangible assets and property, plant and equipment.

	2015				2016			
Automotive (in € millions)								
Revenue	2,515	2,554	2,442	2,466	2,576	2,603	2,524	2,630
EBIT	343	308	356	128	372	367	364	280
• in % of revenue	13.6	12.1	14.6	5.2	14.4	14.1	14.4	10.6
EBIT before special items [1]	350	308	356	359	372	367	364	388
• in % of revenue	13.9	12.1	14.6	14.6	14.4	14.1	14.4	14.8
Industrial (in € millions)								
Revenue	824	828	795	755	767	766	741	731
EBIT	91	76	77	23	49	71	53	0
• in % of revenue	11.0	9.2	9.7	3.0	6.4	9.3	7.2	0.0
EBIT before special items [1]	91	76	77	59	49	71	53	36
• in % of revenue	11.0	9.2	9.7	7.8	6.4	9.3	7.2	4.9

Prior year information presented based on 2016 segment structure.
[1] EBIT before special items, please refer to page 48.

Multi-year comparison

	2012	2013	2014	2015	2016
Income statement (in € millions)					
Revenue	11,125	11,205	12,124	13,179	13,338
EBIT	1,469	1,008	1,523	1,402	1,556
• in % of revenue	13.2	9.0	12.6	10.6	11.7
EBIT before special items [1]	-	1,436	1,561	1,676	1,700
• in % of revenue	-	12.8	12.9	12.7	12.7
Net income [2]	380	127	654	591	859
Earnings per common non-voting share (basic/ diluted, in €) [3]	-	-	1.29	1.28	1.30
Statement of financial position (in € millions)					
Total assets	8,463	8,387	11,617	12,480	11,564
Shareholders' equity [4]	-2,598	-1,966	258	1,568	1,997
• in % of total assets	-30.7	-23.4	2.2	12.6	17.3
Net financial debt	6,541	5,447	5,778	4,889	2,636
• Net financial debt to EBITDA ratio before special items [1]	3.1	2.6	2.6	2.1	1.1
• Gearing ratio (Net financial debt to shareholders' equity, in %)	-	-	2,239.5	311.8	132.0
Statement of cash flows (in € millions)					
EBITDA	2,087	1,660	2,172	2,096	2,293
• in % of revenue	18.8	14.8	17.9	15.9	17.2
EBITDA before special items [1]	-	2,088	2,210	2,370	2,437
• in % of revenue	-	18.6	18.2	18.0	18.3
Cash flows from operating activities [5]	1,133	1,027	900	1,372	1,876
Capital expenditures (capex) [6]	860	572	857	1,025	1,146
• in % of revenue (capex ratio)	7.7	5.1	7.1	7.8	8.6
Free cash flow [5]	301	473	48	370	735
Value added					
ROCE before special items (in %) [1]	-	22.1	23.1	22.5	21.7
Schaeffler Value Added before special items (in € millions) [1]	-	787	885	931	915
Employees					
Headcount (at end of reporting period)	75,810	78,258	82,294	84,198	86,662

1) EBIT before special items, please refer to page 48.
2) Attributable to shareholders of the parent company.
3) Earnings per share were calculated in accordance with IAS 33.
4) Including non-controlling interests.
5) Including an outflow of EUR 371 m for the EU antitrust penalty in 2014.
6) Capital expenditures on intangible assets and property, plant and equipment.

Financial calendar 2017

March 08, 2017

Publication of annual results 2016

April 26, 2017

Annual general meeting 2017

May 11, 2017

Publication of results for the first three months 2017

August 08, 2017

Publication of results for the first six months 2017

November 08, 2017

Publication of results for the first nine months 2017

All information is subject to correction and
may be changed at short notice.

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PDF version for download:
www.schaeffler.com/ir

Online version of the annual report:
www.schaeffler-annual-report.com

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A glossary is available on pages 165 to 170.

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