KENDRION

WE MAGNETISE THE WORLD

INTEGRATED ANNUAL REPORT 2017

CONTENTS

PHOTOGRAPHY AND IMAGES
Kendrion N.V.
Shutterstock
Artphotographs Dieter Marx e.K.
SSI Schäfer

A digital version of this Report is available on the websites www.kendrion.com and annualreport.kendrion.com along with other publications such as press releases.

Better climate solutions
Electromagnetic control valves help to reduce emissions and improve energy consumption.

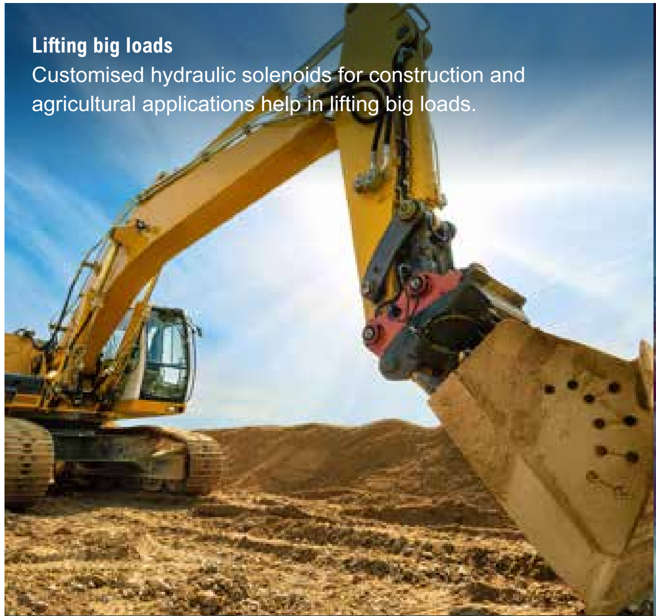
Industrial safety
Electromagnetic actuators used in safety switches protect people from getting injured while working with automated equipment.

Road and pedestrian safety
Sound actuators create a specific engine sound for hybrid and electric cars to ensure a safer environment for pedestrians and cyclists.

Safe no-break solutions in hospitals
Our solenoids help to switch to the power generators instantly in case of a power outage (and provide a constant source of power when it is needed most).

Safe transshipment
During loading and unloading, Kendrion's spring-applied brakes hold heavy goods safely.

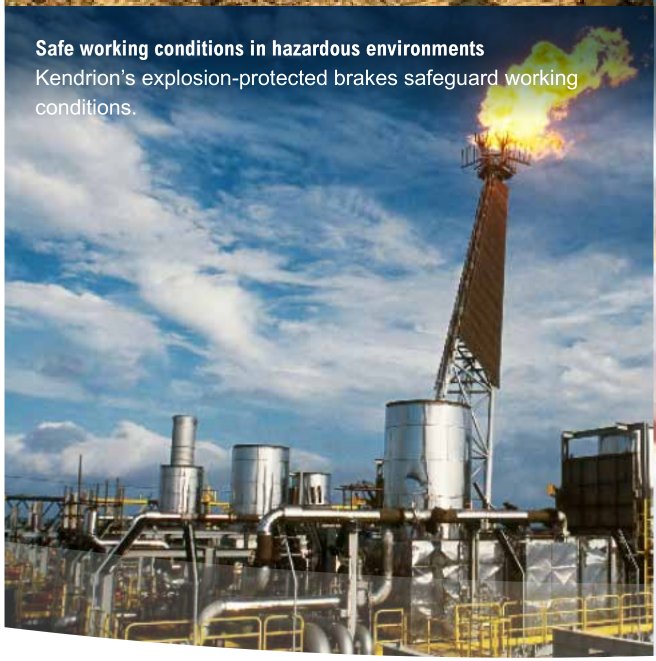
Comfort solutions
Electromagnetic clutches for mobile air conditioning ensure a pleasant climate in buses and trains.



Lifting big loads
Customised hydraulic solenoids for construction and agricultural applications help in lifting big loads.

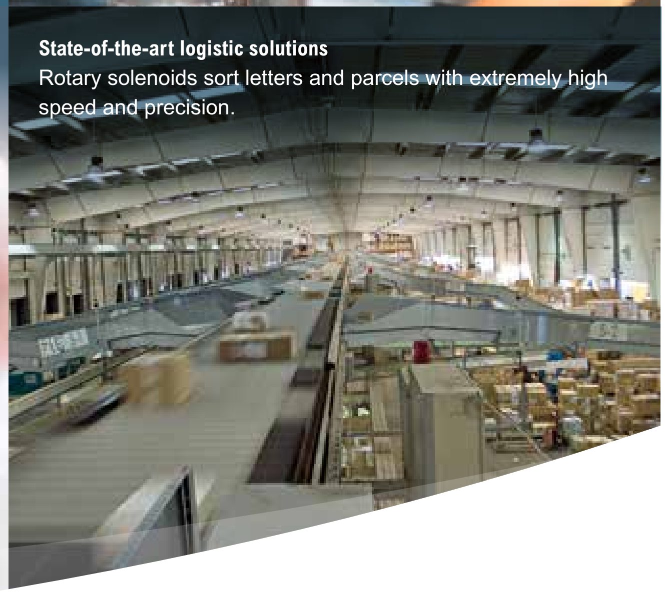
Comfortable and safe driving
Our electromagnetic actuators for active damping systems ensure a comfortable and safe ride.

High-quality industrial production processes
Power heat control systems provide efficient power management in blow molding machines for PET bottles.



Safe working conditions in hazardous environments
Kendrion's explosion-protected brakes safeguard working conditions.

Baby comfort technology
Electromagnetic valves solutions control oxygen flow in incubators for neonatology.



State-of-the-art logistic solutions
Rotary solenoids sort letters and parcels with extremely high speed and precision.

Kendrion develops, manufactures and markets high-quality electromagnetic systems and components for industrial and automotive applications.

For over a century, we have been engineering precision parts for the world's leading innovators in passenger cars, commercial vehicles and industrial applications. As a leading technology pioneer, Kendrion invents, designs and manufactures complex components and customised systems as well as local solutions on demand.

We are committed to the engineering challenges of tomorrow, and taking responsibility for how we source, manufacture and conduct business is embedded into our culture of innovation. Rooted in Germany, headquartered in the Netherlands and listed on the Amsterdam stock exchange, Kendrion's expertise extends across Europe to the Americas and Asia. Created with passion and engineered with precision.

Kendrion We magnetise the world

KENDRION N.V.

INDUSTRIAL

INDUSTRIAL MAGNETIC SYSTEMS

Customised solutions for switching, locking, holding and positioning based on electromagnetic technology

INDUSTRIAL CONTROL SYSTEMS

Industrial automation, locking units and fluid control systems

INDUSTRIAL DRIVE SYSTEMS

Full-line provider of electromagnetic brakes and clutches for industrial applications

AUTOMOTIVE

PASSENGER CARS

Electromagnetic and electronic components and systems for specific customer applications in the automotive industry

COMMERCIAL VEHICLES

Systems and components for commercial vehicles and off-highway applications with focus on hydraulics, valves and clutches

CEO
Joep van Beurden

2017: A good year for Kendrion

In 2016, CEO Joep van Beurden and CFO Frank Sonnemans announced ambitious targets for Kendrion: expected organic growth of 5% per year on average and a return on sales of 10% as from the end of 2018, close to doubling the results of 2015. In 2017, the company took an important step towards delivering those goals.

Joep van Beurden: 'We had a good 2017, as growth related to our existing project pipeline and more favourable market conditions enhanced the positive effect of our simplification measures. Revenue increased by 4.6% at constant rates of exchange and EBITA and net profit by 19% compared to 2016. Return on Sales (ROS) increased to 8%, a solid step towards the ambitious targets we set in 2016.'

GROWTH IN ALL BUSINESS UNITS

Frank Sonnemans: 'The Industrial activities recorded strong 7% revenue growth with higher activity levels across all business units. Industrial Drive Systems did especially well as it benefited from its focus on permanent magnet brakes for industrial robots. Germany, Kendrion's most important European market, continued to do well, driven by good growth of the German machine-building markets and related exports. There was also good progress in the USA and China. Automotive grew by 3%. Passenger Cars continued to benefit from the ramp-up of the production of the active damping valves for ThyssenKrupp Bilstein. Commercial Vehicles revenue declined somewhat due to the closure of its facility in Brazil in 2016 and the discontinuation of operations in India in 2017. Excluding these factors, the underlying Commercial Vehicles business showed good growth.'

PROGRESS IN STRATEGY

Joep van Beurden: 'We have made good progress on implementing Kendrion's *Simplify, Focus, Grow* strategy for 2016 – 2018. The primary objective is to deliver sustainable profitable growth for the business in the medium to long term. We do this by simplifying and streamlining our business activities and by focusing our resources and investments on market opportunities where we expect we can achieve double-digit growth. We see opportunity in Passenger Cars, specifically in the areas of electrification, autonomous driving, safety and comfort, in permanent magnet brakes for robots and in China. In 2017, the simplification and restructuring measures

CFO
Frank Sonnemans

resulted in one-off costs of EUR 5.1 million with corresponding cost savings of EUR 5.0 million. We have further optimised our manufacturing footprint, by discontinuing operations in India and Brazil and by consolidating our facilities in Nanjing (China), Switzerland and most recently Toluca (Mexico). We had a good year in China, with double-digit growth in both the top and bottom line. We also more than doubled our production capacity by opening a new facility in Suzhou, and we signed an LOI with one of our leading customers to set up a permanent magnet brake line in the same facility. Passenger Cars added several smart damping projects and increased the project pipeline for its sound actuators.'

STRONG FINANCIAL POSITION

Frank Sonnemans: 'Our financial position remains strong with a solvency ratio of 52% and an improved net debt/EBITDA cover of 0.95 at the end of the year. Return on Invested Capital (ROIC) increased strongly to almost 15%. In 2015, ROIC was at 10%, so we have achieved good progress here.'

TAKING RESPONSIBILITY

In 2017, Kendrion concluded its 2015 – 2017 CSR programme entitled 'Taking Responsibility'. This programme anchored sustainability practices in Kendrion's business processes and achieved significant progress on a number of sustainability parameters. 'We reduced our relative CO_2 emissions by almost 60% compared to 2014, we doubled the number of suppliers that have signed our Supplier Code of Conduct and we implemented comprehensive waste reduction plans, to give just a few examples. For 2018 and beyond, we have determined the outline of the next phase of our CSR strategy, building on the progress we have made over the past few years.'

IN GOOD SHAPE FOR FURTHER GROWTH

Joep van Beurden: 'For 2018, we expect favourable economic conditions in Europe, the USA and China. We expect to further simplify our business and focus on the markets where we believe we can grow by double digits: automotive, robotics, and in China. We look at the future with confidence, based on our strong business fundamentals, broad R&D capabilities, close customer relationships and growing project pipeline. We reiterate our expectation to grow annual revenue by an average of 5% and deliver an EBITA margin of 10% as from the end of 2018.'

Indicator	2017	Change	2016	2015
Revenue (EUR million)	461.8	↑ 4.2%	443.4	442.1
EBITA[1] (EUR million)	37.0	↑ 19%	31.1	25.8
Net profit[1] (EUR million)	23.3	↑ 19%	19.6	16.8
ROI[1,2] (in %)	14.5%	↑ 2.1%	12.4%	10.2%
Working capital[1] (as % of revenue)	9.9%	↑ 0.6%	9.3%	9.8%
Free cash flow[1] (EUR million)	14.2	↓ 37%	22.3	21.2
Solvency	52.3%	↑ 1.0%	51.3%	49.8%
Net debt / EBITDA[1]	1.0	↓ 10%	1.1	1.5

[1] Excluding one-off costs relating to simplifying measures.
The bridge from reported to normalised figures can be found on page 35.

[2] Total invested capital is property, plant and equipment, intangible assets, other investments and current assets less cash and non-interest bearing debts.

2,645 ↑ 2.6%
Total number of employees (FTE)
(at 31 December)
2016 **2,578** 2015 **2,658**

50%/50%
Total number of employees by gender
(in % M vs F)
2016 **50%/50%** 2015 **51%/49%**

2.7%
Illness rate
(in %)
2016 **2.6%** 2015 **2.5%**

18
Accidents
2016 **37**
2015 **41**

432
Lost Time Injuries
(in days)
2016 **418**
2015 **863**

173.9 ↓ 8.5%
Relative energy consumption
(in tonnes kWh/million added value)
2016 **190.1** 2015 **201.6**

33.5 ↓ 7.1%
Relative CO_2 emission
(in tonnes kWh/million added value)
2016 **36.0** 2015 **62.4**

728
Number of accepted Supplier Codes of Conduct
2016 **669** 2015 **368**

37
Number of CSR supplier audits
2016 **37** 2015 **36**

See for reporting periods, definitions, scope and external assurance pages 162 and 163 of this report.

SIMPLIFY

Kendrion has decided it needs to simplify the way it does business. Complexity drives cost and slows down decision-making and Kendrion is reducing costs in order to improve operating margin and profitability.

THREE YEAR PLAN – SPECIFIC FOCUS

- **Cost reduction**
- **Organisational structure**
  Industrial Magnetic Systems
  Industrial Control Systems
  Industrial Drive Systems
  Passenger Cars
  Commercial Vehicles

FOCUS

Kendrion will focus its resources and capital on those areas which have the most opportunities for profitable growth. Taking Responsibility (our CSR policy) is part of this focus.

THREE YEAR PLAN – SPECIFIC FOCUS

- **China**
- **Passenger Cars**
- **Permanent Magnet brakes in robots**

GROW

The clarity Kendrion will gain through the first two pillars of the plan is intended to allow growth in revenue in a way which will ultimately provide the opportunity to grow faster than the historical average of 5%. Due to the project lead time in Kendrion's business, Kendrion expects organic growth to accelerate in the years beyond 2018.

THREE YEAR PLAN – SPECIFIC FOCUS

- **Automotive market**
  Fuel systems, engine management, sound systems, fuel cell valves, chassis suspension, human machine interface
- **Industrial market**
  Drive systems, conveyor systems, energy generation and distribution, elevator systems, door access and control for machinery, oxygen systems

Strategic financial targets

TARGET	ACTUAL	
5%	4.6%	**Expected average organic growth** at constant rates of exchange, per annum until 2018
10%	8.0%	**EBITA margin** as from the end of 2018
35-50%	50%	**Dividend policy** pay out ratio of the net profit

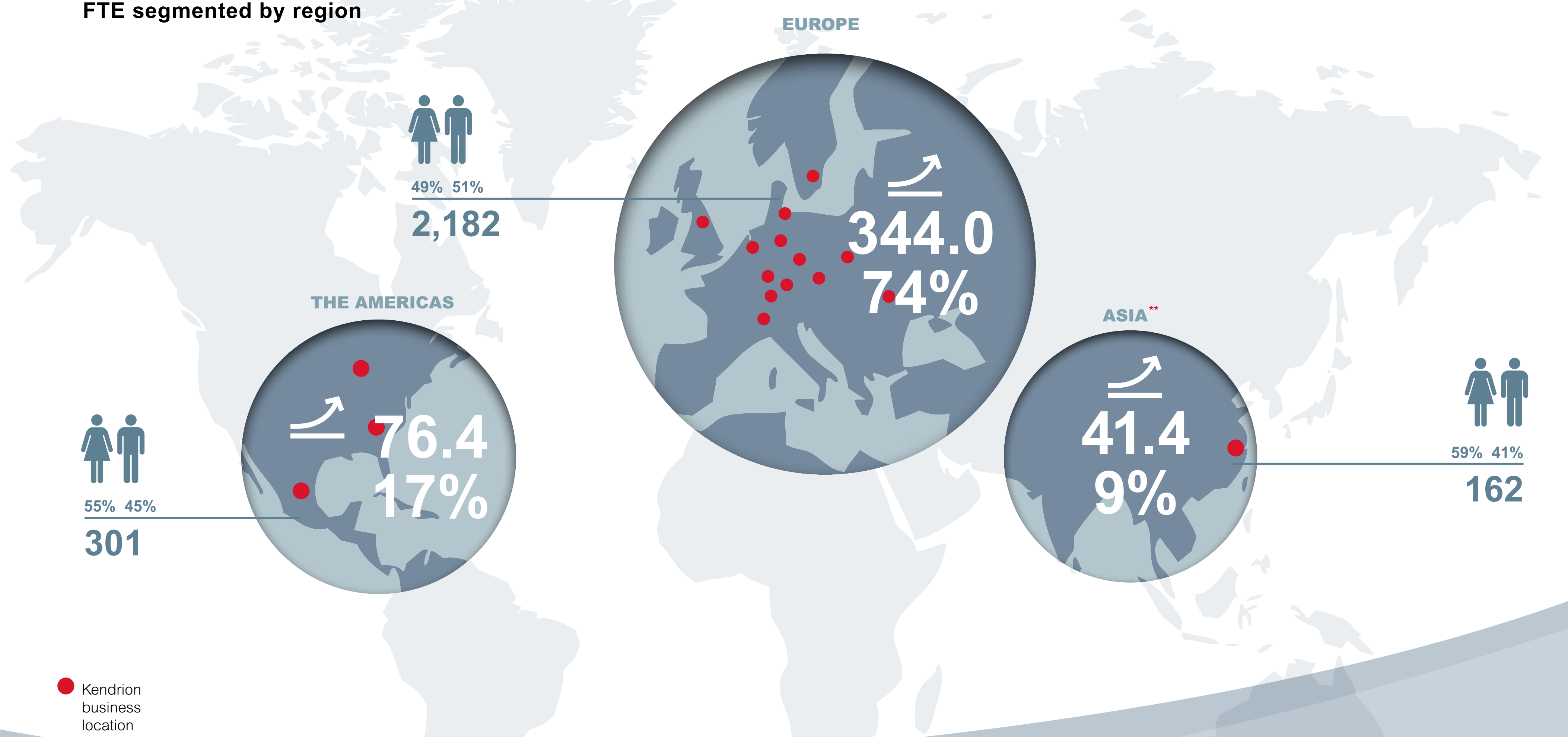
Our target up to 2018

Kendrion stated its medium-term financial objectives on 3 May 2016. The three-year targets are to deliver an EBITA margin of 10% as from the end of 2018, to grow organically until 2018 broadly in line with Kendrion's average historical organic growth of an average of 5% per annum and to maintain the dividend policy of paying out 35 to 50% of the net profit.

Targeted add-on acquisitions

Kendrion has a strong financial position and has delivered excellent rates of cash conversion which have contributed to a healthy balance sheet. Kendrion endeavours to acquire companies that enhance the company's leading position in its automotive and industrial markets. Acquisition targets need to offer good returns in terms of their EBIT and ROI, preferably at levels similar to or above Kendrion's returns and that leads to an improvement in earnings per share.

Revenue (in EUR million) segmented by customer location
FTE segmented by region



FINANCIAL RESULTS
EUR million

Revenue	EBITA*	Net profit*	EBITA %*	ROI*	Total FTE
461.8	37.0	23.3	8.0%	14.5%	2,645

* Excluding one-off costs relating to simplifying measures. The bridge from reported to normalised figures can be found on page 35.
** Including Other countries with revenue of EUR 2.0 million.

Strengths

- Innovation
- Engineering capabilities
- Reputation for quality and reliability
- Leading positions in key markets segments
- Longstanding relationships with reputable customers
- The ability to produce globally at consistently high standards
- Sound financial position and high cash conversion
- Advanced in Corporate Social Responsibility

Weaknesses

- Still underrepresented in Chinese market
- Low growth in certain legacy activities
- Suboptimal use of synergies between locations and business units due to the decentralised structure
- Less than desired diversification in top management positions

Opportunities

- The electrification and automation of cars and trucks
- Robotisation requiring electromagnetic brake solutions
- Sound systems for acoustic alerting systems in electric vehicles
- M&A
- China
- Ongoing reduction of complexity to enhance organisational effectiveness

Threats

- High investments required in research and development and production lines
- Lower demand for diesel-powered cars
- Scarcity of highly qualified staff and engineers in particular
- Commoditisation of part of the product portfolio
- Shortage of raw materials and fluctuating prices
- Deterioration of global geopolitical and economic environment

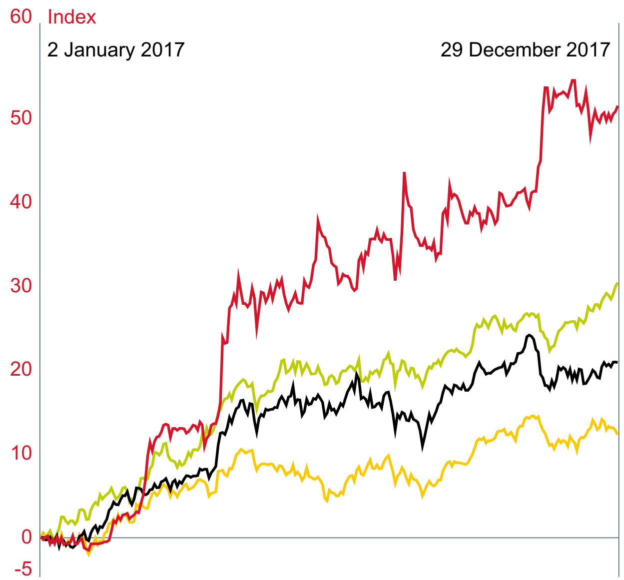
Share capital

The authorised share capital of Kendrion N.V. amounts to EUR 80,000,000, divided into 40,000,000 ordinary shares, each having a nominal value of EUR 2.00. The total number of issued shares as at 31 December 2017 amounted to 13,517,620. There is only one class of ordinary shares and no depositary receipts for shares have been issued. Kendrion's ordinary shares are listed on NYSE Euronext Amsterdam Small Cap Index (AScX).

Movements in the share price

from 2 January 2017 to 29 December 2017

Kendrion N.V. share | AEX
ASCX | AMX



Movements in the number of outstanding shares

	Shares entitled to dividend	Shares owned by Kendrion	Total number of issued shares
At 1 January 2017	13,396,034	–	13,396,034
Issued shares (share dividend)	115,157	–	115,157
Issued registered shares (share plan)	6,429	–	6,429
Delivered shares	1,843	(1,843)	–
Repurchased shares	(123,429)	123,429	–
At 31 December 2017	13,396,034	121,586	13,517,620

Other information

EUR, unless otherwise stated	2017	2016	2015
Number of shares x 1,000 at 31 December	13,518	13,396	13,188
Market capitalisation at 31 December (EUR million)	542.9	358.3	319.7
Enterprise value (EV) (EUR million)	597.4	412.3	388.8
Highest share price in the financial year	40.95	27.87	30.39
Lowest share price in the financial year	26.30	19.00	19.18
Share price on 31 December	40.16	26.75	24.24
Average daily ordinary share volume	18,048	13,352	37,123
EBITDA multiple (over EV)[1]	10.42	8.02	8.59
Result per share	1.45	1.12	1.28
Normalised result per share[1]	1.73	1.47	1.28
Share price earnings ratio[1]	23.16	18.18	19.01

Major shareholders as at 31 December 2017

	Interest in %	Date of report
Teslin Participaties Coöperatief U.A.	12.29	At 6 July 2017
NN Group N.V.	9.52	At 7 April 2017
Kempen Capital Management N.V.	5.98	At 23 November 2015
Cross Options Beheer B.V.	5.37	At 8 May 2017
Monolith N.V.	5.24	At 8 May 2017
T. Rowe Price Group, Inc.	4.97	At 5 May 2017
T. Rowe Price International Funds, Inc.	4.03	At 18 April 2017
Capfi Delen Asset Management	3.21	At 9 May 2017
Total	50.61	

[1] Excluding one-off costs relating to simplifying measures.
The bridge from reported to normalised figures can be found on page 35.

HIGH-TECH SORTING SWITCH IN OVERHEAD CONVEYING SYSTEMS

Product: High-performance bistable rotary solenoid.

Customer: A leading international company which offers a wide range of modular transport solutions, capable of handling the most diverse commercial goods flows with maximum efficiency.

Kendrion's solution: An overhead conveying system is an efficient transport system as it uses available space below the ceiling. The rotary solenoids execute quick and reliable switching operations within the rail system. Kendrion is using this application to expand its expertise in the replacement of pneumatics and is growing in the logistics industry.

Added value: Replacing the pneumatic components with electromagnets allows the customer to offer a low-maintenance and energy-efficient solution that does not require a compressed air supply.

Treasury shares

Due to a share buyback programme in 2017, Kendrion N.V. currently holds 121,586 ordinary shares in its own capital, representing 0.9% of the total issued share capital.
The own shares held by Kendrion N.V. are non-voting, do not have any dividend entitlement, and are held in treasury for distributing stock dividends, the share plan for top management and general company purposes.

Dividend policy

Kendrion endeavours to realise an attractive return for shareholders supported by a suitable dividend policy. However, in view of safeguarding a healthy financial position, consideration is also given to the amount of profit to be retained to support the company's medium- and long-term strategic plans and to maintaining a minimum solvency ratio of 35%. Kendrion strives to distribute dividends representing between 35% and 50% of its net profit.

In principle, Kendrion offers shareholders an opportunity to opt for dividends in cash or in the form of ordinary shares in Kendrion N.V.'s capital.

Kendrion will propose a dividend of EUR 0.87 per share, representing a payment of dividend of 50% of normalised net profit for 2017 at the Annual General Meeting of Shareholders on 9 April 2018. The total amount of dividend is EUR 11.7 million. It will be proposed that payment of the dividend be made in cash, or, at the option of shareholders, in the form of ordinary shares charged to the share premium reserve with any remaining fraction being settled in cash.

Major shareholders

Any person holding or acquiring an interest of 3% or more in a Dutch publicly listed company is bound, based on the Financial Supervision Act (*Wet op het Financieel Toezicht*), to disclose such a holding to the Dutch Authority for the Financial Markets (AFM). The disclosure is recorded in the register of the AFM and listed on the AFM website (www.afm.nl).

Share buybacks

A programme for buying back 121,586 ordinary shares was launched in 2017 to neutralise the dilutive effect of the 2016 final stock dividend and share-based incentive plans. These shares will be held as treasury shares and will be used to pay future stock dividends and share-based incentive plans. The programme commenced on 21 August 2017 and was completed on 1 December 2017.

Participation

The share plan for top management provides for the issue of shares in Kendrion. The Business Unit Managers and a number of other officers were eligible to apply for the conversion of a maximum of half of the amount of their annual net cash bonus into shares. Under this plan, Kendrion offers to double the number of shares after three years, provided the Business Unit Manager or other officer concerned is still employed by Kendrion and still holds the shares. Pursuant to these share plans, a total of 6,430 ordinary shares was issued in 2017.

A bonus in shares was granted to the members of the Executive Board for 2017. More information about the shares granted to the members of the Executive Board is set out on pages 136 and 137 and 145 and 146. A comprehensive description of the bonus scheme is included in the 'Remuneration policy' section on pages 73-75.

Regulations to prevent insider trading

Kendrion has regulations covering securities transactions by members of the Executive Board, members of the Supervisory Board, members of the Management Team and other designated employees. The Insider Trading Code is published on Kendrion's website. The Insider Trading Code is intended to ensure the avoidance of insider trading or the appearance thereof, and any mixing of business and private interests.

Investor relations

Kendrion attaches great importance to appropriate communications with financial stakeholders such as investors, debt capital providers and analysts to provide them with good insight into the developments at Kendrion. Transparency is intended to lead to healthy pricing, and supports sufficient liquidity.

Liquidity provider

In 2017, NIBC Bank N.V. acted as a liquidity provider for Kendrion N.V. As such, NIBC Bank acts as the counterparty for buy or sell orders for which the bid and ask prices are set within a range around the last executed price. Relatively small (retail) buy and sell orders can then be conducted via the liquidity provider, which results in a fairer and more orderly market.

Analysts

The following stock exchange analysts actively monitor the Kendrion share:

ABN AMRO Bank N.V.	Maarten Bakker
Degroof Petercam	Frank Claassen
ING Bank N.V.	Tijs Hollestelle
Kepler Cheuvreux	Guido Nunes
NIBC Markets N.V.	Johan van den Hooven
The Idea-Driven Equities Analyses Company	Maarten Verbeek

Financial calendar

Wednesday, 21 February 2018	Publication of the 2017 full-year figures
Monday, 12 March 2018	Record date General Meeting of Shareholders
Monday, 9 April 2018	General Meeting of Shareholders
Wednesday, 11 April 2018	Ex-dividend date
Thursday, 12 April 2018	Dividend record date
Friday, 13 April – Monday, 30 April 2018, 3 pm	Dividend election period (stock and/or cash)
Wednesday, 2 May 2018	Determination stock dividend exchange ratio
Friday, 4 May 2018	Cash dividend made payable and delivery stock dividend
Wednesday, 9 May 2018	Publication of the results for the first quarter of 2018
Wednesday, 15 August 2018	Publication of the results for the first six months of 2018
Wednesday, 7 November 2018	Publication of the results for the third quarter of 2018
Tuesday, 19 February 2019	Publication of the 2018 full-year figures
Monday, 8 April 2019	General Meeting of Shareholders

T.J. Wünsche
H. ten Hove
J.T.M. van der Meijs
M.J.G. Mestrom

H. ten Hove (65)

Mr Ten Hove was appointed Chairman of the Supervisory Board as of December 2013. The Extraordinary General Meeting of Shareholders appointed Mr Ten Hove as a member of the Supervisory Board for a four-year term from 19 August 2013 until 2017. He was reappointed in April 2017 for a period of four years until 2021.
Mr Ten Hove is a member of the HR Committee of Kendrion N.V.
Mr Ten Hove is a member of the Supervisory Boards of SPG Prints B.V. and Unica Groep B.V. He is Chairman of the Economic Board of the Zwolle region and Chairman of the foundation which owns the shares of BDR Thermea. He is a former CEO of Wavin N.V.
Mr Ten Hove is a Dutch national.
He does not hold any shares in Kendrion.

J.T.M. van der Meijs (52)

Mrs Van der Meijs was appointed a member of the Supervisory Board for a term of three years during the Extraordinary General Meeting of Shareholders held on 31 October 2016. She has served as Chair of the Audit Committee of Kendrion N.V. since 10 April 2017.
She has broad experience in international senior finance roles. Mrs Van der Meijs is CFO of Royal Schiphol Group.
Mrs Van der Meijs is a non-executive member of the board of AdP (Aéroports de Paris). In the period from 2009 to October 2016, she was Vice-President Finance (Capital Projects) at Shell Global Solutions in Rijswijk, the Netherlands.
She previously served as Finance Director at Shell Australia from 2007 to 2009 and as Financial Controller/Deputy Finance Director at the Brunei Shell Companies from 2002 to 2007.
Mrs Van der Meijs is a Dutch national.
She does not hold any shares in Kendrion.

M.J.G. Mestrom (56)

Mrs Mestrom was appointed a member of the Supervisory Board for a term of four years during the General Meeting of Shareholders held on 11 April 2016. She is Chair of the HR Committee of Kendrion N.V.
Mrs Mestrom has broad experience in global senior HR roles and is currently Head of Global Human Resources at Brenntag AG, a German listed company. She previously headed Global Human Resources for the Germany-based Siegwerk Druckfarben Group. Before joining Siegwerk, she held several Global Human Resources positions within Royal Philips, including an international posting in Asia for almost five years.
Mrs Mestrom is a Dutch national.
She does not hold any shares in Kendrion.

T.J. Wünsche (54)

Mr Wünsche was appointed a member of the Supervisory Board for a term of four years during the Extraordinary General Meeting of Shareholders held on 31 October 2016. He is also a member of the Audit Committee of Kendrion N.V.
Mr Wünsche has more than twenty years' automotive experience, including more than ten years' experience in North America.
He is Global CEO of the Chassis Brakes International Group in Eindhoven, the Netherlands. He previously served as CEO of Benteler Automotive from 2012 to 2014 and as CEO of Eberspächer Exhaust Technology from 2006 to 2012. Mr Wünsche is also a member of the Supervisory Board of the Altenloh, Brinck & Co. Group, based in Germany.
Mr Wünsche is a German national.
He does not hold any shares in Kendrion.

In accordance with the schedule of rotation, Mr De Bakker retired as a member of the Supervisory Board during the General Meeting of Shareholders held on 10 April 2017.

Introduction

The Supervisory Board's main responsibility is to supervise and advise the Executive Board, in particular regarding the strategy for realising long-term value creation and the manner in which the strategy is implemented.

In May 2016, Kendrion launched an updated strategy to deliver sustainable profitable growth for the business in the medium to long term through the three pillars: 'Simplify, Focus, Grow'. To meet its targets in a sustainable and profitable manner, Kendrion is committed to reducing complexity and increasing cost efficiency, while focusing its R&D on areas that can generate long-term sustainable growth. In 2017, the Executive Board continued to implement simplification measures with a view to establishing a simpler and more streamlined organisation. The Executive Board also enhanced its focus on Passenger Cars, Permanent Magnet brakes for robotics and China, where Kendrion has substantial growth opportunities.

After one and a half years, the organisation is less complex in its footprint and structure and has more focus in its product and customer portfolio, while innovation initiatives have been streamlined.

In 2018, the Executive Board is committed to building on its 'Simplify, Focus, Grow' strategy.

Activities and priorities

The Supervisory Board acknowledges that a simplified and focused organisation provides a solid foundation for the realisation of Kendrion's growth targets in a sustainable and profitable manner. The year ahead is pivotal in the 'Simplify, Focus, Grow' drive. The Supervisory Board is closely monitoring the preparations for the follow-on plan that will cover the years after 2018. Similarly, the Executive Board engaged with the Supervisory Board concerning the CSR strategy for the period 2018 and beyond, which will be integrated with the Mid-term Plan 2019 – 2023.

The Supervisory Board, in coordination with the Executive Board and the Management Team, identified a number of key items requiring specific attention and emphasis during 2017:

- *Revenue growth beyond 2018*

One of the expectations of the 'Simplify, Focus, Grow' strategy relates to the ambition to maintain an average 5% annual organic revenue growth. Understanding that year-on-year growth may vary due to different circumstances, the Supervisory Board put emphasis on gaining adequate insight into changes in Kendrion's key markets beyond 2018. Particular consideration was given to the developments in the automotive industry in the areas of electrification, autonomous driving, safety & comfort and especially the extent to which these developments may create opportunities and challenges for Kendrion. Regarding Kendrion Industrial, developments and trends relating to the robotics branch are key as it presents Kendrion with substantial opportunities. The Supervisory Board deliberated about the growth opportunities from a geographical perspective with a specific focus on China and the USA.

- *Revised Dutch Corporate Governance Code*

In 2016, the Corporate Governance Code Monitoring Committee amended the Dutch Corporate Governance Code (the 'Code'). Kendrion has a policy to improve its governance structure and ensure alignment with the Code. Therefore, during 2017, specific attention and priority was given to the amendments of the Code.

Consistent with past practices, the Supervisory Board considered the importance of long-term value creation when performing its supervisory responsibilities, thereby taking into account the interests and reasonable expectations of Kendrion's stakeholders.

'Company culture' is an important theme, and going forward the further encouragement of a culture focused on long-term value creation and compliance continues to be important, including the development of values that contribute positively to such a culture.

Substantial efforts were made with regard to the effectiveness of risk management and internal control systems and the integrity and quality of financial reporting, including the implementation of further improvements to the risk management process and procedures in 2017. Furthermore, the Supervisory Board was able to review and discuss the main findings included in the management letter prepared by the external auditor Deloitte Accountants B.V.

As further described in the report of the HR Committee, the Supervisory Board reconsidered the remuneration policy for the members of the Executive Board with a view to reducing the complexity of the policy, whilst – to the extent possible and reasonable – adhering to the principle of maintaining the overall value of the remuneration packages of the members of the Executive Board.

At the next General Meeting of Shareholders on 9 April 2018, the updated remuneration policy and the share-based plan associated with it will be presented for adoption and approval, respectively.

Reference is made to the Supervisory Board report on pages 25 and 26 for more information about the HR Committee meetings, including the preparation of proposals for a revised remuneration policy for the Executive Board and related plan documentation.

The introduction of the new Code also triggered a detailed review of the Supervisory Board regulations as well as the regulations for its committees. During several Supervisory Board meetings, updates to these regulations were discussed and subsequently adopted in January 2018.

- *New long-term Corporate Social Responsibility programme*

2017 was the final year of Kendrion's CSR strategy for 2015 – 2017. In the course of 2017, the Executive Board together with the Management Team developed proposals for the CSR strategy for 2018 and beyond. The emphasis of the updated CSR strategy is on long-term value creation for Kendrion and society through pillars of value creation. The Supervisory Board believes that the CSR strategy outlined for 2018 and beyond reconfirms Kendrion's continued commitment to increasing sustainable practices within Kendrion's business processes.

Reference is made to the section 'Corporate Social Responsibility' on pages 41-57 for more information about CSR and the realisation of CSR-related targets.

- *Management development and succession planning*

Kendrion continued to improve its HR processes during the year under review. One of these improvements concerns the implementation of a web-based global talent management and succession planning tool. The tool allows for consistent monitoring of the individual performance and development of senior management across the Kendrion group and provides insight into potential critical succession gaps.

- *Team effectiveness of the Supervisory Board in its new composition*

The Supervisory Board had team training and regular bilateral contacts, which contributed to its effectiveness. The Supervisory Board continued to spend the necessary time relevant for the proper performance of its duties, including regular meetings with the Executive Board, the Management Team and visits to selected Kendrion operations.

For 2018, the Supervisory Board expects to focus specifically on:

- Formulation of a sustainable profitable growth strategy for a rolling five-year strategy cycle: 2019 – 2023;
- Ensuring a continuous operational improvement programme throughout Kendrion;
- Finalisation of an ambitious CSR strategy for the period 2018 and beyond;
- Follow-up on growth opportunities in China and the USA.

Composition and diversity

The Supervisory Board consists of four members, the Executive Board consists of two members and the Management Team consists of eleven members.

Mr De Bakker stepped down after the maximum period of 12 years as a member of the Supervisory Board during the General Meeting of Shareholders held on 10 April 2017. He was a respected and appreciated member of the Supervisory Board and Chairman of the Audit Committee. The Supervisory Board is grateful for his contribution to Kendrion.

The Supervisory Board operates independently of the Executive Board, the Management Team, any other participating interests and each other. Each of the Supervisory Board members has the necessary expertise, experience and background to perform his or her tasks and responsibilities. All members of the Supervisory Board are independent within the meaning of the Dutch Corporate Governance Code as amended by the Corporate Governance Code Monitoring Committee in 2016. The members of the Supervisory Board satisfy the statutory requirements concerning the number of supervisory or non-executive functions that they can have with large enterprises.

On 10 April 2017, Mr Frank Sonnemans was reappointed to the Executive Board, and there were two vacancies within the Management Team which were filled in the course of 2017.

> The Supervisory Board advocates focusing strongly on the company's social and environmental standards with regard to its processes and on the relationship between the overall strategy and sustainability.

For the current composition of the Supervisory Board and its committees, reference is made to the profiles of the members of the Supervisory Board, which can be found in the Report of the Supervisory Board on pages 19 and 20.

For the current composition of the Executive Board and information about its members, reference is made to the profiles, which can be found in the Report of the Executive Board on page 27. For more information about the composition of the Management Team, reference is made to the 'Corporate Governance' section on page 68.

The Supervisory Board is dedicated to encouraging a diverse and inclusive culture within Kendrion. Diversity is a recurring theme in its discussions with the Executive Board and the members of the Management Team.

The Supervisory Board attaches great value to diversity and upholding a tailored diversity strategy with appropriate objectives, which is not limited to encouragement of diversity at the level of the Executive Board, the Management Team, and the Supervisory Board, but also includes encouragement of a diverse workforce in terms of gender, skills, nationality, age and other factors across the Kendrion group.

The composition of the Supervisory Board reflects balanced participation of two men and two women within the meaning of article 2:66 of the Dutch Civil Code. The Executive Board currently does not reflect this gender balance, and consists of two men. The Management Team consists of a healthy mix of skills, nationality, age, background and other relevant factors. Gender diversity in the Management Team improved in 2017.

Name	Year of appointment	Year of next reappointment	Final term expires	Current number of SB positions
H. ten Hove (Chairman)	2013	2021	2025	3 (1 Chair)
J.T.M. van der Meijs	2016	2019	2023/2028	2
M.J. G. Mestrom	2016	2020	2024/2028	1
T. J. Wünsche	2016	2020	2024/2028	2

Name	Year of birth	Nationality	International expertise	Professional experience	Gender
H. ten Hove (Chairman)	1952	Dutch	Yes	Manufacturing/industry	Male
J.T.M. van der Meijs	1966	Dutch	Yes	Finance	Female
M.J. G. Mestrom	1961	Dutch	Yes	HR/org. design	Female
T. J. Wünsche	1964	German	Yes	Automotive	Male

Meetings and attendance

The Supervisory Board held seven meetings in 2017, which were all regular scheduled meetings. All meetings were attended by the members of the Executive Board, and at times by members of the Management Team. In addition, several meetings were held without the members of the Executive Board and the Management Team. The external auditor Deloitte Accountants B.V. attended two meetings of the Supervisory Board.

Supervisory Board attendance during 2017 was 93%. Absence was limited to exceptional situations. Mr Wünsche attended six of the seven Supervisory Board meetings in 2017. Mr De Bakker attended one of the two Supervisory Board meetings before he stepped down as a member of the Supervisory Board on 10 April 2017. The agenda for the Supervisory Board meetings included a number of recurring items such as: operational and financial performance; progress in executing the strategic plan and the principal risks associated with it; progress and the achievement of milestones of special projects; risk management and internal control systems; governance and compliance. In February 2017, the external auditor attended the meeting of the Supervisory Board in which the full-year figures for 2016 and the auditor's report were discussed, including, amongst other things, the key findings, valuation of goodwill, internal control and the draft auditor's opinion.

In December 2017, the external auditor attended the meeting of the Supervisory Board when the management letter and key findings of the external auditor and risk management were discussed. The Supervisory Board expressed its satisfaction that the management letter once again revealed only a limited number of findings and no findings which qualified as significant. More information can be found in the section 'Risks and risk management' on pages 58-66.

At various times, presentations were given to the Supervisory Board by one or more members of the Management Team or other responsible senior managers.

Other topics that were given specific attention and emphasis during 2017 included sustainability and value creation, Executive Board remuneration, risk management, IT and cybersecurity, management development, progress on the business and organisation in China and the USA, and the closure of certain manufacturing sites.

Together with the Executive Board and certain members of the Management Team, the Supervisory Board attended a two-day strategic session at Kendrion's US site located in Shelby, North Carolina. Topics discussed during the session included relevant market trends, Kendrion's position and the competitive landscape. The Chairman of the Supervisory Board held monthly meetings with the CEO. The Supervisory Board – often through coordination of the Chairman of the Supervisory Board – maintained regular contact with the members of the Management Team.

Committees of the Supervisory Board

The Supervisory Board has established two committees: an Audit Committee and an HR Committee, the latter was previously referred to as the Remuneration Committee. The primary task of the committees of the Supervisory Board is to advise and facilitate the Supervisory Board with respect to its responsibilities and to prepare the decision-making by the Supervisory Board. The committees of the Supervisory Board have their own regulations, which include a detailed description of the committee's tasks and responsibilities.

Audit Committee

The Audit Committee uses its knowledge and expertise to advise on and prepare the Supervisory Board's decision-making, particularly concerning matters relating to the integrity and quality of financial reporting and effectiveness of risk management and internal control systems. This includes a focus on IT and cybersecurity and the risks related thereto.
The Audit Committee consists of Mrs Jabine van der Meijs and Mr Thomas Wünsche. Mrs Van der Meijs took over the role of Chair of the Audit Committee from Mr De Bakker when he stepped down as member of the Supervisory Board at the General Meeting of Shareholders on 10 April 2017. The members of the Audit Committee collectively have the experience and expertise to perform the responsibilities assigned to the Audit Committee and are dedicated to ensuring the quality of Kendrion's financial reporting and to ascertaining that Kendrion maintains adequate procedures and control systems to manage the risks to which Kendrion is exposed, including strategic, business and operational risks, financial risks and compliance risks.

The Audit Committee held four meetings in 2017. Attendance during 2017 was 78% with Mr Wünsche attending two of the four Audit Committee meetings in 2017. The CFO and the Group Controller attended all meetings. The external auditor Deloitte Accountants B.V. attended the meetings of the Audit Committee at which the full-year figures for 2016 and half-yearly figures for 2017 were discussed. The Audit Committee met once with the external auditor outside the presence of the CFO. The Audit Committee considered regular topics such as: annual and interim financial statements, auditor's report, effectiveness and outcome of risk management and internal control systems, risk management, audit plan of the external auditor, insurance, tax policy, transfer pricing, IT and cybersecurity, speak-up procedure, legal and compliance, annual evaluation of external auditor and annual evaluation concerning the absence of an internal audit department.

The Audit Committee and the Supervisory Board reviewed Kendrion's risk management and internal control systems and their effectiveness in detail. The auditor's overview of internal control issues was discussed together with the status of the internal tests on the financial reporting systems.

In view of the annual evaluation concerning the absence of an internal audit department, the Audit Committee also deliberated about the current set-up of the internal audit function, the approach and operation of the internal audit programme (Kendrion in Control) and the matters arising from the internal audit programme. Based on the recommendation of the Audit Committee, the Supervisory Board is of the opinion that the risk management and internal control systems, as described in more detail in the section 'Risks and risk management' on pages 58-66, meet Kendrion's needs, that adequate measures have been taken and that the establishment of an independent internal audit department is not necessary.

The Audit Committee devoted extensive attention to the Management Letter and internal audit findings and also to the way in which the limited number of small issues can be solved.

SMART TRIP COIL FOR LOW-VOLTAGE CIRCUIT BREAKER

Product: High-performance linear solenoid.

Customer: A global leader in power and automation technologies.

Kendrion's solution: Trip coils for undervoltage and shunt opening releases, including PCBA board (Printed Circuit Board Assembly), making it possible to interrupt the power in case of emergency or issues with the power network. This will contribute to the increase in market share in the important electromagnetic markets for energy and automation solutions.

Added value: Specific R&D competencies, production facilities in China and a strong sales network in Europe.

In addition to the above, the Audit Committee considered the following matters:

- Relevant substantive revisions to the Dutch Corporate Governance Code.
- The irregularity that was reported by an employee in 2017 involving the sale of products by employees for their own personal benefit and allegations of violation of the Kendrion Code of Conduct by local management. The irregularity only had a minor financial impact. For more information, reference is made to the section 'Risks and risk management' on page 60.
- An update on the cybersecurity audits that were conducted in 2016, the risk mitigation measures that have been taken and the additional measures that are planned.
- The functioning of the external auditor Deloitte Accountants B.V., taking into account the outcome of the internal evaluation process involving Kendrion's operating companies and group management. In this context the subject of 'auditor independence' and the extent to which non-audit related services can be performed were considered.
  At the next General Meeting of Shareholders on 9 April 2018, a proposal will be made for the extension of the engagement and reappointment of Deloitte Accountants B.V. as external auditor of Kendrion.

HR Committee

The HR Committee (previously named the Remuneration Committee) deals with all HR-related matters such as management development, company culture, diversity and organisational structure. An important task of the HR Committee is to advise and submit proposals to the Supervisory Board relating to the remuneration policy and the remuneration of individual members of the Executive Board. The HR Committee consists of Mrs Marion Mestrom and Mr Henk ten Hove. The members of the HR Committee collectively have the experience and expertise to perform the responsibilities assigned to the HR Committee. Mrs Mestrom is Chair of the HR Committee.

The HR Committee met twice in 2017; both meetings were regular scheduled meetings. Attendance during 2017 was 100%. Both meetings were attended by the CEO. In addition to the scheduled meetings, the HR Committee had a number of informal meetings with and without the members of the Executive Board being present.

The HR Committee made recommendations, prepared and conducted performance meetings with the members of the Executive Board and discussed the amount of variable remuneration earned for 2016 and the target-setting for 2017. For further details concerning the remuneration of the Executive Board, reference is made to the 'Remuneration policy' section on pages 73-75.

The Executive Board informed the HR Committee about the outlines of the remuneration structure applicable to members of the Management Team, who are not members of the Executive Board.

The HR Committee spent considerable time on the development of a revised remuneration policy for members of the Executive Board, with a view to reducing the complexity of the policy, whilst – to the extent possible and reasonable – adhering to the principle of maintaining the overall value of the remuneration packages of the members of the Executive Board. Based on the advice of the HR Committee, at the next General Meeting of Shareholders on 9 April 2018, proposals will be made for the adoption of an updated remuneration policy for the Executive Board and the approval of share-based plans associated with it. The proposed amendments to the remuneration policy were designed with the support of an external specialised consulting firm. The HR Committee conducted a scenario analysis in the context of the design of the proposed amendments to the remuneration policy.

Functioning of the Supervisory Board and the Executive Board

The Supervisory Board discussed, in the absence of the Executive Board, its own functioning, the functioning of the Audit Committee and the HR Committee and the functioning of the individual members of the Supervisory Board. The evaluation was performed by the Chairman of the Supervisory Board, by means of a structured questionnaire, and subsequently discussed with the members of the Supervisory Board. The questionnaire was also filled in by the Executive Board and addressed items such as: team effectiveness; interaction; transparency; composition and profile; competences; effectiveness of individual members; quality of information and the relationship with the Executive Board and others, which is meant to also include the relationship with the Management Team.

The outcome of the evaluation is generally positive. Despite its relatively new composition, it was found that the Supervisory Board has rapidly organised itself in an effective and efficient manner. There is a good level of transparency among the Supervisory Board members and in the relationship between the Supervisory Board and the Executive Board.

The non-executive directors' training session that was held early in 2017 covered the revised Corporate Governance Code, roles and responsibilities and boardroom dynamics, among other subjects. The session gave guidance on how to operate as an effective non-executive board.

The Supervisory Board discussed, in the absence of the Executive Board, the functioning of the Executive Board and that of the individual members of the Executive Board. The discussions were held on the basis of observations and views shared by each of the members of the Supervisory Board. The outcome of the evaluation of the performance of the Executive Board and its members is positive. The conclusions of the evaluation was discussed with the members of the Executive Board during annual performance meetings.

Financial statements and auditor's opinion

The financial statements 2017 included in this Annual Report have been audited and Deloitte Accountants B.V. has issued an unqualified opinion on them. They were extensively discussed with the Supervisory Board, the Audit Committee in the presence of the external auditor, the CEO and the CFO. The Supervisory Board is of the opinion that the financial statements meet all requirements for transparency and correctness. Therefore, the Supervisory Board recommends that the General Meeting of Shareholders to be held on 9 April 2018 adopt the financial statements and the appropriation of net income.

This Annual Report furthermore contains a limited assurance report of Deloitte Accountants B.V. on the defined Key Performance Indicators of Kendrion's Corporate Social Responsibility Programme 'Taking Responsibility'.

Profit appropriation

Kendrion realised net profit of EUR 19.5 million in 2017. Normalised net profit, which is profit before the one-off costs for the simplification programme, amounted to EUR 23.3 million.

The Supervisory Board approved the proposal of the Executive Board to pay out 50% of normalised net profit as dividend.

The members of the Supervisory Board have signed the financial statements to comply with their statutory obligation pursuant to article 2:101, paragraph 2, of the Dutch Civil Code.

In summary

Looking back, 2017 was a good year for Kendrion. It was a year of continued efforts to implement further simplification measures, with a view to establishing a simpler and more streamlined operation. The Supervisory Board appreciates the solid foundation of the current organisation, which provides a basis for the achievement of Kendrion's long-term targets in a sustainable manner. The Supervisory Board is confident about the fundamental strengths of Kendrion and the ability of the Executive Board – together with the Management Team – to make use of the opportunities in its markets.

Supervisory Board
Henk ten Hove, Chairman
Jabine van der Meijs
Marion Mestrom
Thomas Wünsche, Vice-Chairman

Zeist, 20 February 2018

J.A.J. van Beurden

F.J. Sonnemans

F.J. Sonnemans (56)

Position: Chief Financial Officer
Nationality: Dutch
Joined Kendrion: 15 February 2013
Appointment to current position: 15 April 2013
Reappointment to current position: 10 April 2017

J.A.J. van Beurden (57)

Position: Chief Executive Officer
Nationality: Dutch
Joined Kendrion: 1 December 2015
Appointment to current position: 1 December 2015
Additional positions: Non-Executive Director Antenna Company, member of the Supervisory Board of Adyen, member of the Supervisory Board of the Twente University

Industrial activities

INDUSTRIAL MAGNETIC SYSTEMS (IMS)
Development and production of customised solutions for switching, locking, holding and positioning based on electromagnetic technology.

INDUSTRIAL CONTROL SYSTEMS (ICS)
Development and assembly of gas and fluid control valves and systems and control technology.

INDUSTRIAL DRIVE SYSTEMS (IDS)
Development and manufacture of electromagnetic brakes and clutches.

WHERE OUR PRODUCTS ARE USED
Access control systems
Aircraft interiors
Elevator systems
Energy generation and distribution
Industrial appliances
Industrial automation / robotics
Industrial safety systems
Medical equipment
Textile machinery

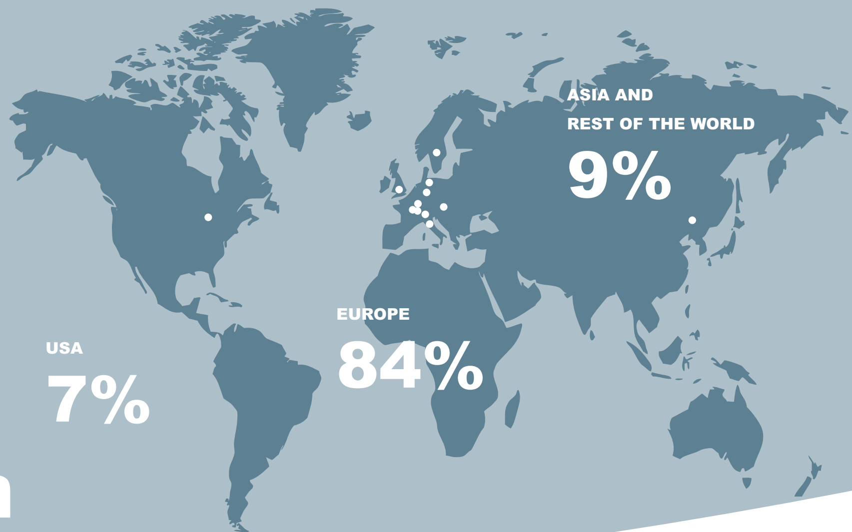
WHO WE DO IT FOR
Bosch Rexroth
Dräger
Eaton Corporation
Euchner
Fresenius
Oerlikon
PerkinElmer
Rockwell Collins
(previously B/E Aerospace)
Schindler
Siemens
Stoll

TOTAL MARKET SIZE
(IN EUR)
3 billion

ACCESSIBLE SIZE CHOSEN FOCUS MARKETS
(IN EUR) Market survey 2015
0.9 billion

TOTAL INDUSTRIAL REVENUE
(IN EUR)
162.5 million
2016 **152.3 million**

KENDRION LOCATIONS WITH REGIONAL REVENUE BREAKDOWN



Profile

The Industrial activities focus on developing and manufacturing electromagnetic systems and components for many industrial applications in markets such as industrial automation, energy generation and distribution, medical and analytical equipment, transportation and aerospace.

The activities are carried out in three business units: Industrial Magnetic Systems, Industrial Control Systems and Industrial Drive Systems. Industrial Magnetic Systems specialises in the development and production of customised solutions for switching, locking, rotating and positioning based on electromagnetic actuator technology. Industrial Control Systems focuses on the development and assembly of gas and fluid control valves and systems and control technology. Industrial Drive Systems specialises in the development and manufacture of electromagnetic brakes and clutches.

In Industrial, the main focus is on customer-specific systems and components for large and mid-size OEMs of industrial or professional equipment. The main differentiators are application expertise and engineering skills to design high-performance products. The production facilities specialise in low-volume and high-variety production. Besides the customer-specific systems and components, the industrial portfolio comprises standard and application-specific components.

The largest industrial production facilities are located in Germany, with further facilities in China, the USA and Romania. Products are marketed via an own sales organisation in Germany, the UK, Austria, Switzerland, Italy, France, Sweden, China and the USA. A worldwide sales distribution network is mainly dedicated to standard and application-specific components.

Market and market position

The total size of the market for electromagnetic systems and components in which the industrial business units operate is estimated to be EUR 3 billion, fragmented across many different end-markets. Approximately 30% of the end markets are in Europe, 30% in the USA and 40% in Asia and the rest of the world.

The Industrial focus areas are process automation and robotics, energy generation and distribution, medical and analytical equipment, industrial appliances, logistics (mail and parcel sorting), transportation, locking and safety and aerospace. These end markets have sufficient size and offer attractive opportunities in which Kendrion is able to deliver superior value and achieve above-average returns. Based on a market survey carried out in 2015, Kendrion estimates the accessible size of the chosen focus markets to be EUR 0.9 billion, with low to midrange single-digit growth over the coming years.

Kendrion competes in a market with many small and mid-sized producers, which often have a regional focus. The main market for the industrial activities continues to be Germany, with its advanced and globally leading mechanical engineering and automation industries. Other key markets are China, the USA, Switzerland, Austria, Italy, France and Sweden.

Customer concentration is relatively low. Siemens is the largest customer, representing just under 5% of total revenue. Other customers represent annual revenue of several million euros.

FRESH WATER FOR AIRCRAFT PASSENGERS

Product: Water valve for opening and closing the sensor-controlled faucet in aircraft lavatories.

Customer: Zodiac Cabin Controls, Hamburg.

Kendrion's solution: Valves in the freshwater systems of aircraft are exposed to contamination due to solid particles from tanks and pipes and on account of various types of disinfectants. Air needs to escape easily and allow the pipes to be refilled completely during frequent draining and filling of the system. The robust and non-corrosive switching valve includes an automatic bleeding function.

Added value: The valve's durability facilitates long service cycles and the automatic bleeding function allows the system to be put back into operation quickly and reliably after draining.

Developments in 2017

Revenue for the Industrial activities amounted to EUR 162.5 million (2016: EUR 152.3 million).

The Industrial activities recorded good revenue growth, with higher activity levels across all business units. Total revenue growth benefited from the favourable market conditions in the German machine building sector, largely driven by higher exports. Several successful product launches in all business units further contributed to revenue in 2017.

Industrial Magnetic Systems successfully further expanded its business with China and North America as its main growth areas. The closure of the Swiss operation was completed and production moved to Germany. The plant in Romania was further expanded, including the establishment of an own coil winding technology centre. The business unit serves customers on a local basis within Europe, Asia and North America. The sales organisation expanded with a new sales presence in France.

Industrial Control Systems saw increased revenue, driven mainly by higher power heat controller sales for synthetic textile machines to Oerlikon. The relocation of production from the Industrial plant in Germany to Sibiu, Romania, continued in 2017. Kendrion expects to further increase the use of the Romanian production facilities over the coming years.

Industrial Drive Systems enjoyed a strong year for electromagnetic Permanent Magnet brakes, driven in particular by the continually growing demand for automation in the robot and machine building industry. In China, a letter of intent was signed with a large customer for the investment in a permanent magnet brakes production line in the Chinese facility in Suzhou.

PASSENGER CARS (PC)

Development and production of advanced valve technology for common rail and gasoline valves, alternative drives and e-drives, active damping systems, engine management, hydraulic and pneumatic solenoids, stroke solenoids, sound actuators for internal and external sound applications and electrodynamic actuators and electronics.

COMMERCIAL VEHICLES (CV)

Development and production of electromagnetic clutches for front-engine cooling, angle gear box systems for rear engine cooling, clutches for switching auxiliary units, custom control flow valves and coils, vibration absorbers, pressure switches.

WHERE OUR PRODUCTS ARE USED

Active suspension systems
Belt damping systems
Engine management
Fuel systems
Human machine interface (HMI)
Hydraulics
Sound systems
Thermal management
Transmission

WHO WE DO IT FOR

Continental
Daimler Group
Delphi
Eaton Corporation
Fiat Chrysler
Great Wall Motors
Hyundai Kia
Standyne
ThyssenKrupp Bilstein
Volkswagen Group
Wabco
ZF Friedrichshafen

TOTAL MARKET SIZE

(IN EUR)

9 billion

ACCESSIBLE SIZE CHOSEN FOCUS MARKETS

(IN EUR) Market survey 2015

2 billion

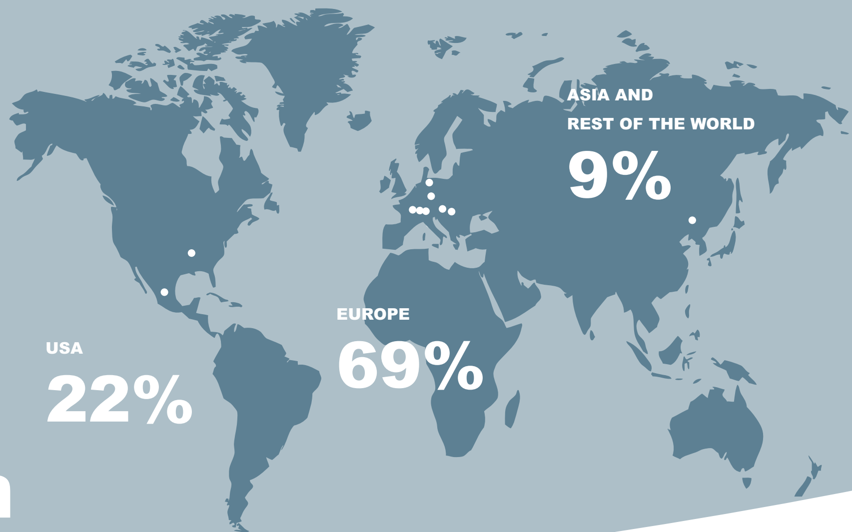
TOTAL AUTOMOTIVE REVENUE

(IN EUR)

299.3 million

2016 **EUR 291.1 million**

KENDRION LOCATIONS WITH REGIONAL REVENUE BREAKDOWN



Profile

Kendrion's automotive business develops, manufactures and markets innovative high-quality electromagnetic components, solutions and applications for customers in the automotive industry worldwide. Customers include major OEMs and Tier One suppliers in the global markets for passenger cars, light commercial vehicles, buses, heavy trucks, construction and agricultural vehicles and engines.

Kendrion is well known as a competent and trusted development and engineering partner with active project teams, in-depth technical knowledge and access to development, testing and production facilities, with an international network and facilities in Germany, Austria, Romania, the Czech Republic, the USA and China.

Products are generally developed and designed in accordance with the customer's specific needs, placing great emphasis on performance, quality and reliability. Kendrion is ISO/TS 16949-certified and supports environmentally friendly working methods in accordance with ISO 14001 and ISO 50001 for several plants.

The automotive operation is split into the business units Passenger Cars and Commercial Vehicles, reflecting different customer needs between these two segments. The business units have similar economic characteristics and display a number of similarities with respect to their technology, production processes, equipment and customers. Employees are largely interchangeable between both business units.

Passenger Cars provides innovative technological solutions, including advanced valve technology for common rail diesel and gasoline fuel systems, active damping systems, engine management, thermal management, sound actuators for internal and external sound applications, electrodynamic actuators for human machine interfaces and electronics. The highly reliable production processes are carried out partially in clean-room conditions and are entirely or partially automated depending on the annual production volume. Passenger Cars complies with stringent quality standards through the use of end-of-line control units for complete systems or individual functions.

Commercial Vehicles' main focus is on the technologies electromagnetic clutches, gear boxes, pressure switches, valves and solenoids. Application areas include compressor, fan and auxiliary drive clutches, thermal management and thermostat units, fluid control systems, and mobile hydraulics. The business unit Commercial Vehicles is evolving its product portfolio from the traditional diesel engine systems to modern hybrid and electrified power trains. New projects focus on auxiliary drive support in fully electrified and hybrid trucks.

Market and market position

The total size of the market for electromagnetic systems and components in which the automotive business units operate is estimated to be EUR 9 billion. Approximately 25% of the end markets are in Europe, 25% in the USA and 50% in Asia and the rest of the world.

Kendrion is focusing on a number of important global trends towards improved performance and efficiency of traditional combustion engines, alternative engines, hybrid drives, automation and the demand for safety and comfort. Kendrion, as a niche player in environmental, safety and comfort applications, is well positioned to capitalise on these trends.

Kendrion has selected a number of focus areas in core markets that have sufficient size, offer attractive growth potential in which Kendrion is able to deliver superior value and achieve above-average returns. Kendrion expects further growth due to new applications in suspension systems, thermal management, engine management, human machine interface, sound design systems and fuel systems that minimise emissions. New hybrid, electric and fuel cell cars are also creating new market opportunities.

Based on a market survey carried out in 2015, Kendrion estimates the accessible size of the chosen focus markets to be EUR 2 billion and to be growing on average by 4% per annum.

Kendrion's largest automotive market remains Europe, and within that market, Germany. Passenger Cars' position outside Europe further improved with several new projects won for thermal management applications, transmission systems and exterior sound design systems for electric vehicles in China. Commercial Vehicles operates globally with a strong footprint in North America, Europe and Asia, especially in China and Korea.

Developments in 2017

Revenue for the automotive activities amounted to EUR 299.3 million in 2017 (2016: EUR 291.1 million).

In 2017, Passenger Cars further strengthened its position with new serial business obtained in fuel systems, thermal management, sound systems, electronics and active damping. New product developments for alternative drive systems such as hybrid and electric cars and thermal management applications were acquired as well.

In China, the business unit benefited from intensified sales activities at local OEMs for fuel systems, engine management and sound system applications and realised double-digit growth. To accommodate the strong growth in China as well as the promising project pipeline, Kendrion decided to move to a larger manufacturing facility in the city of Suzhou. The move is expected to be finalised in the first quarter of 2018. In the USA, the focus has been on improving the efficiency and profitability of the existing product lines and on preparing for serial production of the next generation of gasoline valves, which is expected to launch in 2018. The newly established sales team in Detroit has been delivering its first successes.

Passenger Cars' development focus in 2017 was on fuel efficiency and emission reduction with several applications in engine and thermal management, interior and exterior sound design as well as in new active damping system projects. Kendrion's sound design systems enjoyed ongoing strong interest from customers around the world, also driven by new legal requirements for hybrid and electric cars stipulating that these vehicles must emit an external sound at low speeds.

After a challenging 2016, Commercial Vehicles continued with a major change programme in 2017 in order to improve operational efficiency, scale, customer service and streamline the product portfolio. Small-scale production sites such as those in Brazil, India and Mexico have been closed, or are scheduled to be closed, as part of this programme.

In 2017, the revenue decline experienced by Commercial Vehicles in 2016 stabilised, with especially strong demand for solenoids for mobile hydraulics, produced in the Czech plant, offsetting the revenue impact from the closure of the facilities in India and Brazil. The US heavy truck market stabilised in 2017 and is showing signs of recovery.

Commercial Vehicles is gradually shifting from fragmented custom solutions and projects to more standardised products allowing a higher level of productivity. With these changes, the business unit Commercial Vehicles is well positioned today in the markets for specialised electromagnetic clutches, fluid control valves, pressure switches and solenoids for mobile hydraulics.

Innovation

One of Kendrion's key strengths is its capacity for innovation. Innovation is at the heart of the many new products Kendrion is developing, in many cases in close cooperation with its customers. As outlined in Kendrion's strategic update released on 3 May 2016, Kendrion is keen to position itself at the forefront of a series of important megatrends that provide substantial opportunities for growth in the coming years.

Fuel efficiency

The first area is driven by the desire for automotive companies to improve the performance and efficiency of traditional combustion engines. With respect to this trend, Kendrion sees its products helping fuel efficiency and engine management systems being fundamental as both help reduce emissions.

Alternative drives

The second area is alternative drives. Products for thermal management, fuel cells and e-drives with zero emissions. Its technology in fuel cell valves is equally important to this rapidly evolving market.

Safety and comfort

The third area is safety and comfort in which Kendrion sees its longstanding skills in suspension systems, seating comfort, parking locks and sound systems as being highly relevant.

Automotive activities

Industrial activities

Industrial applications

There is a trend towards increased automation in industrial applications, for example robotics in factory production lines. Kendrion's expertise in drive and conveyor systems is an important differentiator in relation to this trend.

Urbanisation

As more and more people move to urban areas, energy generation and power distribution become ever more complex, which in turn drives demand for Kendrion's power switches and best-in-class circuit breakers. More high-rise buildings will create added demand for Kendrion's skills in elevator systems.

Safety and security

Safety and security remain critical areas for the industrial market. This creates opportunities for Kendrion's control technology and door locking solutions.

Normalised financial results

EUR million	2017	2016
Reported result before net finance costs	28.7	21.7
Reported amortisation	3.2	3.7
Reported operating result before amortisation (EBITA)	**31.9**	**25.4**
One-off costs related to simplifying measures in raw materials	0.2	0.6
One-off costs related to simplifying measures in staff costs	3.2	3.4
One-off costs related to simplifying measures in other operating expenses	1.7	1.7
Normalised EBITA	**37.0**	**31.1**
Reported amortisation	(3.2)	(3.7)
Reported net finance costs	(2.9)	(3.1)
Impact simplifying measures on net finance expense	0.0	0.4
Normalised profit before income tax	**30.9**	**24.7**
Reported income tax expense	(6.3)	(3.7)
Impact one-off costs on income tax expense	(1.3)	(1.4)
Normalised profit for the period	**23.3**	**19.6**

Financial results

EUR million	2017 Normalised	2016 Normalised	2017 Reported	2016 Reported
Revenue	461.8	443.4	461.8	443.4
Operating result before amortisation (EBITA)	37.0	31.1	31.9	25.4
Return on sales (ROS)	8.0%	7.0%	6.9%	5.7%
Net profit	23.3	19.6	19.5	14.9
Net return as %	5.1%	4.4%	4.2%	3.4%
EBITA return on investments (ROI)	14.5%	12.4%	12.7%	10.2%

Normalisation impact

On 3 May 2016, Kendrion announced its updated strategy 'Simplify, Focus, Grow', which included a simplifying programme that is taking place over the period 2016 – 2018. The one-off costs of the programme are significant and have been excluded from the results in order to better show the underlying profit development. In prior years Kendrion also presented normalised (recurring) results in the annual report when the results were significantly impacted by non-recurring events, for example due to acquisitions. The one-off costs for the simplifying measures initiated in 2017 amount to EUR 5.1 million (2016: EUR 5.7 million), with corresponding savings on an annualised basis of EUR 5.0 million (2016: EUR 7.0 million). After tax, the one-off costs amount to EUR 3.8 million (2016: EUR 4.7 million). Further simplifying measures are expected to be implemented during 2018.

Financial results

Kendrion continued its good performance of 2016 in 2017. Revenue increased by 5%, based on constant exchange rates, and profitability improved significantly as the company's simplifying measures took effect combined with favourable market conditions. This resulted in a 19% increase in the normalised operating result before amortisation (EBITA) to EUR 37.0 million (2016: EUR 31.1 million). Normalised net profit improved to EUR 23.3 million (2016: EUR 19.6 million).

The normalised operating result before amortisation (EBITA) as a percentage of revenue increased to 8.0% (2016: 7.0%), driven mainly by the company's simplifying measures and revenue growth.

Revenue

In 2017, revenue increased by 4.2% from EUR 443.4 million to EUR 461.8 million. At constant rates of exchange, revenue growth was 4.6%.

The Industrial activities achieved organic growth of 7.3%, at constant rates of exchange, on the back of favourable market conditions and high demand for permanent magnet brakes. The Automotive activities achieved organic growth of 3.2% at constant rates of exchange. The organic growth of Passenger Cars, with a good contribution from the further ramp-up of its active damping project in Austria, was partly offset by a slight reduction in revenue in Commercial Vehicles, fully due to the closure of Kendrion's plants in India and Brazil.

Developments per segment

Industrial

Industrial – which accounts for 35% of Kendrion's total revenue – reported revenue of EUR 163 million, which is an increase of 7% compared to last year. The normalised operating result before amortisation increased to EUR 16.9 million, compared to EUR 11.6 million in 2016. This resulted in a normalised EBITA margin of 10.4% (2016: 7.6%). All business units contributed to the strong growth in revenue and profitability.

Strong demand from industrial customers, mostly in Germany and China, and the successful launch of new projects resulted in a revenue increase of 7%. Favourable market conditions in the main industrial markets further contributed to growth.

Together with the simplifying measures implemented in 2016 and 2017, this significantly improved profitability compared to last year.

Industrial Magnetic Systems had a strong year, resulting in an increase of 5% in total revenue. Industrial Magnetic Systems also successfully moved its activities in Switzerland to Germany. Market conditions in Germany, China and the USA were good throughout the year. Industrial Magnetic Systems will continue to relocate certain production lines to the plant in Sibiu, Romania. This is expected to further improve cost efficiency.

Industrial Control Systems also had a strong year, with a revenue increase of 6%. The revenue increase was driven mainly by the renewed deliveries of power heat controllers for a new synthetic textile machine and, in general, higher demand from industrial customers. The business unit was again successful in significantly reducing costs in Germany, which, in combination with the aforementioned revenue increase, resulted in improved profitability. The simplifying measures taken in 2017 are expected to further improve profitability in 2018. Industrial Control Systems is continuing to relocate production activities to its plant in Sibiu, Romania, which will help to lower the cost base of the business unit.

Industrial Drive Systems had a strong year, with organic growth of more than 8%. The business unit benefited from high demand for its permanent magnet brakes and from several new orders, which more than offsets the impact of the end-of-life of a high-volume customer project in Germany in 2017 and 2018. As a result of the revenue growth and simplifying measures taken by the business unit, profitability improved compared to 2016.

Overall, Industrial benefited from a favourable German machine-building market, while improving its profitability as a result of the simplifying measures. The measures taken in 2017 and simplifying measures scheduled for 2018 are expected to have a further positive impact on profitability in future years.

Automotive

Automotive – which accounts for 65% of Kendrion's total revenue – realised revenue of EUR 299 million, which is an increase of 3% at constant rates of exchange compared to last year. The normalised operating result before amortisation increased to EUR 20.8 million, compared to EUR 19.9 million in 2016. This resulted in a normalised EBITA margin of 6.9% (2016: 6.8%).

The general market conditions for Automotive were positive, including the heavy truck market in the USA, which improved in the second half of 2017.

The results of Kendrion's Automotive activities were mixed.

Passenger Cars reported organic growth of 5% compared to last year. This growth was mainly attributable to the further ramp-up of the production of solenoid valves for active damping systems in Austria. This is expected to further support revenue development going forward. New projects in the area of sound-design technology have significant potential for future growth. Despite the revenue growth, profitability of the Passenger Cars business unit was below expectation. Additional simplifying measures to address this were taken in the fourth quarter of 2017. Further simplifying measures are scheduled for 2018.

SPECIAL THERMAL CONTROL SYSTEM FOR TEMPERATURE MANAGEMENT

Product: Thermal control system for temperature management of engines and auxiliary units.

Customer: OEMs and manufacturers of combustion engines for commercial vehicles.

Kendrion's solution: The Thermal control system works without a wax thermostat, which is the conventional solution. Kendrion's solution offers reduced temperature deviations compared to wax or other traditional solutions. Ultimately this reduces fuel consumption. The special thermal control system is a unique, innovative solution that increases the engine's efficiency.

Added value: The thermal control system reduces emissions and the consumption of AdBlue (AdBlue is used to lower NOx concentration in the emissions from diesel engines). It also lowers the loads on several engine components due to reduced thermal stress.

Commercial Vehicles had a good year, despite a revenue decline of 1% compared to last year. When adjusting for the impact of the closures in India and Brazil, underlying revenue grew with 6% compared to last year.

The underlying revenue increase is driven by high demand for hydraulic solenoids as a result of good market conditions for agricultural machines. The production facility in the Czech Republic performed particularly well, growing its revenue and profitability. Production facilities in Germany and the USA achieved stable revenues and improved profitability. In the fourth quarter of 2017, Kendrion decided to close its manufacturing facility in Mexico, and move most production to the Shelby facility in the USA. The business unit closed its production plant in India during the second quarter of 2017 as scheduled.

The improvement in the normalised operating result before amortisation of Automotive to EUR 20.8 million (2016: EUR 19.9 million) was driven largely by the simplifying measures taken in Commercial Vehicles. The additional simplifying measures taken in the fourth quarter of 2017 and the additional measures scheduled for 2018 are expected to have a further positive impact on profitability in future years for Passenger Cars in particular.

The main future growth markets for Automotive are suspension (damper) systems, driver assistance systems, valve and camshaft adjustments, fuel systems, thermal management, sound systems and potentially hydrogen valves. The automotive market is currently going through unprecedented disruption in the areas of electrification, hybridisation, autonomous driving, safety and comfort. This creates both uncertainty and opportunities. The current project portfolio, together with the many exciting changes in the market and the simplification actions taken in 2017 create opportunities for significant top and bottom line growth for Automotive in the coming years.

Added value

In 2017, normalised added value amounted to EUR 220.9 million, which is an increase of 3.4% compared to last year (2016: EUR 213.5 million). Added value as a percentage of revenue remained stable compared to last year at 48%.

Pre-agreed annual discounts, which are customary for automotive projects, are usually compensated for by purchase discounts and by new projects that are ramping up.

Staff costs and other operating expenses

Normalised staff costs, including costs for temporary employees, amounted to EUR 131.0 million, compared to EUR 129.2 million in 2016.

The increased staff costs were mainly the result of increased production and the yearly increase in annual salaries (mostly related to the tariff increase in Germany), largely offset by the simplifying measures taken in 2016 and 2017. Consequently, total staff costs as a percentage of revenue decreased by 0.7% compared to last year.

Staff costs in relation to revenue and added value evolved as follows:

Staff costs	2017	2016	2015
Staff costs (in EUR million)	131.0	129.2	133.1
As % of revenue	28.4%	29.1%	30.1%
As % of added value	59.3%	60.5%	62.2%

FTE (at 31 December)	2017	2016	2015
Direct staff	1,355	1,320	1,360
Indirect staff	1,150	1,180	1,213
Temporary employees	140	78	85
Total number of FTE	**2,645**	**2,578**	**2,658**

Normalised other operating expenses for 2017 amounted to EUR 32.6 million (2016: EUR 32.9 million). The slight decrease compared to last year, despite the increased production in 2017, is mainly the result of the simplifying measures taken in 2016 and 2017. As a result, the overall ratio of operating expenses as a percentage of revenue decreased to 7.1% (2016: 7.4%).

Other operating expenses in relation to revenue and added value evolved as follows:

Other operating expenses	2017	2016	2015
Other operating expenses (EUR million)	32.6	32.9	35.7
% of revenue	7.1%	7.4%	8.1%
% of added value	14.7%	15.4%	16.7%

Total Research & Development expenses (including staff and other operating expenses) for 2017 totalled EUR 28.3 million (2016: EUR 27.6 million).

Net financing costs

Normalised net financing costs increased to EUR 2.9 million (2016: EUR 2.7 million), as a result of unfavourable currency exchange results of EUR 0.6 million (2016: negative EUR 0.1 million). Excluding currency results, financing costs decreased by EUR 0.3 million compared to 2016 mainly due to the continued reduction in average debt levels.

Average (gross) debt levels, before deduction of cash and deposits, amounted to EUR 70 million in 2017 (2016: EUR 84 million). The average interest charge on borrowings in 2017 was 1.9% (2016: 2.0%).

More information on the revolving credit facility, available credit lines and conditions can be found on pages 116-118 of the financial statements.

Income tax

The normalised income tax expense in 2017 amounted to EUR 7.6 million (2016 normalised: EUR 5.1 million). The normalised effective income tax rate for 2017 was 25% (2016: 21%).

The higher effective tax rate in 2017 was mainly due to the country mix, with a higher relative portion of the taxable profit in the USA in particular, which has a relatively high corporate income tax rate. More information on the effective tax rate can be found on page 135 of the financial statements.

Normalised tax paid in 2017 amounted to EUR 4.2 million. The difference between tax paid and normalised effective tax expense is largely due to the realisation of deferred tax assets relating to loss carry-forwards during 2017.

Net income

Normalised net income attributable to equity holders of the company (EUR million)	23.3
Normalised earnings per share (EPS) (EUR)	1.73

Kendrion proposes an optional dividend of 50% of the normalised net result (2016: 53%), equivalent to EUR 0.87 per share entitled to dividend.

Financial position and working capital

Total assets decreased to EUR 344.8 million (2016: EUR 347.1 million). Trade and other receivables increased by EUR 3.4 million, inventories by EUR 4.7 million and Trade and other payables by EUR 4.2 million, mainly as a result of higher production and sales compared to 2016. Cash and cash equivalents decreased by EUR 4.8 million. This was mainly caused by a decrease of the cash position in China as a result of a dividend payment. The received dividend was transferred to the company's EUR cash pool.

Net working capital at 31 December

EUR million	2017	2016
Inventories	57.3	52.6
Trade and other receivables, tax receivable	59.1	55.7
Less: Trade and other payables, tax payables, current provisions	74.5	70.3
Net working capital	**41.9**	**38.0**
As % of revenue	9.1%	8.6%

Working capital

Net working capital as a percentage of revenue increased slightly compared to the previous year to 9.1% of revenue (2016: 8.6%). Excluding the effect of the provisions and payables related to the simplifying measures, normalised net working capital amounted to 9.9% of revenue (2016: 9.3%). Receivables, inventory and payables all increased as a result of the higher production and sales compared to 2016. The year-end provision for trade receivables amounted to EUR 0.3 million (2016: EUR 0.1 million).

Condensed consolidated statement of financial position

Assets

EUR million	2017	2016
Property, plant and equipment	90.4	85.5
Intangible assets		
■ Goodwill	90.9	94.3
■ Acquisition related	15.7	19.7
■ Software	8.6	8.9
■ Development costs	2.7	1.6
Other	0.2	0.4
Deferred income tax	12.3	16.0
Non-current assets	**220.8**	**226.4**
Inventories	57.3	52.6
Income tax	1.0	1.2
Trade and other receivables	58.1	54.5
Cash	7.6	12.4
Current assets	**124.0**	**120.7**
Balance sheet total	**344.8**	**347.1**

Intangible assets

Goodwill payments were made for the Linnig Group in 2007, Kendrion (Mishawaka) LLC in 2008, Kendrion (Aerzen) GmbH in 2010, Kendrion (Shelby) Inc. at the end of 2011, and Kendrion Kuhnke Automation and Kendrion Kuhnke Automotive in 2013.

Acquisition related intangible assets consisted largely of the calculated fair value of customer relations and technology. The annual amortisation charge relating to these intangibles amounted to EUR 3.2 million in 2017 (2016: EUR 3.7 million). More information can be found on pages 106-109 and following.

Detailed information regarding the deferred tax positions can be found on pages 110-112 of the financial statements.

Solvency ratio

The year-end solvency ratio increased to 52.3% (year-end 2016: 51.3%), mainly due to the higher net profit.

Net debt

Net debt increased by EUR 0.5 million during 2017 to EUR 54.5 million. Normalised free cash flow, before payments related to the simplifying measures, amounted to EUR 14.2 million in 2017. The free cash flow was more than offset by the cash portion of the optional dividend which amounted to EUR 6.6 million (approximately 65% of total dividend), EUR 4.5 million resulting from the share buy-back programme and the one-off payments related to the simplifying measures.

Net interest-bearing debt at 31 December

EUR million	2017	2016
Non-current borrowings	46.7	59.3
Non-current mortgage loan	3.0	3.7
Current borrowings	12.4	3.4
Less: Cash and cash equivalents	7.6	12.4
Net bank debt at 31 December	**54.5**	**54.0**
EBITDA (normalised)	57.3	51.4
Debt cover	0.95	1.05

Invested capital at 31 December

EUR million	2017	2016
Balance sheet total	344.8	347.1
Less: non-interest bearing debt	74.5	70.3
Less: freely available cash	7.6	12.4
Less: deferred income tax	12.3	16.0
Invested capital	**250.4**	**248.4**

The future activities will be financed via Kendrion's current revolving credit facility (EUR 150.0 million) with a syndicate of three banks and via free cash flow of the Group. Further information is provided in note 10 to the financial statements. The current financing structure will be re-evaluated during 2018.

Free cash flow

In 2017, the normalised free cash flow, before payments related to the simplifying measures, of EUR 14.2 million was below last year (2016: EUR 22.3 million), despite the higher normalised net profit of EUR 23.3 million (2016: EUR 19.6 million). The main reasons for the lower free cash flow compared to normalised net profit were the increase in working capital of EUR 4.3 million and the investments exceeding depreciation by EUR 8.0 million, partly offset by the EUR 3.2 million non-cash amortisation charges on the intangibles arising from acquisitions.

Net investments in property, plant and equipment and software amounted to EUR 28.3 million. Capital expenditure on plant and equipment relates mostly to investments in production lines for new projects.

Normalised free cash flow

EUR million	2017	2016
Reported free cash flow	11.0	21.3
Non-recurring restructuring costs net of tax paid	3.2	1.0
Normalised free cash flow	**14.2**	**22.3**

HIGH-PRECISION CO_2 PRESSURE REGULATOR FOR ENDOSCOPE INSUFFLATORS

Product: Special regulator that allows minimally invasive surgery by inflating the patient's abdominal cavity with carbon dioxide (CO_2). This facilitates the surgical procedure and significantly reduces post-operative complaints.

Customer: A leading endoscope manufacturer.

Kendrion's solution: The precision pressure regulator combines all the manufacturer's requirements in a single special unit qualified for medical use. The pressure regulator is easily integrated into the customer's medical device due to its compact dimensions and range of mounting options.

Added value: State-of-the-art level of hygiene, biocompatibility, high-precision operating pressure, superior reliability and long-term stability.

Contingent liabilities

Information about contingent liabilities is provided on page 131 of the notes to the financial statements.

Management statement

The Executive Board is responsible for the preparation of the financial statements and the annual report in accordance with Dutch law and International Financing Reporting Standards as adopted by the EU (EU-IFRS). As prescribed in article 5:25c of the Financial Supervision Act *(Wet op het Financieel Toezicht)*, and with due regard for the above, the Executive Board declares that to its knowledge (i) the financial statements give a true and fair view of the assets, liabilities, financial position and profit of Kendrion N.V. and the companies jointly included in the consolidation; (ii) the report of the Executive Board gives a true and fair view of the situation at the balance sheet date, the situation during the financial year at Kendrion N.V. and the companies affiliated with Kendrion, whose figures are incorporated in the financial statements, and (iii) that the report of the Executive Board describes the significant risks which Kendrion faces.

The members of the Executive Board have signed the financial statements to comply with their statutory obligation pursuant to article 2:101, paragraph 2 of the Dutch Civil Code and article 5:25c of the Financial Supervision Act.

Introduction

Corporate Social Responsibility (CSR) is an integral part of Kendrion's Simplify, Focus, Grow strategy. Kendrion's vision on CSR is to conduct business ethically in an environmentally and socially conscious and responsible manner while implementing and executing its growth strategy in a profitable way in line with the reasonable expectations of Kendrion's stakeholders. To encourage this vision, financial and non-financial targets are integrated in Kendrion's strategy and Kendrion's business processes.

Kendrion acknowledges the increasing interest among its stakeholders relating to transparent disclosures about Kendrion's sustainable business practices. Partly with a view to addressing this increasing interest of stakeholders, Kendrion's 2017 Integrated Report highlights how Kendrion aims to create long-term value, both financial and non-financial.

CSR strategy 2015 – 2017

Kendrion is committed to taking responsibility for the impact of its decisions and activities as a company, not only in terms of their effects on its stakeholders, but also of those on the environment and society. To this end, Kendrion's CSR strategy 2015 – 2017 entitled 'Taking Responsibility' is aimed at the consistent integration of sustainable practices within Kendrion's business processes and aligned with Kendrion's growth targets. The CSR strategy is supported by a clear set of non-financial targets.

The CSR strategy 2015 – 2017, its material topics and targets have been designed in a structural dialogue with Kendrion's stakeholders.

The Executive Board and the Management Team are committed to undertaking an effort to achieve the non-financial targets underlying the CSR strategy 2015 – 2017. Having due regard to the decentralised set-up of the Kendrion organisation, each business unit is required to design and implement a CSR strategy tailored to the specifics of its business processes.

Part of the variable remuneration of the Executive Board, the Management Team and senior management is conditional upon the achievement of non-financial targets in the area of sustainability.

The Supervisory Board supports Kendrion's CSR strategy and supervises the manner in which the Executive Board and the Management Team implement the CSR strategy. Reference is made to the Report of the Supervisory Board on pages 21-26 for more information about the activities of the Supervisory Board in 2017.

CSR embedded in the Kendrion organisation

Under the supervision of the Supervisory Board, the Executive Board develops the CSR strategy and sets overall CSR objectives and targets and monitors progress on the achievement of these objectives and targets, in consultation with the Management Team. In addition, Kendrion has established a CSR Board that contributes to the execution and implementation of the CSR strategy. Moreover, the CSR Board provides general support to the Executive Board and the Management Team regarding relevant developments and sustainability issues and progress on the achievement of the targets and objectives underlying the CSR strategy. The CSR Board consists of Kendrion employees and includes representatives from different regions and from various business units and departments. Designated CSR ambassadors throughout the Kendrion organisation support CSR activities locally.

Collection and validation of data

The information contained in this 2017 Integrated Report relates to all operating companies of Kendrion. To safeguard the quality and accuracy of data collected internally, Kendrion follows a solid reporting process which has been recorded in a CSR reporting manual. The CSR reporting manual is regularly updated to ensure alignment with relevant developments and to encourage continuous improvement. In addition, information is collected and validated through meetings with members of the Management Team and other internal and external stakeholders.

The selected Key Performance Indicators defined in Kendrion's CSR strategy are subject to a limited assurance review by Deloitte Accountants B.V.

UN Global Compact and OECD Guidelines for Multinational Enterprises

In 2009, Kendrion joined the United Nations Global Compact. The United Nations Global Compact is an international network of businesses and stakeholders that support the Ten Universal Principles of the United Nations Global Compact. The Ten Universal Principles focus on four main areas: human rights, labour and labour standards, environment and anti-corruption.

The Organisation for Economic Co-operation and Development (OECD) promotes policies that are aimed at improving the economic wellbeing of people. The Guidelines for Multinational Enterprises issued by the OECD provide for principles and standards relevant to responsible business conduct.

Kendrion contributes to sustainable development by endorsing the Ten Universal Principles and the OECD

HIGHEST SAFETY FOR ELEVATORS

Product: High-tech safety brakes.

Customer: Global manufacturers of elevator systems.

Kendrion's solution: The solution offers redundant brake circuits. Each circuit must be in a position to stop and hold the elevator load within split seconds. Other requirements, such as gentle stopping to improve passenger comfort, are upheld.

Added value: While conforming to the stringent safety regulations, the solution provides a simplified assembly process.

Guidelines for Multinational Enterprises. The four main areas as included in the Ten Universal Principles and the OECD Guidelines for Multinational Enterprises form the basis of Kendrion's Global Legal Compliance and Governance Framework.

Reference is made to the section 'Risks and risk management' on pages 58-66 and to the paragraph 'Responsible business conduct' on pages 49 and 50 for more information about Kendrion's Global Legal Compliance and Governance Framework.

Global Reporting Initiative GRI G4

Kendrion applies the guidelines of the Global Reporting Initiative (GRI) G4 'core level', the global best practice used for sustainability reporting. The 'GRI Index' containing page references to the relevant GRI components can be found on pages 164-167.

Dutch Transparency benchmark

Kendrion participates in the Transparency benchmark, an assessment by the Dutch Ministry of Economic Affairs of the content and quality of CSR reports of Dutch companies. Kendrion consistently improved its ranking during the last five years, and was most recently ranked number 37 (2016: number 60).

Stakeholder dialogue

Kendrion values its relationships with its stakeholders and engages with important stakeholders on CSR strategy, activities and underlying objectives. The exchange of best practices and experiences and making active use of its networks add to Kendrion's CSR activities in a constructive manner. Kendrion's stakeholders include customers, suppliers, employees, investors, the local communities in which Kendrion is active and other relevant parties such as technical universities, schools and institutes. Kendrion's stakeholders also consider the importance of sustainable business practices that are supported by concrete targets. With its own CSR strategy, Kendrion also intends to contribute to the achievement of the respective CSR targets of its stakeholders.

Customers
A substantial number of Kendrion's customers are major tier 1 suppliers and OEMs in the automotive sector, or other large industrial companies. Increasingly these customers have implemented CSR and sustainability requirements for suppliers. Kendrion focuses on consistent compliance with their requirements, including quality and environmental requirements.

Suppliers
Kendrion expects its suppliers to adhere to the standards of the Kendrion Supplier Code of Conduct. A substantial number of Kendrion's suppliers have signed the Supplier Code of Conduct in recent years, and Kendrion follows a consistent approach towards the performance of CSR audits at its suppliers. These efforts contribute to the further improvement of Kendrion's supply chain.

Employees
Kendrion's employees are the company's most valuable resource. Kendrion undertakes efforts to create the right culture and conditions to attract and retain the right people with the right capabilities. The opportunities Kendrion offers for career development and personal growth in a safe and attractive working environment are an important motivational factor for employees. An engaged and committed workforce contributes to the achievement of Kendrion's overall business goals, including CSR-related goals and ambitions.

Reference is made to the section 'Human Resources' on pages 54-57 for further information about Kendrion's approach towards 'talent management and recruitment', 'training and development' and other relevant topics.

Investors

Investors commonly acknowledge that the companies they invest in have an impact on the environment and society. The endorsement of sustainable development and addressing environmental, social and governance (ESG) related matters is becoming increasingly important for Kendrion's investors. Kendrion engages with its major shareholders and banks, not only concerning Kendrion's CSR strategy, its material topics and objectives, but also about the ESG policies and activities of its major shareholders and banks.

Local communities

Through its local community investment programme 'Together@Kendrion', Kendrion is committed to making a positive contribution to the reduction of social and economic gaps, specifically in the jurisdictions where Kendrion conducts its business activities.

Kendrion appreciates the importance of maintaining constructive and appropriate contacts with local authorities.

Technical universities, schools and institutes

With its CSR strategy, Kendrion also expresses to contribute to a better and sustainable standard of living for future generations. Active engagement with students is key to understanding their views and observations on CSR and forms a valuable platform for the exchange of knowledge and experiences. Dialogues with students are often inspirational and stimulate the formulation of innovative CSR-related goals and ambitions. These dialogues also raise awareness among students about sustainability and its importance.

Kendrion maintains contacts with technical universities, schools and other relevant institutes by attending fairs, organising student events, projects and workshops and offering internships. Student events were organised in 2017 that focused exclusively on CSR and exchanging knowledge and experiences relating to CSR.

The overview on the next page generally describes the communication resources and channels per stakeholder and their relevance to Kendrion's CSR strategy.

Overview of stakeholder dialogues

Stakeholder	Communication resources and channels	Topics discussed	Relevance to Kendrion's CSR policy
General			Enhancing transparency and interaction with Kendrion stakeholders
Customers	Customer and sales meetings, Kendrion websites, contract meetings, press releases	Quality of products and services, Kendrion's CSR strategy and CSR objectives, customer satisfaction, waste, energy, water use, use of rare earth materials, conflict minerals, responsible business conduct, ISO certification	Obtain views and observations concerning CSR from customer perspective, further insight into customer needs and expectations, also concerning CSR related matters, sharing experiences and best practices, continuous improvement and development of CSR contributions by Kendrion and its customers
Suppliers	Supplier Code of Conduct, supplier implementation audits, Kendrion websites, supplier and contract meetings	Quality of products and services, Kendrion's CSR strategy and CSR objectives, supply chain management and joint pursuit of improvements in the supply chain, responsible business conduct, Supplier Code of Conduct, waste, energy, water use, use of rare earth materials, conflict minerals	Obtain views and observations concerning CSR from supplier perspective, further insight into supplier needs and expectations, also concerning CSR related matters, sharing experiences and best practices, continuous improvement and development of CSR contributions by Kendrion and its suppliers
Employees	Works Council meetings/meetings with employee representatives, employee satisfaction and culture surveys, workshops, training courses, internal personnel magazine, e-mail newsletters, feedback meetings, staff meetings	Kendrion's CSR strategy and CSR objectives, particularly regarding health and safety, employability, training and development, employee satisfaction and company culture, responsible business conduct, Global Legal Compliance and Governance Framework	Obtain views and observations concerning CSR from employee perspective, further insight into employees' capabilities and motivations, strengthening business sustainability culture, enhancing employee participation and awareness
Investors	General Meeting of Shareholders, analysts- and investors meetings, press releases, Kendrion website	Kendrion's CSR strategy and CSR objectives	Obtain views and observations concerning CSR from investor perspective, further insight into investor needs and expectations, sharing experiences and best practices, continuous improvement and development of CSR contributions by Kendrion and investors
Local communities	Local meetings, Kendrion websites, open days	Communities participations and investments	Community connection, involvement and participation
Technical universities, schools and institutes	Presence at fairs, organisation of student events, projects and internships	Kendrion's CSR strategy and CSR objectives, also with a view to creating awareness and stressing the importance and relevance of CSR	Obtain views and observations concerning CSR of new generation and raise awareness

Supply chain management

TARGET 2017	RESULT 2017
100% of top 30 of suppliers signed Supplier Code of Conduct	100%
At least 3 CSR supplier audits per plant with more than 80 employees and at least 1 CSR supplier audit per each other plant	95%

Business ethics and compliance

TARGET 2017	RESULT 2017
Effective Global Legal Compliance and Governance Framework in each plant	80%

Sustainable operations

TARGET 2017	RESULT 2017
Waste data plan and subtargets implemented in major plants	80%
CSR is part of all important business processes	100%

Our People

TARGET 2017	RESULT 2017
Staff satisfaction survey introduced in all plants (except for small locations)	100%
Overall satisfaction survey score of at least 75%	100%
Effective diversity policy implemented	100%

Energy & CO_2 reduction

TARGET 2017	RESULT 2017
25% reduction of relative CO_2 emission compared to 2014	100%
25% reduction of relative energy consumption compared to 2014	70%

Health & safety

TARGET 2017	RESULT 2017
≤10 accidents per 1,000 FTE	100%
Illness rate on comparable level and not above 4% in each plant	90%

See for reporting periods, definitions, scope and external assurance pages 162 and 163 of this report.

Achievements – CSR strategy 2015 – 2017
A description of the most important achievements under the Taking Responsibility programme during the period 2015 – 2017 is set out below.

Supply chain management

Kendrion operates as part of a supply chain with a central focus on manufacturing and production processes and customers. Kendrion and other parties forming part of the supply chain are collectively responsible for maintaining the quality and sustainability of the products in the supply chain. All parties forming part of the supply chain play a role in addressing major issues that affect the supply chain as a whole.

The supply chains in which Kendrion is active have an impact on people, the environment and society that cannot be specified in unequivocal terms. Kendrion's manufacturing and production processes are not polluting, in the sense that they do not result in large quantities of residual products that have a major impact on the environment and that cannot be recycled. Nor do they result in substantial emissions of substances with an environmental impact. Many of Kendrion's products enable the company's customers to reduce the environmental impact of their products, for example in terms of emissions and energy consumption.

Kendrion intends to play a meaningful role in the chain in which the company is active. In many instances, Kendrion is a relatively minor link in the supply chain. As a result, Kendrion's sphere of influence is limited. In order to achieve realistic results, it is of great importance that Kendrion continues the dialogue with its suppliers and, in the selection and assessment of suppliers, continues to consider their performance as regards sustainability.

Kendrion does not add any conflict minerals from the Congo region to its products during its own production process.

Permanent magnets are used in some of Kendrion's products. A category of permanent magnets contains a number of rare earth metals. Mining and refining rare earth metals is highly energy-intensive. The use of permanent magnets in products increases their functionality, such as the torque. As a result, less material is required and the product is lighter, which in turn reduces energy consumption and emissions. Mining and refining rare earth materials are both difficult and energy-intensive activities. The related mining and refining by-products that cause environmental pollution often pose a further complication. While there is a need for alternative sources of energy, such as wind turbines and electric cars, they actually exacerbate the shortage of rare earth metals and the environmental pollution caused by their extraction. The volumes of the permanent magnets used by Kendrion are comparatively limited but Kendrion cannot avoid the use of permanent magnets altogether.

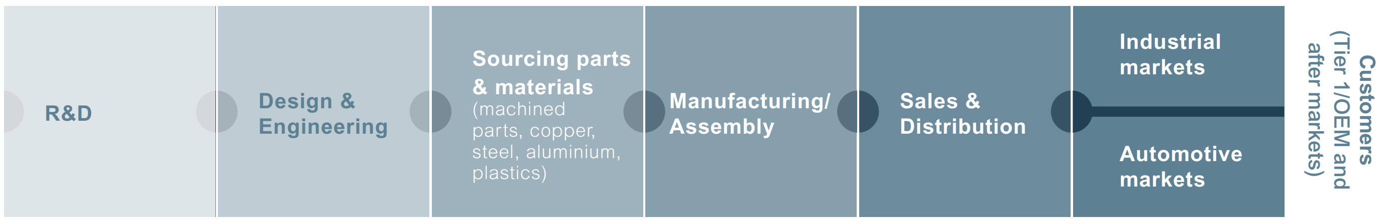
The above could result in a dilemma with respect to achieving the targets related to the material topics (see the materiality matrix on page 50).

Few critical materials are used other than those referred to in this section.
Kendrion applies a local sourcing strategy as appropriate. The most frequently-used materials are steel, aluminium, copper and plastics. In many cases, semi-finished products are purchased on the basis of specifications of Kendrion or its customers, and only the final assembly takes place in Kendrion's plants. In 2017, Kendrion used 1,916 tonnes of copper (best estimate) in the manufacture of the company's products (2016: 1,860 tonnes).

Supplier Code of Conduct
The Kendrion Supplier Code of Conduct requires suppliers to assume their responsibility for matters concerning the environment, human rights, working conditions and fair trade. The suppliers are also requested to introduce similar rules themselves. Kendrion has set a target stipulating that the Kendrion Supplier Code of Conduct must be accepted by all its main suppliers in all business units.

Kendrion obtained increased commitment from its suppliers in 2017, with twice as many suppliers having signed the Supplier Code of Conduct as in 2014. This includes 100% of the top 30 suppliers.

Simplified supply chain overview Kendrion



Supplier selection and audits
The extent to which a potential supplier addresses environmental and social issues and business ethics is important to supplier selection, in addition to standard criteria such as product quality, in the selection of suppliers. Kendrion conducts CSR supplier audits to review whether suppliers continue to comply with the required standards. Audits that result in unsatisfactory assessments and that reveal that the relevant supplier does not meet the requirements for compliance with the Supplier Code of Conduct are followed by a meeting to prepare a remediation plan and review means of achieving improvements. Failure to adequately follow up the remediation plan may result in the termination of the relationship with the relevant supplier.

For 2017, the aim was to conduct at least three CSR supplier audits for each plant with more than eighty employees and at least one for each other operating company. In total this would lead to 39 audits. The number of audits in 2017 was 37, which means that the target was nearly achieved (95%). The results of the supplier CSR audits have generally been positive and there were no suppliers that did not fulfil the recommended requirements for compliance with the Supplier Code of Conduct.

With the approach and initiatives as described above, Kendrion actively encourages its suppliers to take responsibility in addressing issues that affect the supply chain as a whole.

Sustainable operations

Waste management
Kendrion aims to minimise and dispose waste in an environmentally responsible manner and considers feasible recycling solutions for its business, with a view to reducing process residuals, reducing costs and maintaining environmental compliance, while continuing to streamline its operations.

ISO certification overview

17 production plants (of which 9 Automotive)

Plants	ISO 9001	ISO/TS 16949	ISO 14001	ISO 50001
2015	20	11	15	2
2016	20	11	16	7
2017[1]	17	8	15	9

[1] Operations in Brazil and India were discontinued and the facilities in Nanjing (China) and Switzerland were closed with manufacturing moved to other Kendrion locations.

All Kendrion companies which have been awarded ISO 14001 certification keep records of their production and processing of waste. Internal instructions at these companies are issued for the safe use of materials and the separated collection and disposal of waste. The companies work solely with certified waste processing companies. As part of the certification process, new waste reduction measures must be implemented each year, and measures that reduce the use of hazardous goods are externally audited. Those measures can differ from plant to plant.

In 2017, Kendrion worked on the further development of an environmentally conscious plan to dispose of hazardous waste generated by its business activities, and it aims to progress the finalisation of this plan in the course of 2018.

In defining its global waste management plan, Kendrion experiences different local practices towards the minimisation and disposal of waste in the different regions in which it operates. Local practices of the USA, China and Europe are different.

ISO certification
Within Kendrion, the quality, environmental and safety systems are usually combined in a single system that forms the basis for the implementation of many projects. Virtually all of Kendrion's operating companies comply with the most stringent quality and safety requirements.

ISO 9001 lays down general requirements for the company's quality management system, while ISO/TS 16949 has been developed specifically for the automotive industry and imposes stringent requirements. ISO 14001 is an environmental management system certification. As from 2016 all Kendrion manufacturing sites are ISO 14001 certified except for Mishawaka, USA and Toluca, Mexico (will be closed in 2018). The ISO 50001 standard is focused on the reduction of organisations' energy consumption on the basis of detailed insight into their energy consumption and use of energy. In 2016, five European manufacturing sites gained ISO 50001 certification and in 2017 two European manufacturing sites gained ISO 50001 certification.

Integrated business processes
Kendrion is committed to the integration of sustainable practices within its business processes. Further improvement measures aimed at the increased integration of sustainable

business practices were introduced in 2017. Sustainability is a mandatory element of Kendrion's investment approval process and an integrated part of the standardised management reporting forms and discussions. As explained in the 'Risks and risk management' section on page 60, Kendrion uses Letters of Representation. The standardised Letters of Representation require officers to also confirm the accuracy of the reported non-financial information.

Energy & CO_2 reduction

Kendrion endeavours to make efficient use of energy and aspires to reduce energy consumption in an effort to combat climate change and the depletion of fossil fuels. Reduction of energy consumption and reduction of CO_2 emissions are important themes of the CSR strategy and good progress was achieved in this respect. Relative CO_2 emissions and energy consumption were reduced 58% and 17% respectively compared to 2014. In addition, many of the companies have switched to CO_2 neutral gas contracts.

Activities and investments

Kendrion encourages awareness of electricity and gas use among its employees at its operating companies by requiring simple changes in behaviour such as switching off lights and lowering thermostats after working hours. Kendrion has invested well over EUR 3 million in energy-efficient systems in recent years. In 2017, Kendrion made further investments in energy-efficient systems for manufacturing sites in Germany and the USA that will lead to further improvements in 2018 and 2019. These investments include the installation of new combined heating and power systems, compressors and LED light projects. In 2017, Kendrion devoted a great deal of effort reducing production-line energy consumption in and around the workplace, for example by more efficient use of air-conditioning systems.

CO_2 emissions[1]		2017	2016	Δ % (2017/2016)	**Δ % (2017/2014)**
Absolute emissions, tonnes		7,098	7,187	(1.2)	**(54.1)**
Relative emissions, tonnes / million EUR added value		33.5	36.0	(7.1)	**(58.4)**

Energy consumption[2]		2017	2016	Δ % (2017/2016)	**Δ % (2017/2014)**
Power	kWh	24,954,778	25,562,201	(2.4)	**(16.6)**
Fuel oil	kWh[3]	498,940	758,093	(34.2)	**(64.9)**
Natural gas	kWh	11,443,447	11,597,007	(1.3)	**25.3**
Absolute consumption, kWh		36,897,165	37,917,301	(2.7)	**(8.8)**

Energy consumption per EUR million added value		2017	2016	Δ % (2017/2016)	**Δ % (2017/2014)**
Power	kWh	117,635	128,143	(8.2)	**(24.4)**
Fuel oil	kWh	2,352	3,800	(38.1)	**(68.2)**
Natural gas	kWh	53,944	58,135	(7.2)	**13.5**
Relative consumption, kWh / million EUR added value		173,931	190,078	(8.5)	**(17.4)**

1 Scope 1 and 2 of the Greenhouse Gas Protocol.
2 See for reporting periods, definitions, conversion factors and scope pages 162 and 163 of this Report.
3 Conversion 1 kWh=0.099 ltr..

As an international company operating in various jurisdictions, Kendrion cannot avoid travel. Kendrion does, however, strive to avoid unnecessary travel as much as possible and encourages its employees to use teleconference calls and other remote communications or messenger services. Electric cars are made available for business use at some Kendrion operating companies.

Health and safety

Kendrion regards a healthy and safe working environment as one of the basic rights of its employees. Kendrion's operating companies comply with the most stringent quality and safety requirements. The requirements include the appointment of safety officers, the periodic training of employees and the consistent performance of safety audits.

In addition to certain centrally coordinated health and safety-related policies and procedures, day-to-day responsibility for health and safety is concentrated within the operating companies. Accidents, lost time injury rates and illness rates are monitored by the operating companies and consolidated centrally in accordance with Kendrion's established reporting processes as recorded in its CSR reporting manual.

TAILOR-MADE ELECTRICAL VEHICLE SOUND FOR CHINA

Product: Sound system for exterior sound in electric and hybrid cars.

Customer: OEMs of electric and hybrid vehicles in China.

Kendrion's solution: Our sound system consists of a sound actuator and includes the required electronic control unit and software that can be easily adjusted to each specific vehicle sound requirement.

Added value: Our solution complies with the Acoustic Vehicle Alerting System (AVAS) regulation issued by the United Nations Economic Commission for Europe (UNECE). It contributes to a safer traffic environment for cars, cyclists and pedestrians.

Kendrion's continual focus on the safety of the production processes has enabled the company to limit the number of accidents in recent years. In 2017, the reported number of accidents decreased to 6.8 accidents per 1,000 FTE (2016: 14.4 accidents per 1,000 FTE). Accident figures are below the relevant industry benchmarks. There have been no fatal accidents at work in recent years. Kendrion maintains safety as a priority and will continue to pay considerable attention to further reducing the number of accidents. Accidents are reported on a monthly basis and followed by a comprehensive evaluation and review of the feasibility of implementing further improvements in safety procedures and working methods.

In 2017, the lost time injury (LTI) rate, which is time lost due to accidents, increased to 432 days (2016: 418 days) as a result of the carry-over effect of two accidents that occured at the end of 2016. The overall illness rate based on illness hours with wage continuation in 2017 was 2.7%, in line with the previous year. Four operating companies reported illness rates above 4%.

Many Kendrion companies have implemented programmes to promote their employees' health. Examples include the availability of free 'stop smoking' courses, fresh fruit and mineral water, and the opportunity offered to employees to receive an influenza vaccination during working hours. In 2017, employees at various operating companies were able to participate in an annual health day that offered them a general health check (blood pressure, diabetes, etc.).

Other examples of measures include training courses designed to avoid back complaints, ergonomic advice and grants to attend a gym at various locations.

Responsible business conduct

Ethical culture

Kendrion believes it is important that all activities at the company are conducted with integrity and in a transparent manner. To this end, Kendrion aims to foster a culture where shared norms and universal ethical values and behaviours are the minimum standard. Shared norms, ethical values and expected behaviours are recorded in a set of internal policies and procedures that form part of the Global Legal Compliance and Governance Framework. In addition to setting norms, values and expected behaviours, the Global Legal Compliance and Governance Framework is aimed at ensuring compliance with applicable laws and regulations.

The Global Legal Compliance and Governance Framework includes the following key policies and procedures: Code of Conduct, Anti-Bribery and Anti-Corruption Policy, Speak-up Procedure, Competition Compliance Manual, Insider Trading Code, Supplier Code of Conduct and related internal policies and procedures.

Kendrion considers it essential that every employee understands, complies with and conveys the shared norms and universal ethical values and behaviours as laid down in the policies and procedures of the Global Legal Compliance and Governance Framework. The policies and procedures of the Global Legal Compliance and Governance Framework are fundamental to secure responsible business conduct. It is the responsibility of senior management to lead by example, and to ensure that all Kendrion employees are aware of the Global Legal Compliance and Governance Framework and behave in accordance with the spirit and the letter of Kendrion's policies and procedures.

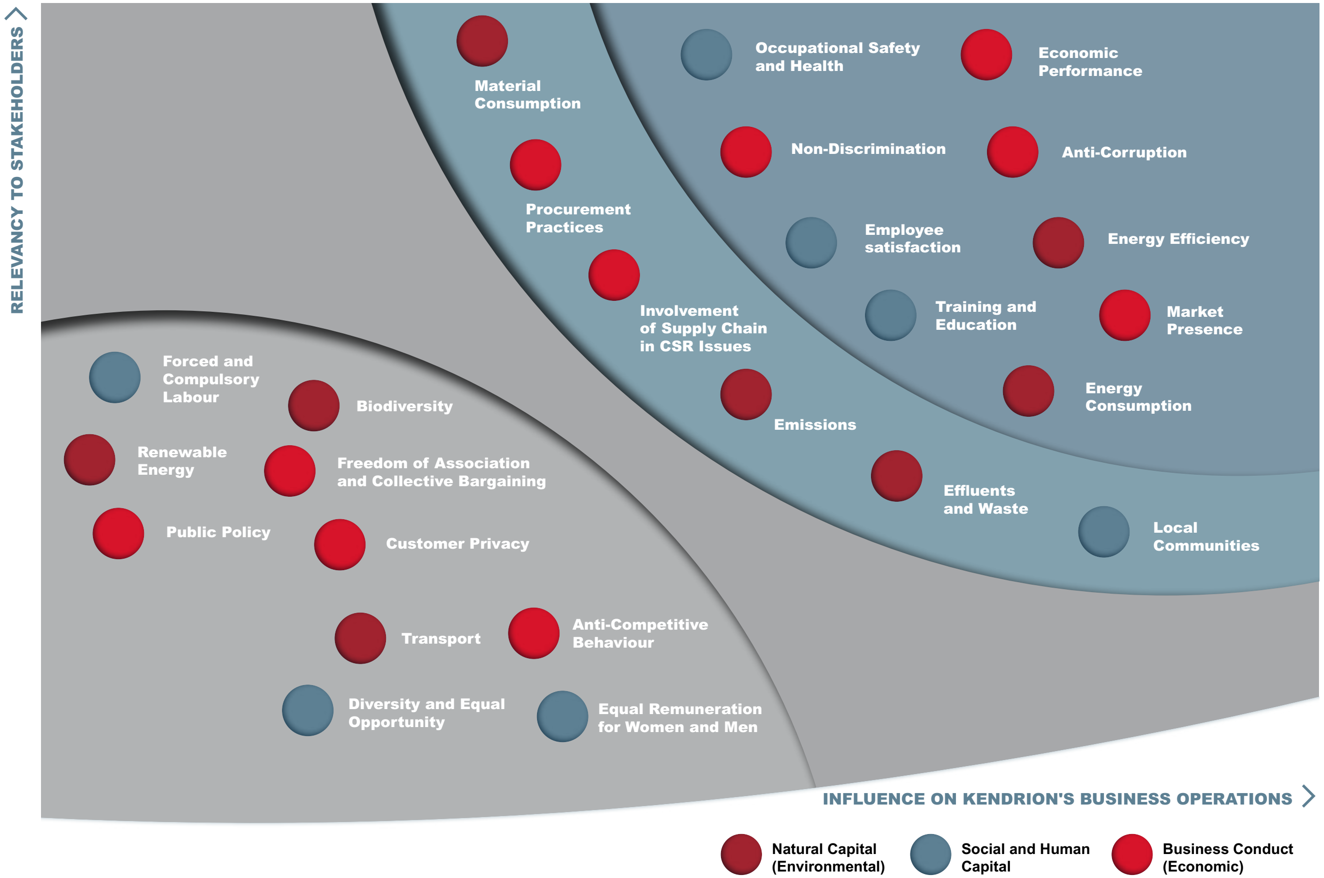
Kendrion requires its operating companies to implement the Global Legal Compliance and Governance Framework and to issue additional measures and guidelines as required under local laws and regulations. In 2017 the Global Legal Compliance and Governance Framework was further strengthened.

Reference is made to the section 'Risks and risk management' on pages 60-62 for information about the Global Legal Compliance and Governance Framework, the Code of Conduct, the Speak-up Procedure and the Insider Trading Code.

Anti-Bribery and Anti-Corruption policy
Kendrion does not tolerate bribery or any form of corruption. Bribery can include the offering, promising or giving of payments or other advantages to any person (including government officials or public officials) to influence a business outcome improperly, but it also covers accepting payment or advantages given to influence a business outcome improperly. Integrity of financial reporting is also a key principle. The Kendrion Anti-Bribery and Anti-Corruption Policy specifically addresses these matters.

Training and awareness
Online training courses are offered to increase awareness of Kendrion's norms and values and expected behaviours, and to ensure compliance with the policies and procedures that form part of the Global Legal Compliance and Governance Framework.

Materiality matrix



Community connection

Together@Kendrion
Kendrion believes it is imperative to its responsibility, to increase awareness of social problems and to contribute to the reduction of social and economic gaps in the world in general and in the local communities in which Kendrion operates in particular. Kendrion cares about long-term futures and values the social good that can be done by showing initiative.
In 2017, Kendrion launched the Together@Kendrion initiative. By means of Together@Kendrion, Kendrion rewards community investment initiatives submitted by the Kendrion operating companies and employees. Through the Together@Kendrion initiative, all Kendrion employees are invited to submit a proposal for the funding by Together@ Kendrion of a project or initiative with a link to the local community. Focus areas include for example, education and development, human rights, equal opportunities, health and safety, environmental protection and technology.

Materiality analysis

The materiality analysis is partly carried out based on

EFFICIENT AND SUSTAINABLE COMBUSTION IN ENGINES

Product: Piston cooling valve for combustion engines.

Customer: OEMs of combustion engines and hybrid vehicles.

Kendrion's solution: The piston cooling valve regulates the oil flow for cooling the engine's piston. By generating optimum temperature conditions, the valve enhances efficiency and consequently helps reduce energy consumption and CO_2 emissions. It furthermore extends the lifespan of the engine.

Added value: The new-generation valve allows for easy adaptation to customer-specific installation spaces with different geometries. Unlike conventional technology with spool valves, this patented Kendrion solution achieves lower leakage and is also less sensitive to contamination in the oil circuit.

a number of material aspects as described in the guidelines of the Global Reporting Initiative (GRI) G4. The pre-selection of these material and non-material aspects has been made with due regard for:

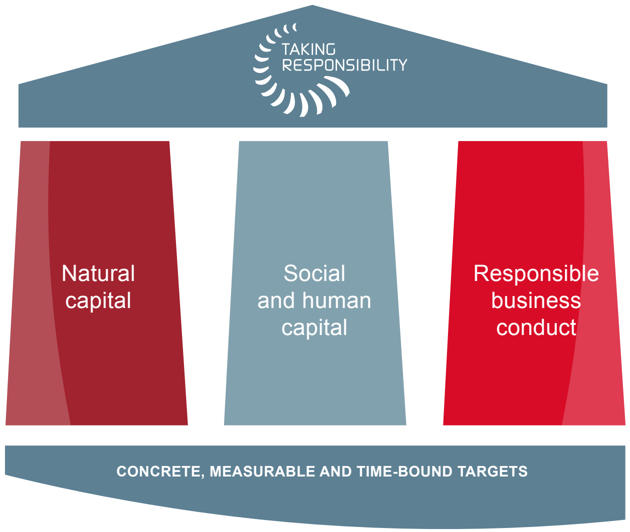
- The *nature* of Kendrion's activities and business processes;
- The demands made on Kendrion and its products by its customers in connection with sustainability in the short term and long term (the *urgency*);
- Kendrion's potential *impact* and *influence* in the chain in the short and long term;
- The potential *benefit* for Kendrion;
- The *effort* it takes to implement measures in Kendrion's business processes and activities, with a view to the other strategic spearheads;
- The *relevance* for stakeholders and the possible effect on them.

The outcome is based on the stakeholder dialogues conducted during the past three years and is characteristic for the continuity of Kendrion's CSR strategy. It is anticipated to further engage with Kendrion's stakeholders in 2018 to gain deeper insight into the relevance and importance of CSR related themes for Kendrion and its stakeholders and the reasonable expectations of stakeholders.

CSR strategy 2018 and beyond

Kendrion's Taking Responsibility programme has resulted in major achievements over the past three years. Progress was made in many areas, including the establishment and further improvement of sustainable business processes, the reduction of energy consumption and CO_2 emissions, the introduction of various health and safety initiatives, the increased commitment of Kendrion's suppliers to make a positive contribution through their adherence to the Kendrion Supplier Code of Conduct, the launch of the Together@Kendrion initiative, and many other important accomplishments. 2017 was the final year of Kendrion's CSR strategy for 2015 – 2017.

In the course of 2017, the Executive Board together with the Management Team developed proposals to extend the CSR strategy to 2018 and beyond. The proposals are directed at further alignment and integration of the CSR strategy with the 'Simplify, Focus and Grow' strategy. Moreover, the emphasis of the updated CSR strategy is on long-term value creation for Kendrion and society through pillars of value creation, taking into account the interests and reasonable expectations of Kendrion's stakeholders. Important pillars of value creation are: Natural Capital, Social and Human Capital and Responsible Business Conduct. A thematic approach applies for each pillar, as this contributes to an integrated way of thinking and acting.



VALUE CREATION PILLARS

SDGs most relevant for Kendrion

5	– Gender equality	Achieve gender equality and empower all women and girls
7	– Affordable and clean energy	Ensure access to affordable, reliable, sustainable and modern energy for all
12	– Responsible consumption and production	Ensure sustainable consumption and production patterns

Having due regard to the achievements under the Taking Responsibility programme over the past three years and the outcome of the materiality analysis, themes for the three pillars of value creation have been identified for the CSR strategy for 2018 and beyond. The themes for the Natural Capital pillar include: further reduction of energy consumption and CO_2 emissions and waste and recycling. The Social and Human Capital pillar focuses on themes such as community connection and investment, health and safety, diversity and inclusion and company culture. General business principles, anti-bribery and anti-corruption, supply chain management and compliance and governance are themes for the Responsible Business Conduct pillar. The material themes for each pillar will be supported by concrete and measurable targets.

In 2015, the United Nations introduced 17 Sustainable Development Goals (SDGs) and 169 associated targets aimed at sustainable development worldwide. In 2017, Kendrion made an initial assessment to identify which SDGs are most relevant for Kendrion. Following its initial assessment, Kendrion considers the SDGs described in the table above to be those to which Kendrion can contribute most.

Following further engagement with Kendrion's stakeholders in the course of 2018, Kendrion may decide to adjust the material topics for the three pillars of value creation and the selection of SDGs as described above. The outcome of such further stakeholder engagement may also lead to the identification of associated targets relevant to the SDGs concerned. The final selection of material and non-material topics, SDGs and related measures will be further addressed in the updated CSR strategy for 2018 and beyond. The CSR strategy for 2018 and beyond will be integrated with the Mid-Term Plan 2019 – 2023. It is anticipated to finalise and communicate the updated CSR strategy and the related long-term targets in the course of 2018 together with the Mid-Term Plan 2019 – 2023.

Natural Capital – annual targets 2018

5% annual reduction of relative energy consumption compared to 2017

5% annual reduction of relative CO_2 emission compared to 2017

Social and Human Capital – annual targets 2018

≤ 10 accidents per 1,000 FTE

LTI rate: **≤ 400** days
(Kendrion group-wide total)

Illness rate of **≤ 2.6%**
(Kendrion group-wide total)

Responsible Business Conduct – annual targets 2018

90% of strategic suppliers have signed the Supplier Code of Conduct (Kendrion group-wide total)

25 implementation audits to be performed at strategic suppliers (Kendrion group-wide total)

Value creation model

OUTCOME

INCREASED SAFETY | INCREASED MOBILITY | INCREASED COMFORT | INCREASED HEALTH

5 GENDER EQUALITY | 7 AFFORDABLE AND CLEAN ENERGY | 12 RESPONSIBLE CONSUMPTION AND PRODUCTION

OUTPUT

Business output[1]

Revenue	€ 461.8 mln
EBITA	€ 37.0 mln
Net profit	€ 23.3 mln

Natural output

58.4% Relative reduction of CO_2 emissions compared to 2014

17.4% Relative reduction of energy consumption compared to 2014

Human output

Accidents
6.8 accidents per 1,000 FTE
432 LTI (days)

Illness rate
2.7% average

Business conduct output

728 Number of strategic suppliers signed Code of Conduct

37 Number of CSR supplier audits

ADDED VALUE

SIMPLIFY | FOCUS | GROW

ENTERPRISE RISK MANAGEMENT | GLOBAL LEGAL COMPLIANCE AND GOVERNANCE FRAMEWORK

INPUT

Financial capital[1]

Free cashflow	€ 14.2 mln
Net working capital	€ 45.6 mln
Invested capital	€ 255.1 mln

Natural capital

Power	24,954,778 kWh
Fuel oil	498,940 kWh
Natural gas	11,443,447 kWh
Copper	1,916 tons

Human capital

2,645
FTEs

Manufactured capital

> 10,000
Solutions and services

[1] Nomalised for one-off impact simplifying measures.

2,645	**Total number of employees in FTEs** at 31 December (number FTE)	2016 **2,578**
1,355	**Direct employees** (number FTE)	2016 **1,320**
1,150	**Indirect employees** (number FTE)	2016 **1,180**
140	**Temporary employees** (number FTE)	2016 **78**
2,664	**Total number of employees** at 31 December	2016 **2,668**
1,142	**Women in permanent employment** (number)	2016 **1,154**
1,165	**Men in permanent employment** (number)	2016 **1,199**
357	**Employees with a fixed-term contract** (number)	2016 **315**
42	**Average age of all employees**	2016 **42**
11	**Average number of years' service**	2016 **11**
48,436	**Wage costs per FTE** (EUR)	2016 **47,552**
0.7%	**Training costs** (as a % of wage costs)	2016 **0.7%**

MICRO-PULSING TO EXTEND THE LIFETIME OF AIR CONDITIONING CLUTCHES IN BUSES OPERATING IN HOT COUNTRIES

Product: Micro-pulsing of an electromagnetic clutch.

Customer: OEMs and producers of air conditioning systems for commercial vehicles.

Kendrion's solution: Micro-pulsing is used to solve problems with air conditioning clutches in bus applications, especially in hot countries where the air conditioning is switched on for long periods. The longer a clutch is engaged, the greater the risk of losing ball-bearing lubrication. The solution is to let the bearing roll off despite the clutch being engaged. An electronic circuit, which opens the clutch just for a brief moment, generates a micro-movement of the rolling elements and thus ensures lubrication of these anti-friction bearings.

Added value: Extension of lifetime for air conditioning clutches in buses in hot countries.

Human Resources

Kendrion's employees are the company's most valuable resource. Human Resources supports creating the right culture and conditions to help Kendrion attract and retain the right people with the right capabilities. To achieve that, we aspire to offer our employees the right opportunities for career development and personal growth, in a safe and attractive working environment. Through various initiatives such as Together@Kendrion, we also stimulate our employees to actively contribute to the reduction of social and economic gaps. Reference is made to the 'Corporate Social Responsibility' section for more information about community involvement and investment initiatives.

In May 2016, Kendrion launched an updated strategy to deliver sustainable profitable growth for the business in the medium to long term through the three pillars: 'Simplify, Focus, Grow'. The focus in 2016 was on complexity reduction and cost efficiency, resulting in a range of simplification measures ahead of schedule. In 2017, Kendrion continued to accelerate the implementation of simplification measures where possible, resulting in a more simple and focused organisational structure. Human Resources played an important role in facilitating the organisational transition and the design and implementation of an adjusted agile organisation structure that will enable Kendrion to meet its growth targets in a sustainable and profitable way.

The Human Resources teams operate locally in Kendrion's operating companies but are committed to a cooperative structure globally under the responsibility of Kendrion's Global HR Manager based in Villingen, Germany.

Talent management and recruitment

Kendrion's new organisational structure also requires a different balance of skills and competences throughout our business. This is both a challenge and an opportunity as we compete for talented people in a tight market where there is a shortage of skilled engineers and other specialists.

Kendrion's recruitment initiatives include a regular presence at job fairs of technical universities and other relevant institutes. We also conduct targeted PR activities, aimed at promoting Kendrion as an attractive employer. A substantial number of students began their apprenticeship or course of study at Kendrion in 2017.

Kendrion has continued to professionalise its Human Resources processes, including the completion of the implementation of a web-based talent management and succession-planning tool.

Kendrion advocates the principle of internal mobility and aims to fill vacancies with internal candidates. Internal moves are considered beneficial to the development of Kendrion employees by providing them with new and challenging opportunities, while at the same time keeping knowledge within the organisation. In 2017, the Human Resources teams were able to fill over 30% of vacancies with internal candidates.

Training and development

Training is key to both recruiting and retaining the right people and to maintaining a strong and solid position in a competitive market. To ensure that Kendrion employees remain fully committed and aligned with the strategy and to provide our employees with opportunities for professional and personal growth, Kendrion's operating companies offer a wide range of internal training courses.

Kendrion aims to ensure that employees receive the right training for their current positions and for positions employees may be able to occupy in the future. Several new training courses were added in 2017, and where appropriate, existing training courses were adapted to ensure continued alignment with Kendrion's strategy.

A new Leadership & Performance Programme was introduced in 2017. This Programme was developed jointly with the Rotterdam School of Management and comprises three modules exclusively designed for Kendrion. Kendrion's Leadership Team (consisting of Kendrion's 30 most senior employees) participated in two modules with the remaining module to be offered in 2018. The modules of the Leadership & Performance Programme focus on themes such as understanding and improving performance within the context of the market and industry in which Kendrion operates and are aligned with the rationale underlying the 'Simplify, Focus, Grow' strategy. The Leadership & Performance Programme also constitutes an important platform for exchanges of experience between the (senior) management and for further expansion of collaboration between the operating companies.

Kendrion also offers a three-year modular training programme (Kendrion High Potential Programme) specifically designed for talented and ambitious employees with potential for management roles. A group of eleven high-potential employees graduated in 2017, and a new group of high-potentials will commence the programme in 2018.

Employee diversity

At Kendrion, we believe in the strength of a diverse workforce. Diversity promotes better decision-making and the exchange of intercultural experience and ideas. We aspire to recruit the right mix of people for Kendrion as a whole, as well as for each department, taking into account competences and skills, gender, nationality, background and other factors. However, diversity is not a goal in itself, as Kendrion always strives to appoint the best and most suitable person for the job.

In 2017, Kendrion's workforce comprised 38 nationalities employed in 10 countries. Fifty% (50%) of our workforce is female. Across the organisation as a whole, we feel we have a healthy balance of nationalities and gender. However, the percentage of women in senior management positions in Kendrion's operating companies is relatively low. Kendrion actively strives to recruit more women for senior management positions through various initiatives, including proactive and regular contact with universities and the organisation of internal events, all with a view to further improve the balance of gender diversity in senior management positions. These initiatives contributed to the appointment of a woman to the Management Team as well as additional appointments of women to the Leadership Team.

Kendrion promotes the formation of a workforce and management that reflects the composition of the local population as closely as possible.

Remuneration

The remuneration framework is designed to create transparency and fairness in the structure of both fixed remuneration and variable remuneration. Kendrion offers its employees attractive remuneration packages that are in line with industry standards and the local market and are based on job-specific requirements. A bonus scheme has been implemented for senior management that is based on Kendrion's financial performance and on certain individual non-financial performance targets. These also include CSR targets.

Employee satisfaction and culture survey

Kendrion's existing group-wide employee satisfaction and culture survey was extended in 2017 to all major operating companies. One of the aims of the survey is to determine how employees value Kendrion's culture and to identity which areas require improvement. In 2017, two additional operating companies, representing a total workforce of approximately 500 employees, participated in the survey. Nearly 70% of that workforce participated in the survey. The survey results revealed that employees appreciate the work environment, culture and atmosphere, but see room for improvement with respect to the workload and cooperation between departments. Kendrion is taking measures to address this. The average score achieved in the employee satisfaction surveys of all major companies is 76%.

Kendrion intends to further improve the group-wide employee satisfaction and culture survey in 2018. Going forward, Kendrion will repeat the survey at regular intervals to monitor progress and identify areas that require further action.

HIGHEST QUALITY IN SERVO MOTORS FOR ROBOTS IN THE AUTOMOTIVE INDUSTRY

Product: Spring-applied brakes for servo motors.

Customer: Global suppliers of welding robots for applications in the automotive industry and other industries.

Kendrion's solution: The highest reliability, repeatability and brake accuracy, which are key in providing robots with minimal downtime.

Added value: Long life and high product reliability with a passion for the best possible quality advantage.

As part of the new CSR strategy for the period 2018 and beyond, Kendrion will enhance its focus on people's competences, capabilities and experiences, and motivation. In this context, 'company culture' is and continues to be a material theme. It is important to foster a company culture that contributes to the successful realisation of Kendrion's strategy.

Employee representation

Works councils or employee representatives that have been installed at Kendrion's largest operating companies in Germany, Romania and Austria are involved in a wide range of employment, health & safety and social matters, in accordance with local labour legislation. About 60% of all Kendrion employees are represented by these works councils and employee representatives. Approximately 1,350 of the contracts of employment in Germany and Austria are governed by or follow the collective bargaining agreements for the metal industry in the country concerned. Kendrion has a good relationship with the works councils and the trade unions.

Background

Kendrion promotes local entrepreneurship at its companies and, consequently, offers scope to the management to exercise the associated discretionary powers. Kendrion actively conveys the essential need to maintain a healthy equilibrium between entrepreneurial spirit and the extent to which risks are accepted.

Adequate risk management is an integral element of good business practice. When risks are made visible Kendrion's managers can implement adequate measures that offer optimal control of those risks. Of course, Kendrion's risk management is not intended to eliminate all risks entirely: doing business is never without risks. Kendrion's objective is to adopt an approach to business risks that minimises the chance to have adverse events and the impact of such events, while always taking into account the necessary balance between risk exposure and costs. Kendrion's risk appetite is periodically evaluated by the Executive Board and shared and discussed with the Supervisory Board and the Management Team. The Executive Board strives to balance business opportunities with the expectations of shareholders, employees, regulators and other stakeholders.

The risk-reward appetite can be specified in the following terms:

Risk category	Kendrion's risk appetite
Strategic risks	**Moderate:** strike appropriate balance between risk and reward
Operational risks	**Moderate:** align targets and the related costs, focus on sustainable profit maximisation
Financial reporting risks	**Low:** full compliance with financial reporting rules and regulations
Compliance and fraud risks	**Low:** full compliance with relevant legislation and regulations in all jurisdictions where Kendrion operates

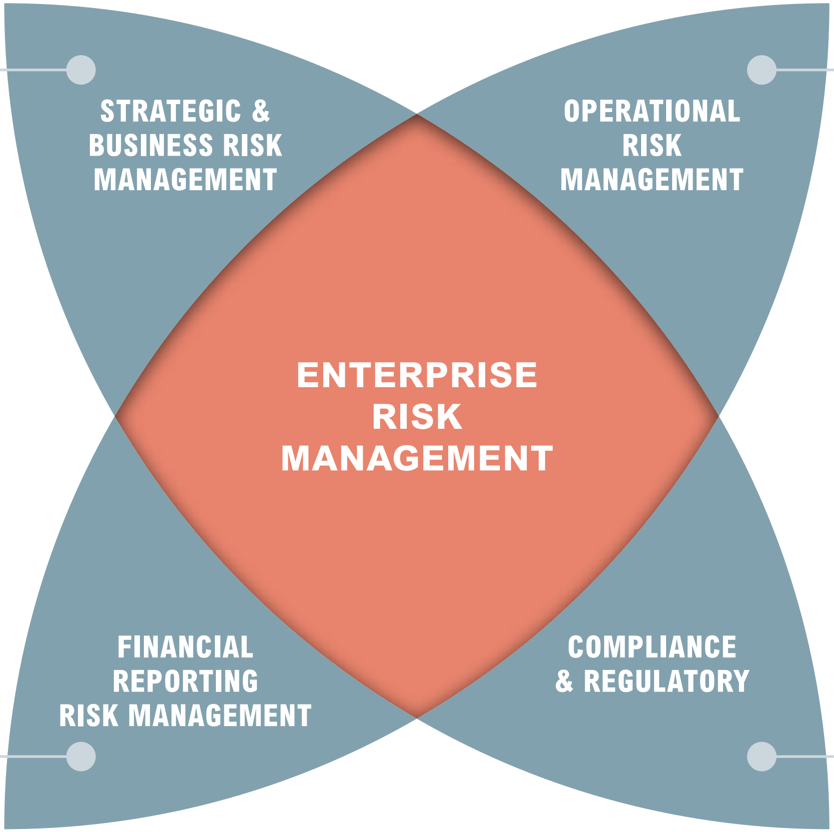
The Supervisory Board oversees governance and risk control measures and evaluates the effectiveness of the implemented control measures. The Audit Committee prepares the decision-making of the Supervisory Board on risk management, compliance and audit matters. For further details on the Supervisory Board and the Audit Committee, reference is made to the 'Corporate Governance' section on pages 67-72.

Kendrion has a responsibility to put internal controls and procedures into place and test them to verify their effectiveness. Local management is expected to be fully aware of the operating risks and the necessity for internal control procedures. Kendrion devotes continual attention to the optimisation of risk management and control systems as part of the everyday decision-making. The Executive Board emphasises that risk management and control systems – no matter how professional they may be – can neither offer absolute guarantees that the company's objectives shall be achieved nor entirely prevent material errors, loss, fraud, or violations of laws or regulations.

Kendrion employs a structured risk management framework that connects the various elements of risk management and the relationship between the elements. Kendrion's objective is to avoid duplication within separate risk management systems whenever possible. The factors that underpin the quality of the risk management framework are integrity, business ethics and the staff's expertise. Management style and the manner in which authorisations and responsibilities are delegated and monitored by the management are equally important.

Enterprise Risk Management

Kendrion's approach to the company's risk management is laid down in the Enterprise Risk Management Framework as shown in the following illustration:



- Quarterly evaluation per business unit
- Risk management survey
- Yearly strategic update

- Quality systems
- Safety & health; environment
- Hedging against commodity price risk
- Monitoring & hedging financial market risk
- Insurance
- IT governance
- Quarterly evaluation per business unit

- Group Reporting Manuals
- Group Reporting Committee
- Monthly closing procedures
- Internal control procedures
- Audits (external & internal)
- Weekly review cycle with business unit management

- Compliance procedures
- Reporting & disclosures
- Legal counseling
- Internal audits
- Training
- Speak-up line

Control environment and financial reporting risk management in the year under review

Control environment

The Executive Board is responsible for the control environment including risk management and internal control systems, and for the optimum management of the strategic, operational, financial, tax and reporting risks related to Kendrion's business. The risk management and internal control systems extend to areas such as culture, policy-making, processes, duties, influencing conduct and other aspects of doing business that provide for the achievement of targets. Risk management and control aims to prevent or in a timely manner identify material errors, loss, fraud, or infringement of legislation and regulations.
During the year under review the major elements and foundations of Kendrion's risk management and internal control systems were:

Code of Conduct

Kendrion has implemented a Code of Conduct that applies to all Kendrion staff and to the members of the Supervisory Board. The principles and best practices established in the Code of Conduct reflect the main values that guide Kendrion's staff and members of the Supervisory Board in the execution of their duties. The core themes include conduct in the market, authorities, gifts, anti-bribery, corporate social responsibility, accountability in general, and the obligation to exercise due care regarding health and safety, the environment, and social interests. Kendrion promotes compliance with the Code of Conduct by regularly bringing the Code of Conduct to the attention of its managers and staff and Supervisory Board members. Deviations from the Code of Conduct are not tolerated. The Code of Conduct is published on Kendrion's website. Kendrion also has a Supplier Code of Conduct to address the above themes in the supply chain.

Speak-Up Procedure

Kendrion offers employees an opportunity to report irregularities or suspicions without jeopardising their (legal) position. Any such report gives cause to an internal investigation. An external hotline was introduced in 2016. This gives employees an additional means of submitting such reports in their own language by phone or computer in a confidential, anonymous manner if they so choose. Kendrion also appointed Confidential Counsellors whom employees can contact if they wish to make confidential reports about (suspicions of) irregularities.

One irregularity was reported by an employee in 2017 involving the sale of products by employees for their own personal benefit and allegations of violation of the Kendrion Code of Conduct by local management. This report was further investigated with the support of external forensic experts. Adequate measures have been taken against the employees involved and additional internal control measures have been implemented in order to prevent such incidents in the future. The violations found had hardly any financial impact.

Regulations to prevent insider trading

Kendrion has regulations covering securities transactions by members of the Executive Board, members of the Supervisory Board, members of the Management Team and other designated employees. The 'Insider Trading Code' is published on Kendrion's website. The Insider Trading Code is intended to ensure the avoidance of insider trading or the appearance thereof, and any mixing of business and private interests.

Rules and Regulations and Letters of Representation

Kendrion employs Rules and Regulations and Letters of Representation. The Rules and Regulations constitute rules of behaviour governing all Kendrion Managing Directors. The Letters of Representation are submitted once a quarter, in a bottom-up procedure, ultimately to Kendrion's CFO. All officers are required to sign the letter to confirm to their managers that the financial and non-financial information they have reported is correct and complete and no violations of applicable regulations and the Kendrion Code of Conduct with material impact occurred.

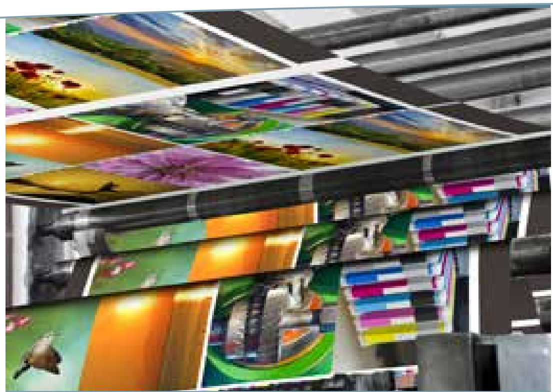
Group Reporting Manual

Kendrion has implemented a Group Reporting Manual governing all operating companies to provide for correct financial reporting. The Group Reporting Manual is continually updated. To this end Kendrion has implemented measures including the formation of the Kendrion Group Reporting Committee, with representatives from the operating companies. Reporting sets are standardised based on a standard Chart of Accounts. A Corporate Social Responsibility Reporting Manual has also been implemented to ensure accurate and reliable reporting of non-financial data.

Planning and control cycle

Insight into Kendrion's performance is obtained from the monthly reports of the current figures submitted by all the operating companies, weekly cash forecasts and daily consolidated revenue reports. In the middle of each year, Kendrion prepares a Mid-term Plan. The planning horizon of the Mid-term Plan is five years. This plan provides insight into the strategic course of the companies and business units.

In the fourth quarter, the Mid-term Plan forms the basis of a more detailed annual budget to provide a precise management tool for the following calendar year. Assessment and follow-up on the progress, development of key performance indicators and deviations from short- and long-



HIGH-TECH INK SUPPLY SYSTEM IN DIGITAL PRINTING MACHINES

Product: Assembly unit combining fluid-isolated valves with FluidBoard®.

Customer: Leading manufacturer of digital printing machines for printing on demand.

Kendrion's solution: The brand-new FluidBoard® is made from multiple layers of plastic plates with integrated channels for fluids which are assembled using modern laser welding technology. The unit controls and supplies the ink for the print head. Up to eight colour systems are used, making an integrated solution possible.

Added value: Integrating and simplifying the whole print head leads to a significant reduction in assembly costs.

term targets are performed periodically at various levels in the organisation. Kendrion has implemented a capital expenditure procedure which makes use of standard investment request forms. Executive Board approval is required for new projects with planned annual revenue in excess of EUR 1 million to test return on investment, payback period and cash flows. Executive Board approval is also required for capital investments in excess of EUR 100,000.

Periodic reports and meetings

Regular discussions in weekly conference calls between the Executive Board, the Management Team and similar reviews within the business units address the risks and internal risk management system. Each business unit submits a comprehensive written report at least once a quarter which provides details about the financial and operational situation and the status of any current claims and proceedings, where relevant.

Strategic and business risk management

In 2017, the Executive Board together with the senior management of the holding, business units and operating companies conducted a risk survey which reviewed almost fifty potential risks that Kendrion might be confronted with in relation to the company's strategic objectives. All participants were also requested to add additional potential risks based on their own experience and expertise. Each risk was scored on perceived likelihood, impact and Kendrion's vulnerability. Based on a multiplication of the scores and an evaluation per risk, the top ten risks per participant was calculated. This initial result of the survey was discussed with the Audit Committee and business unit Management Teams based on their experience and professional judgment in order to establish the main risks for Kendrion. The final results were extensively discussed with the Supervisory Board. The risk assessment is evaluated at periodic intervals in terms of relevance and mitigating actions.

Operational risk management

Kendrion's companies make active use of quality systems designed to improve its processes. Virtually all companies have been awarded ISO certification, and possess the relevant safety and quality certificates.

Financial reporting risk management

The controllers' duties include the management of financial reporting risks. Pursuant to this duty the controllers periodically monitor the organisation's implementation of and compliance with control measures. Kendrion has also implemented corporate guidelines that specify the monthly closing procedures and the controls to be performed.
Kendrion has an internal audit programme (KiC: Kendrion-in-Control) to determine the effectiveness of Kendrion's control framework. Companies with an annual revenue of more than EUR 15 million are audited at least once a year. Companies with annual revenue of less than EUR 15 million are audited at least once every two years. The internal audits encompass the revenue and accounts receivable, the purchases and accounts payable, inventories, fixed assets, human resources and (tax) compliance reporting cycles.
The internal audits also include procedures relating to fraud risks.

Compliance objectives

Kendrion operates in various jurisdictions and is committed to complying with all applicable laws and regulations in these jurisdictions. The responsibility for compliance rests with local management. To ensure that the company's conduct is in compliance with the applicable laws and regulations in the various jurisdictions and in line with stakeholders' expectations, Kendrion has adopted a Global Legal Compliance and Governance Framework. The Global Legal Compliance and Governance Framework is supported by a range of global procedures and policies that need to be applied at all times in the course of conducting business.

The Global Legal Compliance and Governance Framework includes the performance of regular internal legal audits at the operating companies. The global policies can be found on Kendrion's website (www.kendrion.com).

To manage and mitigate the risk of non-compliance, Kendrion also uses external specialists for designated compliance areas and obtain advice from external specialists to acquire timely information about the latest developments in laws and regulations.

Strategic and business risks

Kendrion's strategic and business risks identified are reviewed below. The most important risks selected based on the final outcome of the risk management survey are:

1. Pressure from large customers and customer dependency;
2. Increased competition;
3. Non-performing Information Systems and cyber security;
4. Technological substitution;
5. Attraction and retention of qualified staff;
6. Future product portfolio, including impact of megatrends;
7. Volatile economic conditions.

These risks are associated with Kendrion's strategic objectives and could impact these objectives as follows:

	Expected organic growth 5%	EBITA margin 10% as from end 2018	Dividend 35-50% of net profit	Accelerate growth after 2018
Pressure from large customers and customer dependency	•	•		•
Increased competition	•	•		•
Information Systems and cyber security	•	•		
Technological substitution	•	•		•
Attraction and retention of qualified staff	•	•		
Future product portfolio	•	•		•
Volatile economic conditions	•	•	•	•

Pressure from large customers and customer dependency
Kendrion has a wide range of customers in various markets and, consequently, the company's dependency on a small number of large customers is relatively low. Customer concentration in Automotive is higher than in Industrial; however, in the past two years, these risks have also been ranked higher by the industrial business units. Losing one of the large customers in Automotive would have a high impact and, in the absence of compensatory measures, would be detrimental to Kendrion's growth objective and profitability. The likelihood of this happening is assessed as low to moderate as Kendrion is a technologically advanced player which offers tailor-made customer solutions whose development times and costs are usually high. Kendrion endeavours to minimise its vulnerability by ensuring that single customers do not normally generate more than 5% of Kendrion's total revenues. Three customers (Volkswagen Group, Thyssenkrupp Bilstein and Daimler) each generate more than 5% of the consolidated revenues. Apart from the risks related to large customer accounts, large customers provide opportunities for accelerating (international) growth. It is also easier to justify R&D efforts and investments for larger projects.

Kendrion's main response to this risk is to actively pursue the reduction of single customer dependency by securing projects from other large customers. Kendrion has been successful in this respect during recent years which is evidenced by the changes in the company's large customers' share in consolidated revenue.

Increased competition and technological substitution
Kendrion faces competition from peers, in some cases from competing technologies and on some occasions also from (potential) customers. If Kendrion were to lose its competitive edge in relation to these parties and competing technologies, it would lessen Kendrion's ability to achieve its profitability and growth targets. Furthermore, Kendrion could become unable to offer its markets or customers the solutions they need, due to the company's inability to meet customer requirements. This is particularly important for Automotive. The impact on organic growth and profitability could be significant, the likelihood and vulnerability are moderate. In view of the pressure imposed on prices in this competitive market, especially high technological solutions are essential to realise opportunities for profitability.

The company carries out innovative projects in close consultation with its customers, an approach which Kendrion also perceives as contributing to the company's provision of added value. However, new technologies and innovations in the market environment could result in the imposition of changed requirements on Kendrion's products and operations. Although this would offer the company opportunities it could also result in the risk of being unable to meet the requirements or lagging in developing new solutions. Kendrion uses a number of tools to strengthen innovative development in its operations.

Kendrion's strategy to localise production as much as is feasible reduces its vulnerability to risks from competitive shifts resulting from exchange rate movements and changes in export or import restrictions. Although Kendrion's main focus is on technological leadership, it also actively manages the cost price by exploiting low-cost production opportunities within the group as well as exploring alternative use of materials and sources.

Non-performing Information Systems (IS) and cyber security
Inadequate IS (including the infrastructure) could have a significant impact on the company's business processes and, consequently, the results. The likelihood and vulnerability are low to moderate as a range of mitigating actions have been taken.

The major IS risks include the risk of faults in IS operations, interruptions, loss of data, unauthorised system access and other events as a result of insufficient cyber security. Information Systems are of importance to Kendrion, both in terms of the risks and business support. Kendrion's Executive Board, in particular, the CFO bears the overall IS responsibility. Kendrion has implemented a corporate IS policy and strategy that governs:

- The arrangements for IS decision-making including which decisions can be made at which level (central or local);
- IT governance for system and data responsibility (master data management);
- The arrangements for sourcing IS products and services for operating companies;
- The requirements to be met by the IS organisation in serving its internal customers;
- Periodical external information security audits;
- The measures to mitigate risks, such as access security programmes, equipment backup and recovery, change management procedures, etc.;
- The development of solutions for customer requirements (such as EDI) and the integration of suppliers in the supply chain for Kendrion's processes (supplier portals).

The implementation of new software, servers and network systems can pose interruption risks that can in turn pose major consequential risks (loss of orders, customers, or the company's reputation etc.). These implementations include:

- An adequate governance structure throughout the entire project;
- Thorough preparation;
- Balanced selection of financially strong suppliers;
- Milestones and extensive cutover planning and reviews;
- Audits for important go/no-go decisions;
- Business case analysis – internal and external (benchmark against other companies);
- End user acceptance and training.

Infrastructure – Operating companies are supported by the group's central IT department in Villingen, Germany. This department sets and coordinates the service level agreements with suppliers such as application and network providers, security providers, maintenance companies and suppliers of hardware and networks for the entire group. Kendrion works with highly skilled IT staff and reputable external and international IT suppliers. The servers are well protected against outsiders, with firewall and unauthorised-access control. Appropriate procedures have also been implemented for regular backups and disaster recovery of the data.

Software application portfolio – Operating companies use a standardised ERP system, Microsoft Operating Systems (OS) and applications and software for specific applications such as project management. The software is stable and Kendrion has sufficient knowledge required for user support.

ERP implementations and upgrades always introduce risk of business interruption. Kendrion has implemented measures to minimise these risks by strict and high-level governance that also extends to project management. In 2016, Kendrion's Executive Board decided to implement a global upgrade of the standardised ERP system. The migration to this upgrade was successfully completed as scheduled in the first quarter of 2017.

Attraction and retention of qualified staff
People are Kendrion's most important resource. A lack of skilled staff could impact most of the Kendrion's strategic objectives. The likelihood and vulnerability are moderate to high and, consequently, this is an important area for attention. Kendrion's required know-how is highly specific and requires on-the-job-training.

Mitigating actions include:

- The Kendrion Leadership & Performance Programme for senior management at the Rotterdam School of Management, which provides high-quality management training;
- The HIPO programme for high potentials (see page 56);
- Apprentice programmes at several companies;
- Regular contact with relevant education institutes;
- Various in house training programmes;
- Health & safety programmes, good labour conditions and staff satisfaction surveys, which are also part of the CSR Programme 'Taking Responsibility'.

ACTIVE DAMPER TECHNOLOGY IN CARS

Product: Actuators for shock absorber systems.

Customer: Tier 1 suppliers for active damping systems.

Kendrion's solution: The high-precision shock absorber actuators are used for various purposes, including proportional control of compression and rebound in active damper systems. The valve controls both the extension phase – the force that ensues when the wheel rebounds – and the compression phase. Within a few milliseconds, the damping force is adjusted individually according to the actual quality of the road's surface. This enhances both the safety and comfort of the ride by stabilising the car's body.

Added value: The hydraulic actuators continuously adjust the damping force in the shock absorber and ensure the perfect combination of safe driving, comfort and dynamics.

Kendrion also initiated the implementation of a new Succession Planning tool for Kendrion's top management. The implementation of this tool was finalised in the course of 2017.

Future product portfolio, including impact of megatrends
A focus on products that ultimately prove to be unsuccessful and a failure to respond adequately to market disruptions and to the impact of megatrends may in the longer term lead to stagnation and even a decline of market share and financial performance.

The mitigating measures relating to the risks 'Increased competition' and 'Technical substitution' also apply to this risk. In addition to Kendrion's innovation activities, M&A can provide further support in ensuring an adequate future product portfolio and technology base.

Volatile economic conditions
Deteriorating economic conditions could be detrimental to Kendrion's financial results and the company's ability to achieve its strategic goals. The likelihood is significant and vulnerability is moderate to low. Kendrion has a flexible organisation to enable the company to 'breathe' with the economic tides. Flexibility not only relates to working with temporary staff and focusing on the reduction of variable operating expenses, it also includes the ability to communicate up-to-date financial information efficiently to decision-makers throughout the organisation, make justifiable insourcing and outsourcing decisions, adjust supplier contracts, implement performance-dependent employee benefits, work with flexible hour contracts and make use of opportunities for the reduction of working hours in specific countries.

Kendrion periodically carries out sensitivity analyses to review the relationship between the decrease in revenue and the operating result. These analyses are performed on the basis of a 'top-down' approach with input from the business units.

Furthermore, Kendrion has a solid financial position and sufficient financial resources to continue its investment in growth, both in terms of competent staff and appropriate production equipment. All accounts receivable departments and purchasing departments devote specific attention to the financial position of the company's customers and suppliers.

Other important risks

Strategic	Operational	Financial
Project management	Commodity markets	Treasury
Intellectual property	Product liability	Tax
	Environmental liabilities	

Strategic risks

Project management
Adequate project management is essential if new products are to enter the production phase with success, and the risks associated with inadequate project management can exert a significant effect on the results.

Customers request the company to develop products complying with specific functional requirements that can, on occasion, come close to the limits of the technologically achievable. Project teams and the requisite disciplines assess the feasibility, since an incorrect estimation of the technical feasibility can result in the loss of the project. In addition, the risk that Kendrion's engineers succeed in developing a technologically acceptable solution, but that the customer nevertheless decides not to proceed with Kendrion also needs to be managed. In order to avoid such circumstances, Kendrion is continually aiming for sole suppliership. In general, the majority of the development costs are borne by the customer, either in instalments during the development phase or as part of the selling price per unit.

Intellectual Property (IP)

The technological know-how Kendrion has accrued regularly results in inventions that can be utilised to improve existing products or develop new high-quality products which in turn enable the company to obtain an edge on the competition. There is a risk of this know-how ending up in the hands of the competition, which could ultimately put Kendrion's leading position in jeopardy.

Kendrion mitigates this risk by the strict implementation of its IP policy. An important element of this policy is that Kendrion applies for a patent for each of the company's most important technological innovations.

In other instances the know-how acquired from projects for specific customers can be protected by concluding confidentiality agreements with the relevant customers. For this reason confidentiality agreements may also be concluded with Kendrion developers. Kendrion protects itself from the risk of infringing patents itself by cooperating with a specialised patent agency. This agency carries out studies of potential infringements of Kendrion's rights by third parties and vice versa.

Operational risks

Commodity markets

Kendrion's results could suffer from the reduced availability of raw materials and fluctuations in their price. Steel and copper are Kendrion's most important raw materials, followed by permanent magnets. Raw materials are purchased from reputable suppliers. Steel is Kendrion's number-one raw material, although a large proportion of it is contained in purchased components such as turning parts. Where feasible, Kendrion concludes fixed-price arrangements with steel suppliers. These prices also govern a large number of Kendrion's component suppliers. For copper, when the copper price risk is not passed on to the customer, Kendrion usually fixes the purchase price for the next quarters on a rolling basis. Kendrion closely monitors developments in prices for permanent magnets. The agreements Kendrion has concluded with the majority of customers who buy components containing permanent magnets provide for automatic price adjustments based on movements in the price of permanent magnets.

As far as is feasible, Kendrion actively endeavours to increase the number of alternative sources for its most important raw materials. Obviously, Kendrion aims to minimise the effects of price fluctuations on the group's results. Raw materials are purchased separately by each business unit on the basis of their individual requirements but in accordance with the group policy reviewed periodically to exploit knowledge across business units and economies of scale.

Product liability

Claims under product liability can be detrimental to Kendrion's operations and operating results due to the resultant damage to the company's reputation. In addition to all quality requirements and procedures, Kendrion has taken out liability insurance at group level for its operating companies to reduce the financial risks arising from possible claims under product liability. The amount and scope of the cover are comparable to those of other companies in Kendrion's sectors and is benchmarked periodically. Kendrion also aims to limit the group's liability exposure by employing up-to-date general terms and conditions and mandatory reviews of material or long-term contracts by legal advisors.

Environmental liabilities

The nature of Kendrion's operations and business are such that they give cause to limited environmental risks. Most Kendrion companies have been awarded ISO 14001 certification.

Financial risks

Treasury

Please refer to pages 123 and following of the financial statements for an outline of Kendrion's financial market risks and the policy to mitigate these risks or their impact.

Tax

Kendrion's operating companies have been granted a high degree of autonomy. In most countries the responsibility for accurate tax returns has been assigned to the local management, who receive assistance from reputable local tax consultants. Kendrion carries out an annual inventory at corporate level, in close collaboration with renowned international tax consultants, to assess whether fiscal developments could have an effect on the company's subsidiaries. Corporate reviews of the tax expenses and tax positions of the company's subsidiaries are carried out once a quarter. Kendrion has developed and implemented a tax compliance audit programme. This programme serves as the basis for reviews and assessments of the operating companies' compliance with the regulations governing a variety of taxes. The tax compliance audit programme has been incorporated in the internal audit programme.

Kendrion strongly believes that pursuing a transparent tax policy is a part of doing good business. Kendrion's aim is to manage tax risks effectively and to comply with all applicable rules, regulations and disclosure requirements. The business is leading in setting up international structures: we declare profits and we pay tax in the jurisdictions in which the economic activity occurs. Our tax planning strategy is based on the spirit of the law. This means that we do not seek to avoid taxes through structures in tax haven jurisdictions, we strive to pay our fair share of tax in the countries in which we operate, we aim at filing accurate and timely tax returns and we strive to maintain strong and transparent relationships with tax authorities in the various countries. These values have been formalised in the Kendrion Group tax policy, which is distributed to all operating companies and is updated periodically.

Results from and shortcomings revealed by the internal audit programme (KiC)

The design of Kendrion's internal audit programme, the transparent internal financial reporting system, a culture which promotes transparency and the involvement of Group Controllers at Zeist, the Netherlands, all facilitate Kendrion's maintenance and improvement of the integrity and effectiveness of its internal control and financial reporting systems.

Group companies were visited in 2017 to determine compliance with Kendrion's control framework. All internal audits are supervised by the Group Controllers in Zeist, the Netherlands, to guarantee the independence of the audits conducted. The internal audit programme and audit scope are reviewed at periodic intervals by the Group Controllers in Zeist, the Netherlands and improved as needed on the basis of recent developments and new requirements.

In 2017, the internal audits covered more than 90% of the value of the relevant reporting cycles. The overall results of the audits conducted in 2017 were satisfactory. The limited number of control deficiencies revealed by the 2016 audits had been addressed, with remediation completed or in progress. This conclusion is in line with the Management Letter, in which the external auditors reported a limited number of findings and no findings which qualified as significant.

In control statement

Based on the approach described above, the Executive Board is of the opinion that, to the best of its knowledge:

- the Report of the Executive Board provides sufficient insights into the effectiveness of the risk management and internal control systems;
- the risk management and internal control systems provide reasonable assurance that the financial reporting, including tax, does not contain any material inaccuracies;
- it is justified that the financial reporting is prepared on a going concern basis; and
- the Report of the Executive Board states those material risks and uncertainties that are relevant to the expectation of Kendrion's continuity for the twelve-month period after the date of the Report of the Executive Board.

Properly designed and implemented risk management and internal control systems significantly reduce, but cannot fully eliminate, the possibility of human errors, poor judgement, deliberate circumvention of controls, fraud or infringements of laws or regulations, or the occurrence of unforeseeable circumstances. Another circumstance considered within risk management is that efforts related to risk management and internal control systems should be balanced with the costs of implementation and maintenance.

Kendrion N.V. (hereinafter 'Kendrion') is a public limited liability company incorporated under the laws of the Netherlands, with its corporate seat in Zeist, the Netherlands. For details regarding Kendrion's share capital, reference is made to section 'Share and shareholder information' on pages 16-18.

Kendrion, as the ultimate parent company, holds all the shares of Kendrion Finance B.V., a private limited liability company incorporated under the laws of the Netherlands, with its corporate seat in Zeist, the Netherlands. Kendrion Finance B.V., directly or indirectly, holds the shares in all of Kendrion's operating companies. All operating companies are, directly or indirectly, wholly-owned subsidiaries. Kendrion is not subject to the large company structure regime and does not have a works council. Reference is made to section 'Human Resources' on pages 54-56 for information about works councils and employee representation established at certain of Kendrion's operating companies.

Corporate governance within Kendrion is based on statutory requirements applicable to public limited liability companies in the Netherlands as well as Kendrion's articles of association. Kendrion's articles of association are published on its website www.kendrion.com.

Kendrion has pursued a consistent policy to improve and – as appropriate – adjust its governance structure in line with the Dutch Corporate Governance Code as amended by the Corporate Governance Code Monitoring Committee in 2016 (the 'Code'). A sound and transparent system of checks and balances within Kendrion, including effective risk management and internal control, is fundamental to an effective corporate governance structure as they support better decision-making and contribute to responsible management. Kendrion therefore endorses the Code's principles and best practice provisions. However, Kendrion also subscribes to the concept that there should be a basic recognition that the corporate governance structure must be tailored to the company-specific situation and consequently that non-application of individual provisions by a company may be justified.

Executive Board

Kendrion is managed by an Executive Board, which is supervised and advised by the Supervisory Board. The Executive Board is responsible for the management and general affairs of Kendrion. Moreover, the Executive Board is responsible for compliance with all applicable laws and regulations, for risk management and for the financing of all activities and must provide the Supervisory Board with all information necessary for the exercise of its supervisory duties. Kendrion's risk management structure and regulatory environment are explained in the 'Risks and risk management' section on pages 58-66.

The Executive Board is accountable to the Supervisory Board and the General Meeting of Shareholders. Important resolutions of the Executive Board require the approval of the Supervisory Board.

With due regard to the requirement under Kendrion's articles of association that the Executive Board must consist of at least two members, the Supervisory Board determines the number of members of the Executive Board. Currently the Executive Board consists of two members.

The members of the Executive Board are appointed by the General Meeting of Shareholders upon nomination of the Supervisory Board. In compliance with provision 2.2.1 of the Code, all members of the Executive Board are appointed for a maximum term of four years and may be reappointed for a term of not more than four years at a time. Other than upon a proposal of the Supervisory Board, the members of the Executive Board are dismissed by the General Meeting of Shareholders by a resolution adopted by an absolute majority representing at least one-third of the outstanding share capital.

On 15 April 2013, the General Meeting of Shareholders appointed Mr Sonnemans as CFO. He was reappointed by the General Meeting of Shareholders on 10 April 2017 for a period of four years. On 4 November 2015, the General Meeting of Shareholders appointed Mr Van Beurden as CEO for a period of four years with effect from 1 December 2015. The members of the Executive Board satisfy the statutory requirements concerning the number of supervisory or non-executive functions that they can have with large enterprises. Reference is made to the profiles of the members of the Executive Board, which can be found on page 27.

In accordance with the Code, the severance payment for members of the Executive Board shall not exceed the annual base salary. Regardless of any internal allocation of tasks among the members, the members of the Executive Board are jointly responsible for the management and general affairs of Kendrion. This means, amongst other things, that the members of the Executive Board are responsible for developing and executing Kendrion's strategy, including the responsibility for defining a view on long-term value creation and, more specifically, defining and setting overall strategic Corporate Social Responsibility (CSR) related objectives.

In accordance with the articles of association of Kendrion, the Executive Board adopted Executive Board regulations which have been approved by the Supervisory Board. The Executive Board regulations govern the Executive Board's procedures and decision-making.

NEXT-GENERATION SPILL VALVE IN GASOLINE ENGINES

Product: Spill valve for gasoline engines.

Customer: OEMs and Tier 1 suppliers for combustion and hybrid vehicles.

Kendrion's solution: The state-of-the-art hydraulic spill valve is used to regulate the fuel flow to the high-pressure GDI pump, which supplies the rail with gasoline. The valve determines the quantity of gasoline that flows to the piston pump and therefore controls the pressure in the rail. By changing the switching time of the valve, the flow and consequently the pressure is regulated and the pump compresses only as much fuel as needed in the rail.

Added value: The valve is directly welded on the high-pressure gasoline pump and ensures a high flow rate and withstands a working pressure up to 280 bar.

Pursuant to the Executive Board regulations, a member of the Executive Board may not participate in the deliberation and decision-making process of the Executive Board concerning any subject in which a member of the Executive Board has a personal interest that conflicts with the interests of Kendrion. A member of the Executive Board shall immediately report any conflict of interest to the Chairman of the Supervisory Board. Decisions to enter into transactions in which there are conflicts of interest with a member of the Executive Board require the approval of the Supervisory Board. There were no transactions in which there was a conflict of interest with a member of the Executive Board in 2017. Kendrion does not grant loans or guarantees to Executive Board members.

Management Team

Kendrion has implemented a decentralised organisational structure. Each business unit has a number of operating companies in various jurisdictions. The individual business units have a shared strategy to deliver sustainable profitable growth through the three pillars 'Simplify, Focus, Grow' and collaborate with the various operating companies in a wide range of fields. In the operating companies, local management is responsible for ascertaining, assessing and managing risks that may affect the implementation of Kendrion's strategy.

A sound and transparent system of checks and balances is applied within the decentralised organisation, including the establishment of the Management Team. The Executive Board is responsible for and always has a decisive vote in all significant decisions concerning the strategy and direction of the operations as a whole. The Executive Board is supported by the Management Team. The Management Team is not mandated under the articles of association and acts as a consultative body to the Executive Board.

The Management Team consists of the members of the Executive Board, five Business Unit Managers, the President of Kendrion Asia, the General Counsel, the Global HR Manager and the Director Strategic Initiatives. The Management Team meets regularly and is involved in the review of the financial and operational performance of the business units on the basis of internal management information and identifies prevalent best practices.
An approval matrix is in place pursuant to which certain important decisions require the approval of the Executive Board. Members of the Management Team who are not also members of the Executive Board are regularly invited to attend Supervisory Board meetings and the Supervisory Board – often through coordination of the Chairman of the Supervisory Board – also maintains appropriate contacts with the members of the Management Team who are not also members of the Executive Board.

The members of the Executive Board, together with the other members of the Management Team, conducted an annual review of their own performance, including aspects that require further improvement. During the annual review, the Management Team considered the further encouragement of entrepreneurial and exponential thinking as a key aspect that will support Kendrion in meeting its growth targets in a sustainable and profitable way. This is also in line with the central theme of the 2017 Leadership & Performance Programme: 'understanding and improving performance'.

Supervisory Board

The Supervisory Board is charged with the supervision of the management by the Executive Board and the general performance and development of Kendrion and its affiliated enterprise. It also advises the Executive Board. In discharging its role, the Supervisory Board focuses on – among other things – the effectiveness of Kendrion's risk management and internal control systems and the integrity and quality of the financial reporting.

The specific tasks of the Supervisory Board are further described in Kendrion's articles of association and in Supervisory Board regulations. A detailed review of the Supervisory Board regulations as well as the regulations for its committees was performed in 2017, resulting in updated Supervisory Board regulations and updated regulations for its committees, which were discussed during several Supervisory Board meetings. The Supervisory Board adopted the updated Supervisory Board regulations and the regulations for its committees in January 2018. Information about the Supervisory Board's activities in 2017 can be found in the Report of the Supervisory Board on pages 21-26.

The Supervisory Board is composed in such a way that its members can operate critically and independently of each other, the Executive Board, the Management Team, and any other particular interests. Each of the Supervisory Board members has the necessary expertise, experience and background to perform his or her tasks and duties.

The Supervisory Board consists of four members. Mr Ten Hove was appointed as a member of the Supervisory Board on 19 August 2013 and elected as Chairman of the Supervisory Board. He was reappointed for a period of four years on 10 April 2017. Mrs Mestrom was appointed as a member of the Supervisory Board for a period of four years on 11 April 2016. Mr Wünsche and Mrs Van der Meijs were appointed as members of the Supervisory Board on 31 October 2016 for periods of four years and three years respectively. All members of the Supervisory Board are independent within the meaning of the Code. The members of the Supervisory Board satisfy the statutory requirements concerning the number of supervisory or non-executive functions that they can have with large enterprises. Reference is made to the profiles of the members of the Supervisory Board, which can be found in the Report of the Supervisory Board on page 19.

The members of the Supervisory Board are appointed by the General Meeting of Shareholders on the recommendation of the Supervisory Board for a period of four years. The Supervisory Board elects a Chairman from amongst its members. The Chairman chairs the meetings of the Supervisory Board and ensures the proper functioning of the Supervisory Board and its committees. The Chairman of the Supervisory Board also ensures that the Supervisory Board has proper contact with the Executive Board, the Management Team and the General Meeting of Shareholders. Furthermore the Chairman of the Supervisory Board maintains regular contact with the CEO concerning matters relating to the responsibilities of the Supervisory Board.

The members of the Supervisory Board step down by rotation pursuant to a schedule adopted by the Supervisory Board. Members of the Supervisory Board who step down can be reappointed. These reappointments take account of the manner in which the candidate performed his or her duties as a member of the Supervisory Board and best practice provision 2.2.2 of the Code regarding appointment and reappointment periods. Each member of the Supervisory Board can be dismissed by the General Meeting of Shareholders.

New members of the Supervisory Board follow an introduction programme to get sufficiently acquainted with Kendrion, its business activities as well as certain internal procedures and processes necessary for the discharge of their duties as members of the Supervisory Board. From time to time, members of the Supervisory Board make site visits to Kendrion's operating companies to ensure first-hand insight into Kendrion's business activities.

Meetings of the Supervisory Board are usually attended by the Executive Board and at times by members of the Management Team. The Supervisory Board is supported by the Company Secretary. The Company Secretary ensures that correct procedures are followed and that the statutory obligations and obligations under the articles of association are complied with. Furthermore, the Company Secretary facilitates the provision of information among the Executive Board and the Supervisory Board, and supports the Chairman of the Supervisory Board in the organisation of the affairs of the Supervisory Board.

The Supervisory Board has established two committees: an Audit Committee and an HR Committee; the latter was previously referred to as the Remuneration Committee. The committees of the Supervisory Board are responsible for preparing the decision-making of the Supervisory Board. Both committees have their own regulations, which include a description of the committee's tasks and responsibilities. The committees are chaired by a member of the Supervisory Board, but never by the Chairman of the Supervisory Board. Both committees consist of two members of the Supervisory Board. The Report of the Supervisory Board on pages 24-26 provides further details on the two committees of the Supervisory Board, including the number of meetings and main topics discussed during these meetings.

Based on the benchmark in 2016, the remuneration of the Chairman and other members of the Supervisory Board was raised in 2017 pursuant to a resolution of the General Meeting of Shareholders on 10 April 2017. Furthermore, the remuneration of the chairpersons of the Audit Committee and the HR Committee was raised and the fixed cost allowance was replaced by reimbursement of expenses actually incurred, both effective as of 2017. The section 'Remuneration policy' on pages 73-75 provides further details on the remuneration of the Supervisory Board.

The members of the Supervisory Board do not receive nor do they have any shares and rights to acquire shares in Kendrion as remuneration. Kendrion does not grant loans or guarantees to Supervisory Board members.

Pursuant to the Supervisory Board regulations, a member of the Supervisory Board may not participate in the deliberation and decision-making process concerning any subject in which a member of the Supervisory Board has a personal interest that conflicts with the interests of Kendrion. There were no transactions in which there was a conflict of interest with a member of the Supervisory Board in 2017.

Diversity

The Executive Board, the Management Team and the Supervisory Board value a diverse workforce, not only across the Kendrion organisation as a whole, but also at the level of the Executive Board, the Management Team, and the Supervisory Board. The Executive Board, the Management Team and the Supervisory Board regularly review and discuss diversity and consider setting diversity objectives, taking into account relevant developments in this area.

Under the CSR strategy for the period 2018, which was discussed with the Supervisory Board, Kendrion is committed to further define its approach towards diversity and to further define its diversity strategy and objectives directed at maintaining, and, where needed, improving a healthy and balanced mix of gender, skills, nationality, age, background and other factors. The main objective of Kendrion's approach is a clear commitment to fostering a diverse and inclusive workforce at all levels, including the level of the Executive Board, the Management Team and the Supervisory Board. This is supported through commitments and objectives such as: recognising, valuing and respecting differences; maintaining a flexible working environment that supports effective contributions from all employees; preventing and eliminating discrimination in the workplace, and ensuring that internal policies and processes are aligned with Kendrion's diversity objectives and commitments. Anti-discrimination officers have been appointed in some of the Kendrion operating companies. No reports of incidents of discrimination were submitted in 2017. The Executive Board and the Management Team are responsible for upholding and promoting Kendrion's diversity objectives and commitments, and evaluating and reporting on the effectiveness of Kendrion's approach towards diversity. The Supervisory Board is included in the design of Kendrion's diversity strategy and informed about its effectiveness.

The composition of the Supervisory Board reflects balanced participation of two men and two women within the meaning of article 2:66 of the Dutch Civil Code. The Executive Board currently does not reflect this gender balance, and consists of two men. The Management Team consists of a healthy mix of skills, nationality, age, background and other relevant factors. Gender diversity in the Management Team improved in 2017.

Kendrion believes it is making progress in developing initiatives enhancing diversity, and is committed to making an effort to continue developing diversity-stimulating initiatives and to give appropriate consideration to diversity in the nomination and appointment process with regard to possible future vacancies in the Executive Board, the Management Team and the Supervisory Board, while taking into account the overall profile and selection criteria for the appointment of suitable candidates.

The section 'Corporate Social Responsibility' on pages 41-57 provides more information about employee diversity across the Kendrion organisation as a whole, and describes the approach towards diversity as part of the Taking Responsibility programme – which will be further rolled out within the Kendrion organisation in the course of 2018 – and the importance Kendrion attaches to the concept of 'diversity and inclusion'.

General Meeting of Shareholders

At least once a year, Kendrion convenes an annual General Meeting of Shareholders. Meetings are convened by the Executive Board and/or Supervisory Board. Meetings can also be convened at the request of shareholders jointly representing at least 10% of Kendrion's outstanding share capital if authorised by a competent Dutch court. Shareholders who hold at least 3% of the outstanding share capital have the right to propose an item for the agenda. Kendrion will include the item on the agenda for the General Meeting of Shareholders if it has received the substantiated proposal or draft resolution, in writing, at least sixty days prior to the date of the General Meeting of Shareholders. Each shareholder is entitled to attend General Meetings of Shareholders in person or be represented by written proxy and exercise voting rights in accordance with the provisions of the articles of association.

Each outstanding share entitles the holder to one vote. Resolutions are adopted by absolute majority of the votes cast, unless the articles of association or applicable law provide otherwise.

HEAVY DUTY POWER TRANSMISSIONS IN TUGBOATS

Product: Pneumatic brakes and clutches for tugboats.

Customer: Schottel is one of the world's leading manufacturers of propulsion and steering systems for ships and offshore applications.

Kendrion's solution: Kendrion offers more than fifty years' experience, with a focus on supplying state-of-the-art clutches and brake solutions for heavy duty power transmission in applications such as tugboats.

Added value: Providing the highest reliability in power transmission in harsh and sometimes extreme conditions with the lowest total life cycle cost.

Shareholders representing 54.8% of the total outstanding share capital attended or were represented at the General Meeting of Shareholders held on 10 April 2017.

A resolution to amend the articles of association may only be adopted by the General Meeting of Shareholders upon the proposal of the Executive Board subject to the approval of the Supervisory Board. A resolution to amend the articles of association can only be adopted by an absolute majority of the votes cast during the General Meeting of Shareholders.

More information about the authority of the General Meeting of Shareholders and the articles of association can be found on Kendrion's website www.kendrion.com.

Relations with stakeholders

Kendrion values the relationship with its shareholders and other stakeholders, and endorses the concept of transparent exchange of information with its shareholders. The foregoing is also supported by the 'Policy for (bilateral) contact with shareholders' which can be found on Kendrion's website www.kendrion.com.

Special provisions relating to shares

Unless indicated otherwise, there are no restrictions on the transfer of shares, the exercise of voting rights or the term for exercising those rights, and there are no special controlling rights attached to shares. On 10 April 2017, the General Meeting of Shareholders granted the Executive Board the authority to: (i) subject to the prior approval of the Supervisory Board, issue shares or grant rights to acquire shares and restrict or suspend pre-emptive rights, in each case for a period of eighteen months (i.e. until 10 October 2018); (ii) acquire shares in Kendrion on NYSE Euronext Amsterdam in accordance with the articles of association.

Auditor and internal audit functions

The external auditor, Deloitte Accountants B.V., was appointed for the financial years 2015 through 2017 by the General Meeting of Shareholders on 13 April 2015. The General Meeting of Shareholders may put questions to the external auditor with respect to the external auditor's opinion on the financial statements. The external auditor shall therefore attend and be entitled to address the General Meeting of Shareholders. The design of Kendrion's internal audit programme (Kendrion in Control) contributes to the maintenance and improvement of the integrity and effectiveness of the internal control and financial reporting systems and includes the performance of internal audits to determine the extent to which Kendrion's group companies act in compliance with Kendrion's control framework. For further details about Kendrion's internal audit programme and control framework, reference is made to the section 'Risks and risk management' on pages 58-66.

The Audit Committee of the Supervisory Board is involved in the design of the internal audit programme and is informed about the main findings of the internal audits conducted. For further details about the Audit Committee and the performance of its duties, reference is made to the Report of the Supervisory Board on pages 24 and 25.

For the management statement of the Executive Board which is required pursuant to article 5:25c of the Financial Supervision Act (*Wet op het Financieel Toezicht*), reference is made to the Report of the Executive Board on page 40.

Compliance with the Dutch Corporate Governance Code

Kendrion applied the principles and best practice provisions of the Code, except for the following departure, for which the rationale is described below:

Principle 3.4: The precise criteria for the variable remuneration of the Executive Board will not be publicly disclosed, since Kendrion is of the opinion that disclosure of the relevant performance criteria is undesirable from a competitive and market positioning perspective.

The Code can be found at the website of the Corporate Governance Code Monitoring Committee (www.mccg.nl).

Agreements in the meaning of the Decree for the implementation of article 10 of the Takeover Directive (*Besluit artikel 10 overnamerichtlijn*)
The credit facility of Kendrion N.V. includes a 'change of control' provision. An early repayment obligation is triggered if a party acquires more than half of Kendrion's issued share capital or voting rights.

Corporate Governance statement
This section 'Corporate Governance' and the section 'Share and shareholder information' on pages 16-18 include the information referred to in the Decree for the implementation of article 10 of the Takeover Directive. In addition, this section 'Corporate Governance' in combination with the section 'Risks and risk management' on pages 58-66 and the section 'Report of the Supervisory Board' on pages 21-26 can be regarded as the Corporate Governance Statement required pursuant to the Decree on the contents of the management report (*Besluit inhoud bestuursverslag*).

Taxes

Kendrion strongly believes that pursuing a transparent and honest tax policy is an important part of doing business. This is in line with the group's Code of Conduct. In addition, there is a need to balance the interests of all relevant stakeholders, including customers, local communities, governmental institutions, and shareholders. In 2017, Kendrion reviewed its existing tax policy and tax compliance and control framework and combined this in one Group tax policy applicable to all operating companies. The Group tax policy was discussed with the Audit Committee, to ensure that the interests of all relevant stakeholders were properly reflected in the policy. The Group tax policy also provides guidelines to the relevant employees on how to deal with tax dilemmas and whom to consult in case of any tax dilemmas.

Tax payments can contribute to local development. Kendrion not only pays a substantial amount of corporate income tax in the countries where it does business but is also subject to several other taxes such as VAT, pay-as-you-earn tax deductions (withholding tax), payroll taxes and property taxes. Kendrion believes it has an obligation to pay the amount of tax legally due in any territory.

At the same time, it is in the interest of the company's continuity and its financial results to optimise its tax position. This too is part of sound business operations. Kendrion also has a responsibility in this respect to its shareholders to enhance shareholder value. The commercial needs of Kendrion, however, remain paramount and all tax planning is undertaken in this context. All transactions must have a business purpose and/or commercial rationale: 'tax follows business'. In addition, consideration is also given to Kendrion's reputation and to its corporate and social responsibilities.

Another important aspect of Kendrion's tax policy is to effectively manage risk and to comply with both the letter and the spirit of all applicable tax laws, rules, regulations and disclosure requirements. Kendrion makes use of the services of accredited tax advisers at both local and group levels and has included tax compliance in its internal audit programme. In cases where (the interpretation of) the tax law is unclear, the optimal and legally most defensible position is taken. If necessary and feasible, tax authorities are consulted in advance for additional certainty. Kendrion's aim in this regard is to be open and transparent towards all authorities and to act with complete integrity. Compliance with all anti-bribery legislation is safeguarded and is part of Kendrion's internal training programme. Kendrion's tax policy is discussed with the Audit Committee of the Supervisory Board from time to time.

Transactions conducted between group companies located in different countries are conducted in line with the OECD Guidelines for Multinational Enterprises and other local transfer-pricing regulations. The company uses the Master File concept for transfer-pricing purposes to ensure that coherent and up-to-date principles are applied.

Kendrion is aware of the ongoing OECD BEPS developments in areas including treaty abuse, transfer pricing and country-by-country reporting. As Kendrion's tax position corresponds to the geographical spread of the operations and as no aggressive tax structures are employed involving the movement of funds through secrecy jurisdictions (tax havens), the company believes that the impact of these developments is limited. Furthermore, even though Kendrion understands the tendency to use country-by-country reporting to gain more insight into local tax contributions, it has been decided, with a view to overall competitiveness, not to introduce this particular kind of reporting at this stage.

More information about taxes can be found on pages 38, 110-112 and 135 of this Report.

In 2017, Kendrion was given the no. 3 ranking in the Dutch Tax Transparency benchmark for small cap companies and ranked no. 6 among the 76 listed companies included in the benchmark.

General

Kendrion's remuneration policy for the Executive Board was proposed by the Supervisory Board and – in accordance with the articles of association – adopted by the General Meeting of Shareholders on 4 November 2015.

The remuneration report, which is published on the company's website, explains the policy for the remuneration of the Executive Board and the Supervisory Board. The remuneration report also provides information about the remuneration that was actually paid over 2017. Information about the remuneration received by the individual members of the Executive Board and the Supervisory Board is also enclosed in the financial statements (pages 136 and 137, 145 and 146).

The policy for the remuneration of the members of the Executive Board is based on the allocation of remuneration of an amount and structure such that qualified and expert executives can be recruited. The policy is also challenging to such an extent that it motivates the members of the Executive Board and, when they exhibit an appropriate performance, ensures they can be retained in the longer term. The composition of the remuneration package promotes the achievement of Kendrion's short and long-term objectives. The current remuneration policy provides for a fixed component and a variable component, as well as a pension scheme and a number of additional benefits.

The Supervisory Board possesses discretionary powers for the downward or upward adjustment of the total remuneration should the variable remuneration system result in unreasonable and inequitable remuneration. In addition, when so requested by the Supervisory Board, the variable component of the remuneration adopted in the past two years must be repaid in part or in full should it transpire that this was unjustifiably awarded on the basis of incorrect (financial) information.

The Supervisory Board periodically tests the package to verify that it is in line with the company's objectives and the market on the basis of information supplied by external experts. As recommended by the HR Committee of the Supervisory Board in 2017, the Supervisory Board proposes to amend the current remuneration policy for the Executive Board as of annual periods beginning on or after 1 January 2018 in order to reduce complexity of the remuneration policy, whilst – to the extent possible and reasonable – maintaining the overall value of the remuneration packages of members of the Executive Board. The proposed amendments to the remuneration policy were designed with the support of an external specialised consulting firm. The HR Committee conducted a scenario analysis in the context of the design of the proposed amendments to the remuneration policy.

Fixed remuneration

The members of the Executive Board receive a fixed remuneration in line with the current remuneration policy.

Variable remuneration

The variable remuneration is intended to promote the Executive Board members' attention to the development of the company, sustainable growth and the value of the share. The variable remuneration is appropriate in relation to the fixed remuneration. The Supervisory Board determines the variable remuneration for the individual members of the Executive Board on the basis of their performance and results as compared to the agreed performance criteria.

A variable bonus for the Executive Board members shall be awarded each year that promotes the achievement of Kendrion's short and long-term objectives. The annual variable remuneration for on target performance amounts to 40% of the gross fixed remuneration of the CEO and 35% of the gross fixed remuneration of the CFO, with a maximum of 60% of the gross fixed remuneration for the CEO and 50% of the gross fixed remuneration for the CFO. 60% of the bonus criteria consists of financial performance criteria (net profit, ROS, ROI, organic growth and free cash flow) and 40% consists of individual (non-financial) performance criteria.

One third of the gross amount of the variable remuneration is paid in cash. The remaining two thirds of the gross variable remuneration is paid through a conditional award of shares. The award of the shares becomes unconditional after three years (including the relevant year in which the performance is assessed) if the CEO and CFO are still in office and the Supervisory Board is of the opinion that there are no exceptional circumstances that would render the unconditional award unreasonable. The award of the shares is withdrawn in the event that the relevant member of the Executive Board leaves Kendrion as a 'bad leaver' during the three-year vesting period. The Supervisory Board possesses discretionary powers to refrain from the full issue of the shares in the event that the relevant member of the Executive Board leaves the company as a 'good leaver' in the vesting period (for example, on retirement or in the event of an occupational disability) when the full issue of the shares would be unreasonable under the circumstances.

Once the award of the shares has become unconditional after the expiry of the three-year vesting period they must be retained for a minimum of two years unless the relevant member of the Executive Board terminates his/her term of office or the term of office is terminated during this period. The members of the Executive Board may sell such a portion of the shares as it is needed to pay the personal income taxes as a consequence of the unconditional award of shares ('sell to cover') within the two-year holding period.

The aforementioned financial and individual performance criteria are determined for each full year at the beginning of the relevant financial year.

The variable remuneration policy is supplemented by a share match. As stated above, two thirds of the gross variable remuneration is paid through a conditional award of shares. Depending on the achievement of the long-term performance criteria, Kendrion will increase the number of shares awarded pursuant to the above by 100% net (a matching ratio of 1:1). The performance criteria are the relative Total Shareholders Return (TSR), the absolute TSR (dividend ratio and share price development) and a group of sustainability criteria. The relative TSR and absolute TSR carry a weighting of 30% each, and the sustainability criteria carry a weighting of 40%. The performance period shall be three years, which begins at the time of the award of the annual variable remuneration. Consequently, the award of shares under the share match is made after a period of three years. The shares awarded pursuant to the share match are governed by a holding period of two years, which begins at the time of the award.

The relative TSR performance criterion for the share match is achieved when Kendrion's TSR score is higher than the average of the AScX and the German Small Cap Index, the SDAX. The absolute TSR criterion is achieved if the increase in the share price together with the dividends in the three-year period concerned is reasonable according to the Supervisory Board, taking into account all relevant circumstances. The sustainability criteria are (i) energy/CO_2 reduction, (ii) waste & recycling (sustainable business processes), (iii) employee satisfaction and (iv) management development / succession planning. Equal weighting is allocated to each of these sustainability criteria.

Pensions and risk premium

Kendrion bears the cost of the contributions for the old-age pension and risk premiums for partner pension and disability of the members of the Executive Board and makes a maximum of EUR 75,000 available annually for this. No schemes have been agreed for the (voluntary) early retirement of the members of the Executive Board.

Personal loans

Kendrion does not grant loans, advances or guarantees to the members of the Executive Board. No exceptional remuneration was paid to the members or former members of the Executive Board in the year under review.

Pay ratio

The Executive Board to employee pay ratio is approximately 13. This pay ratio is based on the average of the 2017 Executive Board remuneration including pensions and other expenses and the average wage costs per FTE in 2017 as disclosed on page 54.

Severance pay

In the event of termination of the contract at Kendrion's initiative, the relevant member of the Executive Board will receive a severance payment of a maximum of one year's fixed gross remuneration. Members of the Executive Board are not entitled to the severance payment if the contract is terminated due to urgent cause or serious culpability. In the event of termination of the contract at the initiative of a member of the Executive Board within one year after control in Kendrion N.V. has changed, on the grounds that continuation of the contract cannot reasonably be expected, the relevant member of the Executive Board receives an amount to be determined by the Supervisory Board as a severance payment. The payment is capped at a maximum of one year's gross fixed remuneration.

Remuneration of the Supervisory Board

The remuneration received by the members of the Supervisory Board comprises a fixed remuneration that is independent of the results of Kendrion. The General Meeting of Shareholders held on 10 April 2017 resolved that as of 1 January 2017, the annual gross fixed remuneration of the members of the Supervisory Board is as described in the table below.

Position	Annual gross fixed remuneration
Chairman of the Supervisory Board	EUR 45,000
Member of the Supervisory Board	EUR 35,000
Chairperson of the Audit Committee	EUR 6,000
Member of the Audit Committee	EUR 5,000
Chairperson of the HR Committee	EUR 6,000
Member of the HR Committee	EUR 5,000

As of 1 January 2017, the fixed cost allowance has been replaced and out-of-pocket expenses of the members of the Supervisory Board are reimbursed based on actual expenses incurred.

The remuneration of the members of the Supervisory Board is in line with the median of the peer group.

Element	Fixed	Variable	
	Base salary	Annual incentive	Long-term incentive
Way of payment	Cash	Performance related restricted shares	3-year performance related restricted shares
Performance measure	Not applicable	■ Net profit ■ ROI ■ Free cash flow ■ ROS ■ Organic growth — Total 60% ■ Non-financial individual performance, including sustainability — Total 40%	■ Relative Total Shareholders Return (compared to the average of the AScX and SDAX) — Total 30% ■ Absolute Total Shareholders Return (dividend and share price) — Total 30% ■ Sustainability (energy and CO_2 reduction, waste & recycling, employee satisfaction and management development/succession planning) — Total 40%
Pay-out at minimum performance		0%	0%
Target pay-out		CEO: 40% as % of gross fixed remuneration CFO: 35% as % of gross fixed remuneration	CEO and CFO: 100% of number of shares awarded based on annual incentive (net)
Maximum pay-out		CEO: 60% as % of gross fixed remuneration CFO: 50% as % of gross fixed remuneration	CEO and CFO: 100% of number of shares awarded based on annual incentive (net)

The economic outlook for 2018 is good. In its flagship report, known as the World Economic Outlook, the IMF put its forecast for growth in 2018 at 3.7%, slightly higher compared with 3.6% in 2017 and 3.2% in 2016. All major economies contribute to this growth expectation.

Against this backdrop, Kendrion expects its revenue to increase in 2018, driven mostly by growth in the Passenger Cars business unit. Kendrion expects investments in 2018 to exceed depreciation charges. Most of these investments relate to new projects.

Simplify, Focus, Grow

Kendrion focuses entirely on designing, producing and selling electromagnetic actuators for automotive and industrial applications. Kendrion has a leading position as a technologically advanced and innovative company with an excellent reputation for quality and reliability in Europe, the USA and Asia.

Kendrion announced its mid-term strategic plan entitled 'Simplify, Focus, Grow' in May 2016. Kendrion continues to simplify the way it does business. This will reduce costs and improve decision-making speed, which is in turn expected to improve the operating margin and profitability.

Kendrion will focus its resources and capital on those areas in which it believes it has the most opportunities for profitable growth, rather than spreading its efforts equally across its five business units.

The clarity Kendrion is gaining through simplifying and focusing its business is intended to allow organic growth of the top line in a way that will ultimately enable growth at a faster pace than Kendrion's historical average of 5%.

Due to long project lead times in Kendrion's business, the company expects organic growth to accelerate in the years beyond 2018.

Kendrion has set three clear, simple and ambitious financial goals. Firstly, deliver an EBITA margin of 10% as from the end of 2018. Secondly, maintain expected organic growth broadly in line with the average historical organic growth of 5% per annum until 2018 and finally, pay out a dividend of 35 to 50% of net profit. Kendrion has taken meaningful steps towards this target in both 2016 and 2017 and is committed to completing the transformation it announced in 2016 in 2018.

Kendrion also expects to be announcing new mid-term financial targets during the calendar year 2018.

Outlook per business unit

Industrial Magnetic Systems will start production for a number of new projects in the process automation, locking and safety markets and the logistics markets. An increasing proportion of the new projects will be realised in Kendrion's Chinese facility in Suzhou. The project portfolio furthermore consists of several key projects for the energy distribution markets.

Industrial Control Systems will ramp down two product lines in 2018 due to the scheduled end of the product life cycle. This will be compensated by launching new projects. Specifically, a new valve project for a leading supplier to the aircraft industry is expected to ramp up in 2018. Kendrion also expects sales of the new integrated safety FIO module (Fast Input Output) for process automation customers to grow in 2018. The heat controller business with Oerlikon is projected to run at a high level throughout 2018 and 2019.

Based on the strong economy as described above, Industrial Drive Systems expects another solid year driven mainly by demand for its products in China. The application of electromagnetic brakes in the OEM servo motor segment for robotics is expected to remain the strongest market and Kendrion also plans to install a new production line in Suzhou to deliver to the local Chinese market. Growth will be partly offset by the end-of-life of a large customer project.

As the trend towards hybrid and electric vehicles intensifies, the disruption of the traditional passenger car market continues. Autonomous driving, connectivity and electric mobility offer the automotive industry many opportunities and challenges. Passenger Cars therefore continues to focus on products that benefit from these changes such as its sound actuator for electric cars and its valves for smart shock absorber systems.

As a result, a further increase in turnover and efficiency is expected for Passenger Cars in 2018. Based on its strong technical competence in complex and customised product solutions, Kendrion Passenger Cars aspires to continue to actively shape new trends for the future in close collaboration with its customers.

After a year of consolidation in 2017, Commercial Vehicles is shifting its focus to set the scene for future growth. Clutches for hybrid drives, thermostat units for higher engine efficiency, portfolio expansion for hydraulics as well as further feature evolution of its pressure switch line form the cornerstones of the 2018 R&D efforts. At the same time, investment will be targeted at new segments developing new products for electrified and – especially – hybrid powertrains for commercial vehicles.

FINANCIAL STATEMENTS - CONTENTS

CONSOLIDATED STATEMENT OF FINANCIAL POSITION AT 31 DECEMBER

Note	EUR million	2017	2016
	Assets		
	Non-current assets		
1	Property, plant and equipment	90.4	85.5
2	Intangible assets	117.9	124.5
3	Other investments, including derivatives	0.2	0.4
4	Deferred tax assets	12.3	16.0
	Total non-current assets	**220.8**	**226.4**
	Current assets		
5	Inventories	57.3	52.6
	Current tax assets	1.0	1.2
6	Trade and other receivables	58.1	54.5
7	Cash and cash equivalents	7.6	12.4
	Total current assets	**124.0**	**120.7**
	Total assets	**344.8**	**347.1**

Note	EUR million	2017	2016
	Equity and liabilities		
8, 9	**Equity**		
	Share capital	27.0	26.8
	Share premium	49.6	56.4
	Reserves	84.2	80.0
	Retained earnings	19.5	14.9
	Total equity	**180.3**	**178.1**
	Liabilities		
10	Loans and borrowings	49.7	63.0
11	Employee benefits	19.1	21.4
4	Deferred tax liabilities	8.8	10.9
	Total non-current liabilities	**77.6**	**95.3**
7	Bank overdraft	11.7	2.7
10	Loans and borrowings	0.7	0.7
13	Provisions	0.8	1.2
	Current tax liabilities	1.4	0.7
14	Trade and other payables	72.3	68.4
	Total current liabilities	**86.9**	**73.7**
	Total liabilities	**164.5**	**169.0**
	Total equity and liabilities	**344.8**	**347.1**

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

Note	EUR million	2017	2016
19	Revenue	461.8	443.4
20	Other income	0.0	0.1
	Total revenue and other income	**461.8**	**443.5**
	Changes in inventories of finished goods and work in progress	(1.8)	0.5
	Raw materials and subcontracted work	242.9	230.0
21	Staff costs	134.2	132.6
	Depreciation and amortisation	23.5	24.0
16, 22	Other operating expenses	34.3	34.7
	Result before net finance costs	**28.7**	**21.7**
	Finance income	0.1	0.1
	Finance expense	(3.0)	(3.2)
23	**Net finance costs**	**(2.9)**	**(3.1)**
	Profit before income tax	**25.8**	**18.6**
24, 25	Income tax expense	(6.3)	(3.7)
	Profit for the period	**19.5**	**14.9**

Note	EUR million	2017	2016
	Other comprehensive income		
	Remeasurements of defined benefit plans*	0.6	(1.9)
	Foreign currency translation differences for foreign operations**	(7.6)	1.3
	Net change in fair value of cash flow hedges, net of income tax**	0.6	(0.2)
	Other comprehensive income for the period, net of income tax	**(6.4)**	**(0.8)**
	Total comprehensive income for the period	**13.1**	**14.1**
9	Basic earnings per share (EUR), based on weighted average	1.45	1.12
9	Basic earnings per share (EUR) based on weighted average (diluted)	1.44	1.12

* This item will never be reclassified to profit or loss.

** These items may be reclassified to profit or loss.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

EUR million	Share capital	Share premium	Translation reserve	Hedge reserve	Reserve for own shares	Other reserves	Retained earnings	Total equity
Balance at 1 January 2016	26.4	62.7	10.3	(0.1)	–	53.8	16.8	169.9
Total comprehensive income for the period								
Profit or loss	–	–	–	–	–	–	14.9	14.9
Other comprehensive income								
Remeasurements of defined benefit plans	–	–	–	–	–	(1.9)	–	(1.9)
Foreign currency translation differences for foreign operations	–	–	1.3	–	–	–	–	1.3
Net change in fair value of cash flow hedges, net of income tax	–	–	–	(0.2)	–	–	–	(0.2)
Other comprehensive income for the period, net of income tax	–	–	1.3	(0.2)	–	(1.9)	–	(0.8)
Total comprehensive income for the period	–	–	1.3	(0.2)	–	(1.9)	14.9	14.1
Transactions with owners, recorded directly in equity								
Contributions by and distributions to owners								
Issue of ordinary shares	0.4	3.8	–	–	–	–	–	4.2
Share-based payment transactions	0.0	0.2	–	–	–	0.0	–	0.2
Dividends to equity holders	–	(10.3)	–	–	–	–	–	(10.3)
Appropriation of retained earnings	–	–	–	–	–	16.8	(16.8)	–
Balance at 31 December 2016	26.8	56.4	11.6	(0.3)	–	68.7	14.9	178.1

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY (CONTINUED)

EUR million	Share capital	Share premium	Translation reserve	Hedge reserve	Reserve for own shares	Other reserves	Retained earnings	Total equity
Balance at 1 January 2017	26.8	56.4	11.6	(0.3)	–	68.7	14.9	178.1
Total comprehensive income for the period								
Profit or loss	–	–	–	–	–	–	19.5	19.5
Other comprehensive income								
Remeasurements of defined benefit plans	–	–	–	–	–	0.6	–	0.6
Foreign currency translation differences for foreign operations	–	–	(7.6)	–	–	–	–	(7.6)
Net change in fair value of cash flow hedges, net of income tax	–	–	–	0.6	–	–	–	0.6
Other comprehensive income for the period, net of income tax	–	–	(7.6)	0.6	–	0.6	–	(6.4)
Total comprehensive income for the period	–	–	(7.6)	0.6	–	0.6	19.5	13.1
Transactions with owners, recorded directly in equity								
Contributions by and distributions to owners								
Issue of ordinary shares	0.2	3.5	–	–	–	–	–	3.7
Own shares repurchased	–	–	–	–	(4.5)	–	–	(4.5)
Share-based payment transactions	0.0	0.2	–	–	–	0.2	–	0.4
Dividends to equity holders	–	(10.5)	–	–	–	–	–	(10.5)
Appropriation of retained earnings	–	–	–	–	–	14.9	(14.9)	–
Balance at 31 December 2017	27.0	49.6	4.0	0.3	(4.5)	84.4	19.5	180.3

Note	EUR million	2017	2016
	Cash flows from operating activities		
	Profit for the period	19.5	14.9
	Adjustments for:		
	Net finance costs	2.9	3.1
	Income tax expense	6.3	3.7
	Depreciation of property, plant and equipment and software	20.3	20.3
	Amortisation of other intangible assets	3.2	3.7
	Impairment of property, plant and equipment	1.0	0.5
	Share-based payments	0.3	0.2
		53.5	46.4
	Change in trade and other receivables	(4.9)	(5.7)
	Change in inventories	(6.0)	(0.4)
	Change in trade and other payables	4.7	10.2
	Change in provisions	(2.1)	0.0
		45.2	50.5
	Interest paid	(2.2)	(2.7)
	Interest received	0.1	0.2
	Tax paid	(3.8)	(3.8)
	Net cash flows from operating activities	**39.3**	**44.2**

Note	EUR million	2017	2016
	Cash flows from investing activities		
	Investments in property, plant and equipment	(24.6)	(20.9)
	Disinvestments of property, plant and equipment	0.6	0.6
	Investments in intangible fixed assets	(4.5)	(2.9)
	Disinvestments of intangible fixed assets	0.2	0.3
	(Dis)investments of other investments	(0.0)	0.0
	Net cash from investing activities	**(28.3)**	**(22.9)**
	Free cash flow	**11.0**	**21.3**
	Cash flows from financing activities		
	Repayment of borrowings (non current)	(13.3)	(6.6)
	Proceeds from borrowings (current)	0.0	0.0
	Proceeds from the issue of share capital	0.0	0.0
	Own shares bought	(4.5)	–
	Dividends paid	(6.6)	(6.1)
	Net cash from financing activities	**(24.4)**	**(12.7)**
	Change in cash and cash equivalents	(13.4)	8.6
	Cash and cash equivalents at 1 January	9.7	1.2
	Effect of exchange rate fluctuations on cash held	(0.4)	(0.1)
7	Cash and cash equivalents at 31 December	(4.1)	9.7

Reporting entity

Kendrion N.V. (the 'Company') is domiciled in the Netherlands. The Company's registered office is at Utrechtseweg 33, 3704 HA Zeist. The consolidated financial statements of the Company as at and for the year ended 31 December 2017 comprise the Company and its subsidiaries (together also referred to as the 'Group'). The Group is involved in the design, manufacture and sale of high-quality electromagnetic systems and components.

Basis of preparation

(a) Statement of compliance

The consolidated financial statements as of 31 December 2017 have been prepared in accordance with International Financial Reporting Standards (IFRS) and interpretations of the standards published by the International Accounting Standards Board (IASB) as adopted by the European Union (hereinafter referred to as EU-IFRS). The Company financial statements are part of the 2017 financial statements of Kendrion N.V.

The financial statements were authorised for issue by the Executive Board on 20 February 2018.

(b) Basis of measurement

The financial statements are presented in millions of euros, the euro also being the Group's functional currency.

The financial statements have been prepared on a historical cost basis except that:

- derivative financial instruments are stated at fair value;
- liabilities arising from cash-settled share-based payments arrangements are stated at fair value;
- the defined benefit liability is recognised as net total of plan assets and present value of the defined benefit obligations;
- the contingent consideration is stated at fair value.

The methods used to measure the fair values are disclosed in note q.

The preparation of the financial statements in accordance with EU-IFRS requires the Executive Board to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are considered reasonable in the circumstances, the results of which form the basis for making the judgements about carrying amounts of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates. The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which an estimate is revised if the revision affects only that period or in the period of the revision and future periods if the revision affects both current and future periods. Changes in estimation methods and the impact of such changes are outlined in the notes to the relevant item.

The Executive Board discussed the selection and disclosure of the critical accounting policies for financial reporting and estimates, as well as the application of these policies and estimates, with the Supervisory Board. In preparing the financial statements, the management is required under IFRS to make various judgements, estimates and assumptions that affect the implementation of policy and the amounts disclosed in relation to assets, liabilities, income and expenses. The estimates and assumptions are based on experience and factors deemed reasonable in the circumstances. Estimates and assumptions are constantly reappraised. Changes in the accounting estimates used are reflected in the period in which the estimate is changed if the change affects only that period, or in the period in which the estimate is changed and in future periods if the change affects both the reporting period and future periods.

Executive Board made critical judgements in the process of applying Group's accounting policies and that have the most significant effect on the amounts recognised in the consolidated financial statements, see notes:

- note 4 – tax losses not recognised
- note 11 – measurement of defined benefit obligations
- note 18 – contingent assets and liabilities
- note 19 – applying aggregation criteria with reference to operating segments

Executive Board made estimations concerning the future, and other key sources of estimation uncertainty at the end of the reporting period, that may have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year.

- note 1 – assessment of useful life and residual value of assets with a definite useful life
- note 2 – assessment of useful life and residual value of assets with a definite useful life
- note 2 – management forecast and growth rate of each cash-generating unit to determine whether goodwill is impaired
- note 4 – utilisation of tax losses
- note 5 – valuation of inventories
- note 11 – salary and pension growth of defined benefit obligations
- note 13 – provisions
- note 15 – valuation of financial instruments

Reference is made to those notes for steps taken by the Executive Board to make judgements, estimates and assumptions.

Significant accounting policies

The accounting policies set out below have been applied consistently to all periods presented in these consolidated financial statements and by the Group entities.

(a) Basis of consolidation

(i) Business combinations

Business combinations are accounted for using the acquisition method at the acquisition date, which is the date on which control is transferred to the Group. Control refers to the authority to govern the financial and operating policies of an entity to obtain benefits from its activities. When assessing control, the Group takes into consideration potential voting rights that are currently exercisable.

The Group measures goodwill at the acquisition date as:

- the fair value of the consideration transferred; plus
- the recognised amount of any non-controlling interests in the acquiree; plus
- if the business combination is realised in stages, the fair value of the pre-existing equity interest in the acquiree; less
- the net recognised amount (generally fair value) of the identifiable assets acquired and liabilities assumed.

If the excess is negative, a bargain purchase gain is recognised immediately in comprehensive income (hereafter also referred to as 'profit or loss'). The consideration transferred does not include amounts relating to the settlement of pre-existing relationships. Such amounts are generally recognised in profit or loss.

Transactions costs, other than those associated with the issue of debt or equity securities that the Group incurs in connection with a business combination are expensed as incurred.

Any contingent consideration payable is measured at fair value at the acquisition date. If the contingent consideration is classified as equity, then it is not remeasured and settlement is accounted for within equity. Otherwise, subsequent changes in the fair value of the contingent consideration are recognised in profit or loss.

When share-based payment awards (replacement awards) are required to be exchanged for awards held by the acquiree's employees (acquiree's awards) and relate to past services, then all or part of the amount of the acquirer's replacement awards is included when measuring the consideration transferred in the business combination. This determination is based on the market-based value of the replacement awards as compared to the market-based value of the acquiree's awards and the extent to which the replacement awards relate to past and/or future service.

(ii) Subsidiaries

Subsidiaries are entities controlled by the Company. The Company controls an entity if it is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences, until the date that control ceases. The shares of third parties in shareholders' equity and results are stated separately. The accounting policies of subsidiaries are changed, where necessary, to align them with the policies adopted by the Company.

(iii) Transactions eliminated on consolidation

Intragroup balances and transactions, as well as any unrealised gains and losses or income and expenses arising from intragroup transactions, are eliminated when preparing the consolidated financial statements.

(b) Foreign currency

(i) Foreign currency transactions

Transactions expressed in non-euro zone currencies are translated into euros at exchange rates at the date of the transaction. Monetary assets and liabilities denominated in non-euro zone currencies at the reporting date are translated into euros at the exchange rate at that date. Non-monetary assets and liabilities denominated in non-euro zone currencies that are measured at historical cost are translated at the exchange rate at the date of the transaction. Non-monetary assets and liabilities denominated in non-euro zone currencies that are measured at fair value are translated in euros at the exchange rates when the fair value was determined. Currency differences on foreign currency transactions are recognised in profit or loss, except loans considered to be part of the net investment, or qualifying cash flow hedges to the extent the hedges are effective.

(ii) Translation of foreign currency financial statements

Translation of foreign currency financial statements depends on the functional currency of the company concerned. The closing rate method is applied if the functional currency of the company is other than the euro. With this method, assets and liabilities of non-euro zone operations, including goodwill and fair value adjustments arising at the time of acquisition, are translated into euros at exchange rates at the reporting date. The income and expenses of non-euro zone operations are translated into euros at rates approximating the exchange rates at the date of the transaction. Foreign currency translation differences are recognised in other comprehensive income and accumulated in the translation reserve, which is a component of equity.

On the partial or complete sale of a foreign operation, the related amount is transferred from the translation reserve to profit or loss.

Foreign exchange gains and losses arising from a monetary item receivable from or payable to a non-euro zone operation, of which the settlement is neither planned nor likely in the foreseeable future, are considered to form part of a net investment in a non-euro zone operation and are recognised directly in equity, in the translation reserve.

(c) Property, plant and equipment

(i) Owned assets

Items of property, plant and equipment are measured at cost or assumed cost less accumulated depreciation and accumulated impairment losses (see accounting policy g). The cost includes expenditure that is directly attributable to the acquisition of the asset. The cost of self-constructed assets includes the cost of materials, direct labour, the initial estimate, where relevant, of the costs of dismantling and removing the items and reinstating the site on which they are located, a reasonable proportion of production overheads, and capitalised borrowing costs.

Where parts of an item of property, plant and equipment have different useful lives, they are accounted for as separate items of property, plant and equipment.

(ii) Leased assets

Leases under which the Group assumes substantially all the risks and rewards of ownership are classified as finance leases. Owner-occupied property acquired by way of a finance lease is stated at an amount equal to the lower of its fair value and the present value of the minimum lease payments at inception of the lease, less accumulated depreciation (see below) and impairment losses (see accounting policy g).

(iii) Subsequent costs

The cost of replacing part of an item of property, plant and equipment is recognised in the carrying amount of the item if it is probable that the future economic benefits embodied within the part will flow to the Group, and its cost can be reliably measured. The carrying amount of the replaced part is derecognised. The costs of the day-to-day servicing of property, plant and equipment are recognised as an incurred charge in profit or loss.

(iv) Depreciation

Depreciation is charged to profit or loss on a straight-line basis over the estimated useful life of each component of property, plant and equipment. Land is not depreciated.

Leased assets are depreciated over the shorter of their respective lease terms and useful lives unless it is reasonably certain that the Group will obtain ownership by the end of the lease term.

Depreciation methods, useful lives and residual values are reviewed annually.

(v) Recognition of transaction results

Gains and losses on the disposal of property, plant and equipment are accounted for in other operating income/other expenses in the statement of comprehensive income.

(d) Intangible assets

(i) Goodwill

Goodwill that arises upon acquisition of a subsidiary is included in intangible assets. For the measurement of goodwill at initial recognition, see note a.

Goodwill is carried at cost less any accumulated impairment losses. Goodwill is allocated to cash-generating units and is not amortised but is tested annually for impairment (see note g).

Negative goodwill arising on an acquisition is recognised directly in profit or loss.

(ii) Research and development

Research and development expenses comprise expenditure on research and development and expenses for customer-specific applications, prototypes and testing. Reimbursements from customers are offset against expenses. In addition, the expenses are reduced by the amount relating to the application of research results in the development of new or substantially improved products if the related activity meets the recognition criteria for internally generated intangible assets as laid down in IAS 38.

Expenditure on research activities undertaken with the prospect of gaining new scientific or technical knowledge and understanding is recognised in profit or loss as incurred.

Development activities involve a plan or design for the production of new or substantially improved products and processes. Development expenditure is capitalised only if the development costs can be measured reliably, the product or process is technically and commercially feasible, future economic benefits are probable, and the Group intends to and has sufficient resources to complete the development and to use or sell the asset. The expenditure capitalised includes the cost of materials, direct labour, overhead costs that are directly attributable to preparing the asset for its intended use, and capitalised borrowing costs. Other development expenditure is recognised in profit or loss when incurred.

Research and development expenses incurred by the Industrial activities primarily relate to pre-production prototypes or tests for products already being marketed (application engineering). These expenses do not qualify as development expenditure, but may be recognised as an intangible asset. Research and development expenses incurred by the Automotive activities are not recognised as marketable until Kendrion has been nominated as the supplier for the particular vehicle platform or model and has also successfully completed the pre-production release stages. These release stages also serve as the prerequisite for the demonstration of the technical feasibility of the product, especially in view of the stringent demands imposed on comfort and safety technology. For this reason, development costs are recognised as an asset solely on the date of Kendrion's nomination as the supplier and the completion of a specific pre-production release stage. The development is deemed to have been completed once final approval for series production has been granted. As a result, only a very few of the Automotive research and development projects meet the recognition criteria.

Capitalised development expenditure is measured at cost less accumulated amortisation and accumulated impairment losses.

(iii) Other intangible assets

Other intangible assets that are acquired by the Group and have finite useful lives are stated at cost less accumulated amortisation (see below) and accumulated impairment losses (see note g). Based on the purchase price allocation of acquisitions, intangible assets that are part of the other intangible assets and relate to, for example, valued customer relations, trade names and technologies are also recognised.

(iv) **Subsequent expenditure**

Subsequent expenditure on capitalised intangible assets is capitalised only if it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure is expensed when incurred.

(v) **Amortisation**

Amortisation is recognised in profit or loss on a straight-line basis over the estimated useful lives of the intangible assets unless such lives are indefinite. Goodwill and other intangible assets with an indefinite useful life are systematically tested for impairment at each reporting date. Other intangible assets are amortised from the date they are available for use. Amortisation methods, useful lives and residual values are reviewed at each reporting date and adjusted if appropriate.

(e) Financial instruments and other investments

Financial instruments

Non-derivative financial instruments

Non-derivative financial instruments comprise trade and other receivables, recognised interest bearing loans and borrowings, trade and other payables, cash and cash equivalents, and other non-derivative financial instruments. They are recognised as at the respective dates on which they originate.

Non-derivative financial instruments are recognised initially at fair value, less any directly attributable transaction costs. The Group derecognises a financial asset when the contractual rights to the cash flows from the asset expire, or if it transfers the rights to receive the contractual cash flows as part of a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred. Any interest in such transferred financial assets that is created or retained by the Group is recognised as a separate asset or liability. Financial assets and liabilities are offset and the net amount presented in the statement of financial position if, and only if, the Group has a legal right to offset the amounts and intends either to settle them on a net basis or to realise the asset and settle the liability simultaneously. Subsequent to initial recognition, non-derivative financial instruments are measured as described below.

Trade and other receivables

Trade and other receivables are carried at amortised cost, less impairment losses (see note g).

Recognised interest-bearing loans and borrowings

After initial recognition, interest-bearing loans and borrowings are carried at amortised cost with any difference between the initial carrying amount and the redemption amount, based on the effective interest method, taken to profit or loss over the respective terms of the loans.

Trade and other payables

Trade and other payables are carried at amortised cost.

Cash and cash equivalents

Cash and cash equivalents comprise cash and bank balances and other call deposits payable on demand. Bank overdrafts that are repayable on demand, and form an integral part of the Group's cash management, are included as a component of cash and cash equivalents in the statement of cash flows. They are measured at fair value.

Other non-derivative financial instruments

Other non-derivative financial instruments are measured at amortised cost using the effective interest method, less any impairment losses.

Derivative financial instruments, including hedge accounting

The Group holds derivative financial instruments to hedge its foreign currency and interest rate exposures.

Derivatives are initially measured at fair value, with attributable transaction costs recognised in the statement of comprehensive income when they are incurred. Subsequent to initial recognition, derivatives are carried at fair value. Any changes are taken to profit or loss, unless the instruments are designated as cash flow hedges.

Embedded derivatives are accounted for separately from the host contract. If the economic characteristics and risks of the host contract and the embedded derivative are not closely related, a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative, and the combined instrument is not measured at fair value in profit or loss. Changes in the fair value of separated embedded derivatives are recognised immediately in profit or loss. At 31 December 2017, no embedded derivatives existed.

Changes in the fair value of a derivative hedging instrument designated as a cash flow hedge are recognised in other comprehensive income and presented in the hedging reserve, a component of equity, to the extent that the hedge is effective. To the extent that the hedge is ineffective, changes are recognised immediately in profit or loss.

On initial designation of a derivative as a cash flow hedge, the Group formally documents the relationship between the hedging instrument, the hedged item and the hedged risk, including the risk management objective and strategy for undertaking the hedge transaction, together with the methods that are used to assess the effectiveness of the hedging relationship. The Group makes an assessment, both at the inception of the hedge relationship as well as on an ongoing basis, of whether the hedging instruments are expected to be highly effective in achieving offsetting of the changes in the cash flows for the hedged risks attributable to the respective hedged items, and whether the actual results of each hedge are within a range of 80-125%. Regarding a cash flow hedge for a forecasted transaction, the Group determines whether the hedged transactions are highly likely to occur and present an exposure to variations in cash flows that could ultimately affect profit or loss.

If a hedging instrument no longer meets the criteria for a cash flow hedge, expires or is sold, then hedge accounting is discontinued prospectively. The cumulative result previously included in equity is recognised in profit or loss unless it is expected that the original hedged transaction will still take place.

(f) Inventories

Inventories are measured at the lower of cost and net realisable value. Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and the estimated costs to sell. The cost of inventories of the Group is based on the weighted average cost, and includes expenditure incurred in acquiring the inventories, production or conversion costs, and other costs incurred in bringing them to their current location and condition. The cost of inventories includes an appropriate share of overheads based on normal operating capacity.

(g) Impairment

(i) Financial assets

A financial asset is assessed at each reporting date to determine whether there is any objective evidence that it is impaired. A financial asset is considered to be impaired if objective evidence indicates that one or more events have had a negative effect on the estimated future cash flows of that asset.

An impairment loss, in respect of a financial asset measured at amortised cost, is calculated as the difference between its carrying amount, and the present value of the estimated future cash flows discounted at the original effective interest rate.

Significant financial assets are tested for impairment on an individual basis. The remaining financial assets are assessed collectively in groups of assets that have similar credit risk characteristics.

All impairment losses are recognised in the consolidated statement of comprehensive income.

An impairment loss is reversed if the reversal can be related objectively to an event occurring after the impairment loss was recognised. For financial assets measured at amortised cost, the reversal is recognised in profit or loss.

(ii) Non-financial assets

The carrying amounts of the Group's non-financial assets, other than inventories and deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. For goodwill and intangible assets that have indefinite lives or that are not yet available for use, the recoverable amount is estimated at each reporting date.

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For the purpose of impairment testing, assets are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets (the 'cash-generating unit'). For the purpose of impairment testing, the goodwill acquired in a business combination is allocated to cash-generating units that are expected to benefit from the synergies of the combination.

An impairment loss is recognised if the carrying amount of an asset or its cash-generating unit exceeds its estimated recoverable amount. Impairment losses are recognised in profit or loss. Impairment losses recognised in respect of cash-generating units are first allocated to reduce the carrying amount of any goodwill allocated to the units and then to reduce the carrying amount of the other assets in the unit (group of units) on a pro rata basis.

(iii) Reversal of impairment losses

An impairment in respect of a receivable carried at amortised cost is reversed, if the subsequent increase in the recoverable amount can be related objectively to an event occurring after the impairment loss was recognised. Impairment losses in respect of goodwill are not reversed. Impairment losses in respect of other assets are reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised. Reversals of impairment losses are recognised in profit or loss.

(iv) Calculation of recoverable amount

The recoverable amount of the Group's receivables carried at amortised cost is calculated as the present value of estimated future cash flows, discounted at the original effective interest rate (i.e. the effective interest rate computed on initial recognition of these financial assets). Receivables with a short remaining term are not discounted. The recoverable amount of other assets is the greater of their net selling price and value in use.

In determining value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

(h) Share capital

(i) Ordinary shares

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of ordinary shares are recognised as a deduction from equity, net of any tax effect.

(ii) Repurchase, disposal and reissue of share capital (treasury shares)

When own shares recognised as equity are repurchased, the amount of the consideration paid, including directly attributable costs and net of any tax effects, is recognised as a deduction from equity. Repurchased shares are classified as treasury shares and are presented as a deduction from total equity. If treasury shares are sold or reissued subsequently, the amount received is recognised as an increase in equity, and the resulting surplus or deficit on the transaction is transferred respectively to or from other reserves.

(iii) Dividends

The holders of ordinary shares are entitled to receive dividends as determined from time to time by the General Meeting of Shareholders. The Executive Board has the authority to decide, with the approval of the Supervisory Board, what portion of the profit will be allocated to the reserves. If applicable, the declared but unpaid dividends are recognised as a liability.

(i) Employee benefits

(i) Defined contribution plans

A defined contribution plan is a post-employment benefit plan under which an entity pays fixed contributions into a separate entity and will have no legal or constructive obligation to pay further amounts. Obligations for contributions to defined contribution pension plans are recognised as an employee benefit expense in profit or loss when incurred. Prepaid contributions are recognised as an asset to the extent that a cash refund or reduction in future payments will occur.

(ii) Defined benefit plans

A defined benefit plan is a post-employment benefit plan other than a defined contribution plan. The Group's net obligation in respect of defined benefit plans is calculated separately for each plan by estimating the amount of future benefit that employees have earned in return for their service in the current and prior periods; that benefit is discounted to determine its present value. The fair value of any plan assets is deducted. The Group determines the net interest expense (income) on the net defined benefit liability (asset) for the period by applying the discount rate used to measure the defined benefit obligation at the beginning of the annual period to the net defined benefit liability (asset). The discount rate is the yield at the reporting date on AA credit-rated bonds that have maturity dates approximating the terms of the Group's obligations and that are denominated in the same currency in which the benefits are expected to be paid.

The calculation is performed annually by a qualified actuary using the projected unit credit method. When the calculation results in a benefit to the Group, the recognised asset is limited to the present value of economic benefits available in the form of any future refunds from the plan or reductions in future contributions to the plan. In order to calculate the present value of economic benefits, consideration is given to any minimum funding requirements that apply to any plan in the Group. An economic benefit is available to the Group if it is realisable during the life of the plan, or on settlement of the plan liabilities.

Remeasurements arising from defined benefit plans comprise actuarial gains and losses, the return on plan assets (excluding interest) and the effect of the asset ceiling (if any, excluding interest). The Group recognises them immediately in other comprehensive income, and all other expenses related to defined benefit plans as employee benefit expenses in profit or loss. When the benefits of a plan are changed, or when a plan is curtailed, the portion of the changed benefit relating to past service by employees, or the gain or loss on curtailment, is recognised immediately in profit or loss when the plan amendment or curtailment occurs. The Group recognises gains and losses on the settlement of a defined benefit plan when the settlement occurs. The gain or loss on a settlement is the difference between the present value of the defined benefit obligation being settled as determined on the date of settlement and the settlement price, including any plan assets transferred and any payments made directly by the Group in connection with the settlement.

(iii) **Other long-term service benefits**

The Group's net obligation in respect of long-term service benefits other than pension plans is the amount of future benefit that employees have earned in return for their service in the current and prior periods. The obligation is calculated using the projected unit credit method, discounted to its present value and net of the fair value of any related assets.

The discount rate is the yield at the financial position date on AA-credit rated bonds that have maturity dates approximating the terms of the Group's obligations. Any actuarial gains and losses are recognised in profit or loss in the period in which they arise.

(iv) **Share-based payment transactions**

The fair value on the grant date of share-based payment awards made to employees and the Executive Board is recognised as an employee expense, with a corresponding increase in equity, over the period that the employees unconditionally become entitled to the awards. The amount recognised as an expense is adjusted to reflect the number of awards for which the related service and non-market vesting conditions are expected to be met, so that the amount ultimately recognised as an expense is based on the number of awards that meet the related service and non-market performance conditions at the vesting date. For share-based payment awards with non vesting conditions, the fair value on the grant date of the share-based payment is measured to reflect such conditions, with no true-up for differences between expected and actual outcomes.

(v) **Short-term employee benefits**

A liability is recognised for the amount expected to be paid if the Group has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably. Short-term employee benefits are expensed as the related service is provided.

(vi) **Termination benefits**

Termination benefits are expensed at the earlier of when the Group can no longer withdraw the offer of those benefits and when the Group recongised costs for a restructuring. If benefits are not expected to be settled wholly within 12 months of the reporting date, then they are discounted.

(j) Provisions

A provision is recognised in the statement of financial position if the Group has a present legal or constructive obligation as a result of a past event, that can be measured reliably and it is probable that settlement of the obligation will involve an outflow of funds. If the effect is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability. The unwinding of the discount is recognised as finance cost.

(k) Revenue

(i) **Goods sold and services rendered**

Revenue reflects the fair value of the consideration received or receivable for the sale of goods and services in ordinary course of business, net of discounts, rebates, returns and excluding VAT. Revenue from the sale of goods is recognised when significant risks and rewards of ownership

have been transferred to the customer, collectability of the consideration is probable for the Group, costs incurred can be estimated reliable by the Group, the Group retains neither continuing managerial involvement to the degree normally associated with ownership nor effective control over the goods sold to the customer and amount of revenue can be measured reliably by the Group. The transfer of risks and rewards varies depending on the terms of the individual sales contract.
Transfer of risks and rewards varies depending on the individual terms of the contract of sale. These criteria are met at the time the product is shipped and delivered to the customer and title and risk have passed to the customer (depending on the delivery conditions) and acceptance of the product has been obtained. For products for which a right of return exists during a defined period, revenue recognition is determined based on the historical pattern of actual returns, or in cases where such information is not available, revenue recognition is postponed until the return period has lapsed.

Revenue from services is recognized when the Group can reliably measure the amount of revenue and the associated cost related to the stage of completion of a contract or transaction, and the recovery of the consideration is considered probable.

Royalty income from intellectual property rights is recognized on an accrual basis based on actual or reliably estimated sales made by a licensees. Royalty income from an agreement with lump-sum consideration is recognized on accrual basis based on the contractual terms and substance of the relevant agreement with a licensee.

(ii) Government grants

Grants are initially recognised at fair value in statement of financial position as deferred income. Once there is a reasonable assurance that the Group will comply with the applicable conditions the grant is recognised in proift or loss as operating income. Grants that compensate the Group for expenses incurred are recognised asother income in profit or loss in the periods in which the expenses are incurred. Grants related to the acquisition of fixed assets are recognised in profit or loss as other operating income over the useful life of the asset.

(l) Expenses

(i) Operating lease payments

Payments made under operating leases are recognised in the statement of comprehensive income on a straight-line basis over the term of the lease.

(ii) Financial lease payments

Minimum lease payments are apportioned between the finance expense and the reduction in the outstanding liability. The finance expense is allocated to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability.

(iii) Net finance costs

Finance income comprises interest income on funds invested, and financial assets held to maturity. Interest income is recognised in profit or loss as it accrues, using the effective interest method.

Finance expense comprises interest expense on borrowings, commitment fees, accrued interest on provisions, interest on pension liabilities, impairment losses recognised on financial assets and losses on interest rate hedge instruments to the extent they are recognised in profit or loss. All borrowing costs are recognised in profit or loss using the effective interest method.

Realised and unrealised foreign currency gains and losses on monetary assets and liabilities, including changes in fair value of currency hedge instruments that are not qualified as cash flow hedges, are reported on a net basis.

(m) Income tax

Income tax for the year comprises current and deferred tax. Income tax is recognised in profit or loss unless it relates to items recognised directly in equity, in which case it is recognised in equity.

Current tax is the expected tax, payable or receivable, on the taxable income for the year, using applicable tax rates enacted or substantially enacted by the financial position date, and any adjustment to tax calculated in respect of previous years.

Deferred tax is recognised using the balance sheet method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognised for the following temporary differences:

- the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit;
- relating to investments in subsidiaries and jointly controlled entities to the extent that it is probable that they will not be reversed in the foreseeable future;
- arising on the initial recognition of goodwill.

Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they are reversed, based on the laws that have been enacted or substantially enacted by the reporting date.

Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax assets and liabilities, and they relate to income taxes levied by the same tax authority on the same taxable entity; or on different tax entities, but the intention is to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realised simultaneously.

A deferred tax asset is recognised to the extent that it is probable that future taxable profits will be available against which the asset can be applied. Deferred tax assets are reduced if it is no longer probable that the related tax benefit will be realised.

Additional income taxes that arise from the distribution of a dividend are recognised at the same time as the liability to pay the related dividend is recognised.

(n) Earnings per share

The Company presents basic and diluted earnings per share data for its ordinary shares. Basic earnings per share is calculated by dividing the profit or loss attributable to ordinary shareholders of the Company by the weighted average number of ordinary shares outstanding during the reporting period. Diluted earnings per share is determined by adjusting profit or loss attributable to ordinary shareholders and the weighted average number of ordinary shares outstanding, for the effects of all dilutive potential ordinary shares.

(o) Segment reporting

The Group defines and presents operating segments based on the information that is provided internally to the Executive Board, the Group's chief operating decision-maker. This is in conformity with IFRS 8 – Operating segments.

On the basis of the criteria of IFRS 8, Kendrion's business units are the Group's operating segments. An operating segment is a part of the Group engaging in business activities that may result in revenue and expenses, including the revenue and expenses relating to transactions with any of the Group's other segments. The Executive Board conducts regular reviews of the operating segment's results to reach decisions on the resources to be allocated to the segment and to assess its performance, whereby separate financial information for each operating segment is available.

However, and on the basis of the aggregation criteria of IFRS 8.12, these operating segments have been aggregated into two reportable segments: Automotive and Industrial. In accordance with IFRS 8, the Company also discloses general and entity-wide information, including information about geographical areas and major customers of the Group as a whole. More information on the reportable segments is provided in note 19.

(p) New standards and interpretations

A number of new standards, amendments to standards and interpretations are effective, and have been endorsed by the European Union, for annual periods beginning on or after 1 January 2017 and therefore apply to the year ended 31 December 2017:

- **Amendments to IAS 7 Disclosure Initiative**. Amendments to this standard are part of IASB's Disclosure Initiative and will help users of the financial statements better understand changes in entity's debt. This amendment has no material impact on the consolidated financial statements.

- **Amendment to IAS 12: Recognition of Deferred Tax Assets for Unrealised Losses**. Amendments to this standard do have the purpose to clarify the accounting for deferred tax assets for unrealised losses on debt instruments measured at fair value. An entity needs to consider whether tax law restricts the sources of taxable profits against which it may make deductions on the reversal of that deductible temporary difference. In addition, amendments provide guidance on how an entity should determine future taxable profits and explain circumstances in which taxable profits may include the recovery of some assets for more than their carrying amount. This amendment has no material impact on the consolidated financial statements.

The standards or interpretations published by the International Accounting Standards Board (IASB) and the International Financial Reporting Interpretations Committee (IFRIC) that are not effective at 31 December 2017 but may be relevant are as follows:

- **IFRS 9: Financial instruments**. IFRS 9, endorsed by the European Union on 22 November 2016, replaces the existing guidance in IAS 39 Financial instruments: Recognition and Measurement. IFRS 9 contains new guidance on:
  - Classification and measurement of financial instruments. For financial liabilities designated as accounted for at fair value through profit or loss (FVTPL) using the fair value option (FVO), the amount of the change in the fair value of such financial liabilities that is attributable to changes in credit risk must be presented in other comprehensive income (OCI). The remainder of the change in fair value is presented in profit or loss, unless presentation in OCI of the fair value change in respect of the liability's credit risk would create or enlarge an accounting mismatch in profit or loss. All other IAS 39 requirements for financial liabilities have been carried forward into IFRS 9;
  - Key change in terms of recognition and measurement of impairment losses on financial assets. IAS 39 only allows impairment losses based on losses already incurred. Whereas the IFRS 9 model is based on an expected credit loss model for calculating impairments. For certain financial instruments such as trade accounts receivable, simplifications for recognising impairment losses apply; and
  - New general hedge accounting requirements aiming for a closer alignment of hedge accounting with entity's risk management strategy.

  IFRS 9 applies to annual reporting periods beginning on or after 1 January 2018 (early application is permitted). In 2017 we completed our survey and concluded that this standard has no significant impact on the consolidated financial statements 2018 of the Group.

- **IFRS 15: Revenue from contracts with Customers**. The new standard does not differentiate between different types of contracts and services, but rather introduces uniform criteria for the timing of revenue recognition. According to IFRS 15, an entity can recognise revenue at any time so that it reflects the consideration to which the entity expects to be entitled in exchange for transferring goods or services to a customer. The transfer of major risks and rewards of ownership of the goods is no longer the deciding factor. The new model involves five steps for recognition of revenue with the first steps being the identification of the contract with the customer (I) and the separate performance obligations it contains (II). The transaction price is then determined (III) and allocated to the performance obligations in the contract (IV). Finally (V), sales are recognised for each performance obligation in the amount of the allocated portion of the transaction price as soon as the agreed-upon good or service has been provided or the customer receives control over it. Principles are set out for determining whether the good or service has been provided over time or at one point in time.

  The rules and definitions of IFRS 15 supersede the content of IAS 11, IAS 18, IFRIC 13, IFRIC 15, IFRIC 18 and SIC 31. Consequently, it also amends IAS 16, IAS 38 and IAS 40 requiring entities to use the requirements of IFRS 15 for the recognition and measurement of gains and losses on disposal of non-financial assets that are not an output of an entity's ordinary activities.
  European Union has endorsed this standard for annual reporting periods beginning on or after 1 January 2018, with early adoption permitted. The standard will be adopted for the fiscal year beginning 1 January 2018 applying the modified retrospective approach meaning that the impact on the profit for the period 2017 will be adjusted in equity on 1 January 2018. The timing and amount of revenue that the Group

recognises under IFRS 15 may be effected compared to Kendrion's current accounting policy. Certain type of contracts with customers contain variable considerations. These variable considerations will have an impact on the transaction price to be allocated to the performance obligation(s). However the majority of our contracts with customers will be accounted for at a 'point in time'. IFRS 15 also gives more guidance on how to account for contract modifications than current revenue standard IAS 18. For contract modifications it needs to be assessed whether the change must be accounted for either as a retrospective change, prospectively with a reallocation of revenues amongst identified performance obligations, or prospectively as separate contracts. The Statement of Financial Position will change accordingly (e.g. receivables from contracts with customer, contract assets and contract liabilities (if any)) and disclosures will be amended. In 2017 we completed our survey and concluded that this standard has no significant impact on the consolidated financial statements 2018 of the Group.

- **IFRS 16 Leases:** The European Union has endorsed on 31 October 2017 a new accounting standard, IFRS 16 Leases. This standard eliminates the current accounting model for lessees under IAS 17: on-balance sheet finance leases and off-balance sheet operating leases. IFRS 16 introduces a single on-balance sheet accounting model similar to current finance lease accounting, unless the lease terms is 12 months or less or the underlying asset has a low value. Lessor accounting remains similar to current accounting practice, which means that lessors continue to classify leases as finance and operating leases. Under IFRS 16 the balance sheet of lessees will be impacted by recognising the corresponding asset ('right to use the asset') of the lease arrangement. On the other hand, a liability is recognised with regard to the obligation to make lease payments. This new standard will bring off balance leases on the balance sheet. The statement of comprehensive income is impacted by depreciation of the lease asset and corresponding interest component, which is not necessarily similar to the cash rental previously recognised in the statement of comprehensive income. The new standard is expected to impact financial metrics such as solvency, EBIT(DA), earnings per share and return on equity.

  This standard applies to annual reporting periods beginning on or after 1 January 2019, with early adoption permitted. Transition options to apply are either a full retrospective approach or a modified retrospective approach. The Group decided to adopt full retrospective IFRS 16 as per 1 January 2018. The impact on EBITA of the Group in 2018 is assessed on EUR 0.6 million positive. As per 1 January 2018 total assets will increase by EUR 15.5 million, total liabilities will increase by EUR 16.2 million and total equity will decrease by 0.7 million compared to year-end 2017.

(q) Fair values

(i) Measurement of fair value

Several of the Group's accounting policies, as well as the information supplied by the Group, require the fair value of both financial and non-financial assets and liabilities to be determined. For valuation and information supplied, the fair value is measured using the methods below. Where applicable, more detailed information on the basis of the fair value measurement is disclosed in the specific notes on the asset or liability in question. The principal methods and assumptions used in estimating the fair value of financial instruments included in the summary are given below.

(ii) **Property, plant and equipment**

The fair value of property, plant and equipment recognised as a result of a business combination is based on market value in use. The market value of property is the estimated amount for which the property in question could be exchanged on the valuation date between a buyer and seller in an arm's length transaction, in which both parties have acted knowledgeably, prudently and without compulsion. The market value of other items of property, plant and equipment is based on the quoted market prices of comparable assets and goods.

(iii) **Intangible assets**

The fair value of patents and trademarks acquired as part of a business combination is measured on the basis of the discounted estimated royalties that have been avoided through ownership of the patent or trademark. The fair value of customer relationships acquired in a business combination is based on the excess earnings method over multiple periods, valuing the asset in question by deducting a real return on all other assets which in total create the related cash flows. The fair value of other intangible assets is based on the expected discounted value of the cash flows from the use and ultimate sale of these assets.

(iv) **Financial lease liabilities**

The fair value is estimated on the basis of the present value of future cash flows, discounted at the interest rate for lease contracts of a similar nature. The estimated fair value reflects movements in interest rates.

(v) **Inventories**

The fair value of inventories acquired as part of a business combination is determined on the basis of the estimated selling price as part of normal business operations, less the estimated costs of completion and the selling costs, plus a reasonable profit margin that reflects the completion and sales effort.

(vi) **Trade and other receivables/trade and other payables**

The face value of receivables and liabilities falling due within one year is regarded as a reflection of their fair value. The fair value of all other receivables and liabilities is measured on the basis of present value. The discount factor is based on the risk-free interest rate of the same duration as the receivable and/or payable, plus a credit mark up reflecting the credit worthiness of the Group.

(vii) **Interest-bearing loans**

The fair value is calculated on the basis of the present value of future repayments of principal and interest at the prevailing market rate of interest, supplemented by a credit mark-up reflecting the credit worthiness of the Group.

(viii) **Derivatives**

The fair value of forward exchange contracts is based on the present value of the contractual cash flows for the remaining term based on a risk-free interest rate.

(ix) **Non-derivative financial liabilities**

The fair value of non-derivative financial liabilities is determined from information supplied and is based on the present value of future repayments of principal and interest, discounted at a risk-free rate, and a margin based on the credit worthiness of the Group on the reporting date.

(x) **Contingent consideration**

The fair value of contingent considerations arising in a business combination is calculated using the income approach based on the expected payment amounts and their associated probabilities. If appropriate, it is discounted to present value.

(r) Financial risk management

The Group has exposure to the following risks from its use of financial instruments:

- credit risk;
- liquidity risk;
- market risk.

This section provides general information about the Group's exposure to each of the above risks in the course of its normal business operations, the Group's objectives, policies and processes for measuring and managing risk, and the Group's management of capital. Further quantitative disclosures are included in the financial instrument section in these consolidated financial statements.

The Executive Board bears the ultimate responsibility for the organisation and control of the Group's risk management framework. The Group's risk policy is designed to identify and analyse the risks confronting the Group, implement appropriate risk limits and control measures, and monitor the risks and compliance with the limits. The risk management policy and systems are evaluated at regular intervals and, if necessary, adapted to accommodate changes in market conditions and the Group's operations.

The Company's Supervisory Board supervises compliance with the Group's risk management policy and procedures.

For a more detailed description of risk management and the position of financial risk management in the Group's framework, see Report of the Executive Board.

(i) **Credit risk**

Credit risk is the risk of financial loss to the Group in the event that a customer or counterparty to a financial instrument fails to meet its contractual obligations. Credit risks arise primarily from accounts receivable, derivative transactions concluded with banks, and cash positions and deposits held with banks. The Group continually monitors the credit risk within the Group. The Group does not normally require collateral for trade and other receivables or financial assets.

The credit policy includes an assessment of the creditworthiness of every new major customer before offering payment and delivery terms.

This assessment includes external credit ratings or reports if they are available. The creditworthiness of major customers is actively monitored on an ongoing basis.

The Group recognises impairment provisions of an amount equal to the estimated losses on trade and other receivables and other investments. The main component of this provision comprises specific provisions for losses on individual accounts of material significance.

(ii) Credit risk concentration

The customer with the largest receivable outstanding accounted for 6% of the trade and other receivables at 31 December 2017. In 2016, the largest customer outstanding at 31 December 2016 accounted for 7% of total trade and other receivables. Other customers individually accounted for 5% or less of the trade and other receivables at 31 December 2017. The geographical credit risk from the Group's direct customers is largely concentrated in Germany. However, as the Group's most important customers in the various segments of the German market are multinational or global players, this reduces the Group's dependency on the German market.

(iii) Investments and financial instruments

The Group currently does not invest in debt securities. Cash positions and exposure to the financial instruments of financial counterparties are monitored actively. The Group's main financial counterparties are well-established banks with good creditworthiness. The cash in bank accounts at other than the core-relationship banks is maintained at the minimum level required for the operations of the Group's companies.

(iv) Liquidity risk

The liquidity risk is the risk that the Group is unable to meet its financial obligations at the required time. Liquidity risk management is based on the maintenance of sufficient liquidity in the form of unused (committed) credit facilities or cash to meet present and future financial obligations in normal and adverse circumstances.

A summary of the credit lines available to the Group is disclosed in note 10 of these consolidated financial statements. The majority of the available facilities are provided by a syndicate of lenders consisting of BNP Paribas, Deutsche Bank and ING Bank on an equal basis. The Group had approximately EUR 91 million available within its existing revolving credit facility on the financial position date.

(v) Market risk

The market risk is the risk of the deterioration of the Group's income due to movements in market prices, such as those relating to exchange rates and interest rates. The management of market risk exposure is intended to keep the market risk position within acceptable limits.

Derivatives are used to manage specific market risks. These transactions are carried out within the treasury framework adopted by the Executive Board. If necessary, the Group uses hedge accounting to manage volatility in the statement of comprehensive income.

(vi) Interest rate risk

Pursuant to the Group's policy more than 50% of the exposure to changes in interest rates on borrowings is maintained on a fixed rate basis, taking into account any assets with exposure to changes in interest rates and expected short-term free cash flows. The policy is implemented by making use of derivative financial instruments such as interest rate swaps and interest rate options.

The Group has currently outstanding interest swap contracts with a total underlying notional value of EUR 50 million in order to reduce interest rate risk exposure to increasing market rates. EUR 15 million matures in first quarter of 2018, EUR 15 million in third quarter 2018 and EUR 20 million matures in 2020.

(vii) Currency risk

The Group is exposed to exchange rate risks on sales, purchases, equity positions and loans expressed in currencies other than the euro. The Group companies are primarily financed in their own currency. The majority of the revenues and costs of the Group companies are realised in the euro zone. Approximately 75% of the cost base and revenues are realised in euros. Sales outside the euro zone are partly generated locally and partly through exports from the euro zone. Most of these exports are realised in euros.

The Group's activities in the Czech Republic have the most significant currency exposure, since the majority of revenue is generated in euros and part of the costs are in Czech korunas. Pursuant to the Group's policy this currency exposure is hedged to a level of at least 70% for the next four quarters and at least 35% for the next four quarters thereafter. Exchange rate risks are hedged with derivatives.

The Group also actively hedges intercompany loans in foreign currencies with currency forwards, swaps or back-to-back loans in the same foreign currency.

Pursuant to the Group's policy for other monetary assets and liabilities denominated in a foreign currency, net exposure is maintained at an acceptable level by buying or selling foreign currencies at spot rates as required to correct short-term imbalances.

The Group's policy stipulates that, in principle, equity investments and other translation exposures are not hedged.

(viii) Other price risks

Steel, copper and rare earth metals used in permanent magnets are the most important commodities for the Group.

Copper constitutes the Group's main direct exposure to raw material price risks, since copper wire is an important component of electromagnets. Pursuant to the Group's policy, the sensitivity to copper prices is actively reduced both by concluding fixed-price purchase contracts in the normal course of business with copper wire suppliers and by including raw material clauses in sales contracts. As the need arises the Group can also conclude derivative financial instrument contracts with financial counterparties to hedge the copper risk. No financial derivative contracts for raw materials were outstanding at the balance sheet date.

The Group is also exposed to risks associated with rare earth metals such as neodymium, a component of permanent magnets, which are used in some of the Group's products. Prices of these commodities have shown significant volatility in the past. The Group closely monitors developments in this market and has increased stock levels and the number of supply sources for these permanent magnets.

Furthermore, agreements have been made with customers representing the majority of the sales volume in this context, to link sales prices to movements in permanent magnet prices.

The Group is mainly indirectly exposed to raw material price risks relating to oil and steel, primarily as part of the purchase prices of machined components. This exposure is monitored and, if feasible, reduced by means of raw material clauses with customers and by concluding fixed-price agreements with suppliers for periods of between six and twelve months. The Kendrion steel contracts also partly govern the purchasing from component suppliers.

Raw materials are purchased separately by each business unit, but in accordance with the group policy reviewed periodically with the objective of further increasing and sharing knowledge on commodities and commodity markets between business units, reducing risks and/or prices.

(ix) **Capital management**

The Executive Board's policy is designed to maintain a strong capital gearing to retain the confidence of investors, creditors and the markets, and to safeguard the future development of the business activities. The Executive Board monitors the return on equity, which the Group defines as the net operating result divided by shareholders' equity, excluding minority interests. The Executive Board also monitors the level of dividend distributed to ordinary shareholders.

The Executive Board seeks to strike a balance between a higher return that would be achievable with a higher level of borrowed capital and the benefits and security of sound capital gearing.

Kendrion carried out an evaluation of its dividend policy during the course of 2011. The results of this evaluation were discussed at the General Meeting of Shareholders on 16 April 2012. Kendrion intends to distribute an annual dividend of between 35% and 50% of the net profit, taking into consideration the amount of net profit to be retained to support the medium and long-term strategic plans of the company and to maintain a minimum solvency of 35%.

Neither the Company nor its subsidiaries are subject to any externally imposed capital requirements beyond those stipulated by law.

1 Property, plant and equipment

EUR million	Land and buildings	Plant and equipment	Other fixed assets	Under construction	Total
Cost					
Balance as at 1 January 2016	48.2	100.1	41.8	11.1	201.2
Acquired, other	1.9	16.5	5.4	7.1	30.9
Disposals	(0.4)	(0.5)	(0.3)	(10.0)	(11.2)
Currency translation differences	0.1	0.1	0.0	0.0	0.2
Balance as at 31 December 2016	49.8	116.2	46.9	8.2	221.1
Balance as at 1 January 2017	49.8	116.2	46.9	8.2	221.1
Acquired, other	3.1	11.2	5.9	11.1	31.3
Disposals	(0.6)	(3.3)	(2.1)	(6.7)	(12.7)
Currency translation differences	(0.4)	(0.6)	(0.1)	(0.2)	(1.3)
Balance as at 31 December 2017	51.9	123.5	50.6	12.4	238.4
Depreciation and impairment losses					
Balance as at 1 January 2016	21.3	66.3	30.8	0.1	118.5
Depreciation for the year	2.0	10.8	4.4	–	17.2
Impairment	–	0.2	0.3	–	0.5
Disposals	–	(0.4)	(0.2)	–	(0.6)
Balance as at 31 December 2016	23.3	76.9	35.3	0.1	135.6
Balance as at 1 January 2017	23.3	76.9	35.3	0.1	135.6
Depreciation for the year	1.9	10.4	4.5	0.0	16.8
Impairment	0.1	0.9	0.0	0.0	1.0
Disposals	(0.5)	(2.9)	(2.0)	–	(5.4)
Balance as at 31 December 2017	24.8	85.3	37.8	0.1	148.0

EUR million	Land and buildings	Plant and equipment	Other fixed assets	Under construction	Total
Carrying amounts					
As at 1 January 2016	26.9	33.8	11.0	11.0	82.7
As at 31 December 2016	26.5	39.3	11.6	8.1	85.5
As at 1 January 2017	26.5	39.3	11.6	8.1	85.5
As at 31 December 2017	27.1	38.2	12.8	12.3	90.4

Translation differences are calculated on the carrying amount and reflected in the related item in the cost.

The estimated useful lives are as follows:

Buildings	10 – 30 years
Plant and equipment	5 – 10 years
Other fixed assets	3 – 7 years

The Executive Board reviews at each reporting period the estimated useful lives of each asset with a definite useful life. During the current year, the Executive Board determined that the useful lives do not require to be revised.

2 Intangible assets

EUR million	Goodwill	Development costs	Software	Other	Total
Cost					
Balance as at 1 January 2016	93.4	1.0	17.0	40.9	152.3
Acquired, other	–	0.9	2.0	–	2.9
Disposals	–	(0.2)	(0.0)	(0.1)	(0.3)
Currency translation differences	0.9	0.0	0.0	0.2	1.1
Balance as at 31 December 2016	94.3	1.7	19.0	41.0	156.0
Balance as at 1 January 2017	94.3	1.7	19.0	41.0	156.0
Acquired, other	–	1.6	2.9	–	4.5

EUR million	Goodwill	Development costs	Software	Other	Total
Disposals	–	(0.2)	(0.0)	(0.0)	(0.2)
Currency translation differences	(3.4)	(0.0)	(0.0)	(0.8)	(4.2)
Balance as at 31 December 2017	90.9	3.1	21.9	40.2	156.1
Amortisation and impairment losses					
Balance as at 1 January 2016	–	0.0	7.1	17.6	24.7
Amortisation for the year	–	0.1	3.0	3.7	6.8
Disposals	–	–	(0.0)	(0.0)	(0.0)
Balance as at 31 December 2016	–	0.1	10.1	21.3	31.5
Balance as at 1 January 2017	–	0.1	10.1	21.3	31.5
Amortisation for the year	–	0.3	3.2	3.2	6.7
Disposals	–	–	(0.0)	–	(0.0)
Balance as at 31 December 2017	–	0.4	13.3	24.5	38.2
Carrying amounts					
At 1 January 2016	93.4	1.0	9.9	23.3	127.6
At 31 December 2016	94.3	1.6	8.9	19.7	124.5
At 1 January 2017	94.3	1.6	8.9	19.7	124.5
At 31 December 2017	90.9	2.7	8.6	15.7	117.9

Goodwill has an indefinite estimated useful life. The investments in software during 2017 of EUR 2.9 million (2016: EUR 2.0 million) mainly relate to an upgrade of the ERP system. The other intangible assets comprise the carrying amount of customer relationships amounting to EUR 15.2 million (2016: EUR 18.4 million). These customer relationships were acquired through business combinations.

Depreciation and amortisation

Depreciation and amortisation are recognised in the following items in the consolidated statement of comprehensive income:

EUR million	2017	2016
Depreciation and amortisation	23.5	24.0

The estimated useful life of software is between three and eight years. The estimated useful life of other intangible assets is approximately between eight and fifteen years.

The Executive Board reviews at each reporting period the estimated useful lives of each intangible asset with a definite useful life. As per the upgrade of the ERP system in 2017 the useful life of the ERP system is reassessed and revised. The revision of the usefull life of the ERP sytem had a favorable impact of EUR 0.5 million on amortization in 2017.

Impairment testing for cash-generating units containing goodwill

As part of the strategy announced on 3 May 2016 'Simplify, Focus, Grow' Kendrion eliminated the divisional management layer and reduced the number of business units from seven to five. Managements' approach to manage the company from a business unit perspective has been further enforced and became fully effective as from 1 January 2017. Goodwill as recognised on the balance sheet as on 1 January 2017 is reallocated to the five business units applying the relative value approach (IAS 36.87).

Goodwill EUR million	2017
Business Unit - Industrial Magnetic Systems	6.4
Business Unit - Industrial Control Systems	17.7
Business Unit - Industrial Drive Systems	7.1
Business Unit - Passenger Cars	24.5
Business Unit - Commercial Vehicles	35.2
	90.9

The consolidated financial statements 2016, pages 110-112, show the required goodwill disclosures with regard to the cash-generating units identified as per 31 December 2016.

Key assumptions and method of quantification

The Group recognises its intangible assets in accordance with IAS 38 and IFRS 3. Pursuant to IAS 36, the Group has performed an impairment test with reference to the goodwill allocated to each individual cash-generating unit. This test was carried out by discounting future cash flows (‘value in use’) to be generated from the continuing use of the cash-generating unit to which the goodwill applies and on the assumption of an indefinite life. The cash flows for the next five years were based on mid-term plans and budgets drawn up by the local management and approved by the Executive Board. The Group did not recognise any impairment of goodwill in this reporting period.

For the subsequent years, the residual value was calculated on the basis of the results in the last year of relevant forecasts, with a terminal growth rate of 2% taken into account. The forecasts took no account of tax considerations, i.e. were based on pre-tax cash flow. The weighted average cost of capital (WACC) based on the Capital Asset Pricing Model was also pre-tax. Expansion investments were excluded from the calculations in the residual value. The expected growth in cash flows as a result of these expansion investments was also excluded. Key assumptions used in the calculation of recoverable amounts concern discount rates, terminal value growth rates and EBITA growth. Key assumptions are based on past experience and source from external sources.

These assumptions are as follows:

Discounted cash flow projections

	Discount rate	Terminal value growth rate
	2017	2017
Business Unit - Industrial Magnetic Systems	7.4%	2.0%
Business Unit - Industrial Control Systems	7.1%	2.0%
Business Unit - Industrial Drive Systems	7.0%	2.0%
Business Unit - Passenger Cars	7.3%	2.0%
Business Unit - Commercial Vehicles	8.1%	2.0%

Discount rate

In determining the pre-tax discount rate, first the post-tax average costs of capital were calculated for all cash generating units containing goodwill. The post-tax rate is based on debt leveraging compared to the market value of equity of 22%. All the post-tax weighted average cost of capital rates of cash generating units approximated 5.6% to 6.2%, and these rates were used for calculating the post-tax cash flows.

Terminal value growth rate

All cash generating units with goodwill have five years of cash flows included in their discounted cash flow models. A long-term growth rate in perpetuity has been determined on the basis of a growth rate of 2%.

Sensitivity to changes in assumptions

The recoverable amounts of all cash-generating units with goodwill exceed their carrying amounts. Management has carried out an analysis of sensitivity to changes in the key assumptions. The following table shows the percentage by which either discount rate (post tax) or forecasted EBITA would need to change for the estimated recoverable amount to equal the carrying amount:

Change required for recoverable amount to equal carrying amount	Discount rate (post tax)	Forecasted EBITA
	2017	2017
Business Unit - Industrial Magnetic Systems	24.7%	(83%)
Business Unit - Industrial Control Systems	17.6%	(82%)
Business Unit - Industrial Drive Systems	19.1%	(80%)
Business Unit - Passenger Cars	21.3%	(87%)
Business Unit - Commercial Vehicles	6.7%	(60%)

This table shows that a reasonably possible change in key assumptions would not cause the value in use to fall to the level of the carrying value.

3 Other investments, including derivatives

Other investments in 2017 include financial derivatives and recognised upfront and legal fees related to the facility agreement (see note 10). Kendrion amortises these costs over the remaining maturity of the facility. As these costs relate to the facility agreement as a whole and not to individual loans, these costs are not part of the effective interest rate of outstanding loans.

4 Deferred tax assets and liabilities

The Group has recognised deferred tax assets for tax loss carry-forwards in the following jurisdictions:

Germany

Tax assessments have been submitted for the German companies up to and including 2015. In 2017 tax audits started with regard to the assessment periods 2012-2014 with reference to our Northern Germany operating companies (years up to and 2011 are final) and assessment periods 2010-2014 with respect to our Southern Germany operating companies (years up to and 2009 are final). Only the tax audit of the assessment period 2010-2014 at Kendrion Markdorf is closed. Our operating company in Central Germany, Kendrion Aerzen, has been audited up to and including 2008 and the tax audit started in 2017 relates to assessment periods 2009-2014.

At 31 December 2017 tax loss carry forwards amounted to EUR 7.0 million ('Gewerbesteuer') and EUR 19.5 million ('Körperschaftsteuer'). These are recognised in full, resulting in deferred tax assets of EUR 3.5 million (2016: EUR 4.6 million).

United States of America

Tax assessments have been submitted up to and including 2016. The years 2013 up to 2015 are open for tax audits. At 31 December 2017 the tax loss carry forwards amounted to EUR 2.7 million (2016: EUR 3.7 million). These are recognised in full, resulting in deferred tax assets of EUR 0.6 million (2016: EUR 1.3 million). As per the USA 'Tax Cuts and Jobs Act' (dated 22 December 2017) the corporate income tax rate decreased from 35% to 21% as per 1 January 2018. This new legislation means that deferred tax positons as per 31 December 2017 are revalued and had a postive impact of EUR 0.3 million on net deferred taxes.

The Netherlands

Tax assessments have been submitted up to and including 2015. The years 2011 up to 2017 are still open for potential tax audits. At 31 December 2017 the tax loss carry-forwards amounted to EUR 3.4 million (2016: EUR 4.5 million). These are recognised in full, resulting in deferred tax assets of EUR 0.8 million (2016: EUR 1.1 million). These tax loss carry-forwards originated in 2012.

Deferred tax assets and liabilities included in the financial position

The deferred tax assets and liabilities can be specified as follows:

EUR million	Assets		Liabilities		Net	
	2017	2016	2017	2016	2017	2016
Property, plant and equipment	0.1	0.1	3.1	3.6	(3.0)	(3.5)
Intangible assets	3.6	4.3	5.2	6.8	(1.6)	(2.5)
Inventories	0.2	0.4	0.2	0.2	(0.0)	0.2
Employee benefits	1.6	2.2	–	0.0	1.6	2.2
Provisions	0.2	0.1	0.2	0.2	(0.0)	(0.1)
Other items	1.7	1.9	0.1	0.1	1.6	1.8
Tax value of recognised loss carry-forwards	4.9	7.0	–	–	4.9	7.0
Deferred tax assets/liabilities	12.3	16.0	8.8	10.9	3.5	5.1

The deferred tax liabilities relate almost entirely to temporary differences between the carrying amount and tax base of property, plant and equipment and intangible assets. These are of a relatively long-term nature, mostly longer than five years.

Deferred tax assets are recognised for unused tax losses to the extent that it is probable that future taxable profits will be available against which they can be set off. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised; such reductions are reversed if the probability of future taxable profits improves.

Tax loss carry forward limitation rules apply in certain jurisdictions in which Kendrion has carry forward tax losses. These rules might under certain circumstances lead to a (proportional) forfeiture of recognised and unrecognised carry forward tax losses in case of a direct or indirect change in ownership.

The tax losses carry forward for which no deferred tax assets are recognised in the statement of financial position are reviewed each reporting date. These tax losses carry forward for which no deferred tax assets are recognised in the statement of financial position amount to EUR 0.9 million (expire in 2020).

Movement in temporary differences during the financial year

Net, EUR million	2017			
	At 1 January	Recognised in profit or loss	Recognised in other comprehensive income	At 31 December
Property, plant and equipment	(3.5)	0.5	–	(3.0)
Intangible assets	(2.5)	0.9	–	(1.6)
Inventories	0.2	(0.2)	–	(0.0)
Employee benefits	2.2	(0.4)	(0.2)	1.6
Provisions	(0.1)	0.1	–	(0.0)
Other items	1.8	(0.2)	–	1.6
Tax value of loss carry-forwards used	7.0	(2.1)	–	4.9
	5.1	(1.4)	(0.2)	3.5

Net, EUR million	2016			
	At 1 January	Recognised in profit or loss	Recognised in other comprehensive income	At 31 December
Property, plant and equipment	(3.4)	(0.1)	–	(3.5)
Intangible assets	(6.6)	4.1	–	(2.5)
Inventories	(0.1)	0.3	–	0.2
Employee benefits	1.6	(0.1)	0.7	2.2
Provisions	0.2	(0.3)	–	(0.1)
Other items	2.2	(0.4)	–	1.8
Tax value of loss carry-forwards used	10.6	(3.6)	–	7.0
	4.5	(0.1)	0.7	5.1

In 2017, the net amount from the movement in deferred tax assets and liabilities, presented as tax in the statement of comprehensive income, is negative EUR 1.4 million (2016: negative EUR 0.1 million).

5 Inventories

EUR million	2017	2016
Raw materials, consumables, technical materials and packing materials	31.3	25.9
Work in progress	11.4	11.5
Finished goods	12.2	11.7
Goods for resale	2.4	3.5
	57.3	52.6

The inventories are presented after accounting for a provision of EUR 8.2 million (2016: EUR 9.0 million) for obsolescence. In 2017, the amount of the write-down to net realisable value of the inventories was EUR 1.4 million (2016: EUR 1.9 million). The write-down and reversals are included in cost of sales.

6 Trade and other receivables

EUR million	2017	2016
Trade receivables	50.2	45.6
Other taxes and social security	2.2	4.8
Other receivables	2.3	2.1
Derivatives used for hedging	0.4	-
Prepayments	3.0	2.0
	58.1	54.5

The credit and currency risks associated with trade and other receivables are disclosed in note 15, and in the financial risk management paragraph of note r.

7 Cash and cash equivalents

EUR million	2017	2016
Bank balances	7.6	12.4
Bank overdrafts	(11.7)	(2.7)
Cash and cash equivalents in the statement of cash flows	(4.1)	9.7

The bank balances include EUR 1.1 million of cash that is held in countries where we face cross-border foreign exchange controls and/or other legal restrictions that inhibit our ability to make these balances available for general use by the Group. The other bank balances are freely available. The interest rate risk for the Group and a sensitivity analysis for financial assets and liabilities are disclosed in notes 15 and r.

8 Capital and reserves

Capital and share premium

	Shares entitled to dividend		Shares owned by Kendrion		Total number of issued shares	
	2017	2016	2017	2016	2017	2016
At 1 January	13,396,034	13,188,154	–	–	13,396,034	13,188,154
Issued shares (share dividend)	115,157	199,706	–	–	115,157	199,706
Issued registered shares (share plan)	6,429	8,174	–	–	6,429	8,174
Delivered shares	1,843	1,044	(1,843)	(1,044)	–	–
Repurchased shares	(123,429)	(1,044)	123,429	1,044	–	–
At 31 December	13,396,034	13,396,034	121,586	–	13,517,620	13,396,034

Issuance of ordinary shares

In 2017, in total 115,157 new shares were issued as share dividend (2016: 199,706). During 2017, the Company delivered 8,272 shares to the Executive Board and senior management as part of its share plan and remuneration packages (2016: 9,128). The Company purchased 123,429 of its own shares in 2017 (2016: 1,044).

Ordinary shares

The authorised share capital consists of:

EUR million	2017	2016
40,000,000 ordinary shares of EUR 2.00	80.0	80.0
Issued share capital		
Balance at 1 January 2017: 13,396,034 ordinary shares (2016: 13,188,154)	26.8	26.4
Balance at 31 December 2017: 13,517,620 ordinary shares (2016: 13,396,034)	27.0	26.8

Share premium

EUR million	2017	2016
Balance as at 1 January	56.4	62.7
Dividend payment	(10.5)	(10.3)
Share premium on issued shares	3.7	4.0
Balance as at 31 December	49.6	56.4

Translation reserve

The translation reserve comprises all foreign currency differences arising from the translation of the financial statements of associates in the non-euro zone. Gains and losses relating to the translation risk are recognised in equity. The build-up of the cumulative figure commenced on 1 January 2004.

Hedge reserve

The hedge reserve comprises the effective portion of the cumulative net movement in the fair value of cash flow hedging instruments relating to hedged transactions that have not yet occurred, net of tax.

The net movement was EUR 0.6 million positive (2016: EUR 0.2 million, negative). The hedge reserve increased by EUR 0.4 million due to the realisation of hedged transactions (2016: EUR 0.0 million). The hedge reserve increased by EUR 0.2 million due to valuation effects (2016: negative EUR 0.2 million). There was no hedge ineffectiveness in 2017 (2016: EUR 0.0 million).

Reserve for own shares (treasury shares)

The reserve for the Company's own shares comprises the shares held by the Company for issueance of share dividend and the remuneration packages for the Executive Board. At 31 December 2017, the Company held 121,586 of its own shares (2016: none).

Other reserves

Other reserves are all the reserves other than those shown separately and primarily represent the accumulated, undistributed profits from previous financial years.

Retained earnings

In 2017, the result for 2016 was fully transferred to other reserves. Retained earnings in the 2017 financial statements consequently consist solely of the result for 2017.

9 Earnings per share

Basic earnings per share

The calculation of the basic earnings per share at 31 December 2017 is based on the profit for the period of EUR 19.5 million (2016: EUR 14.9 million) attributable to the holders of ordinary shares and the weighted average number of shares outstanding during the year 2017: 13,446,000 (2016: 13,327,000).

EUR million	2017	2016
Net profit attributable to ordinary shareholders	19.5	14.9

Weighted average number of ordinary shares

In thousands of shares	2017	2016
Issued ordinary shares at 1 January	13,396	13,188
Effect of shares issued as share dividend	115	200
Effect of shares issued as share plan	7	8
Effect of own shares delivered and repurchased	–	–
Ordinary shares outstanding at 31 December	13,518	13,396
Weighted average number of ordinary shares entitled to dividend	13,446	13,327
Basic earnings per share (EUR), based on ordinary shares outstanding at 31 December	1.44	1.11
Basic earnings per share (EUR), based on weighted average shares entitled to dividend	1.45	1.12

Diluted earnings per share

The calculation of the diluted earnings per share at 31 December 2017 is based on the profit of EUR 19.5 million (2016: EUR 14.9 million) attributable to the holders of ordinary shares and the weighted average number of shares in issue during the year, after adjustment for the effects of all dilutive potential ordinary shares amounting to 13,488,000 (2016: 13,333,000).

EUR million	2017	2016
Net profit attributable to ordinary shareholders	19.5	14.9
Effect of dilution	(0.0)	(0.0)
Net profit attributable to ordinary shareholders (diluted)	19.5	14.9

Weighted average number of ordinary shares (diluted)

In thousands of shares	2017	2016
Weighted average numbers of ordinary shares	13,446	13,327
Weighted average numbers of ordinary shares (diluted)	13,488	13,333
Basic earnings per share (EUR), based on weighted average (diluted)	1.44	1.12

10 Loans and borrowings

These notes contain information on the contractual provisions of the Group's interest-bearing loans and borrowings, which are carried at amortised cost price. For further information on the interest rates, and the currency and liquidity risks borne by the Group, see note 15 and accounting policy r.

EUR million	2017	2016
Non-current liabilities		
Bank syndicate loans	46.0	58.0
Mortgage loans	3.0	3.7
Financial lease liabilities	0.1	0.3
Other loans	0.6	1.0
	49.7	63.0

EUR million	2017	2016
Current liabilities		
Current portion loans	0.7	0.7
	0.7	0.7

Financing conditions

At 31 December 2017, the Group had the following credit lines available:

- EUR 150 million revolving Credit Facility with a syndicate of three banks consisting of BNP Paribas, Deutsche Bank and ING Bank. The Credit Facility is committed until 15 August 2019 and includes an option (accordion option) to increase the facility by a maximum of EUR 75.0 million;
- EUR 3.7 million mortgage loan for the premises of the Kuhnke facilities in Malente, Germany. The loan ultimately matures in 2022;
- EUR 0.6 million in subsidised term loans with final maturity in 2019;
- EUR 0.1 million in financial leases for various equipment in Germany;
- EUR 1.0 million in other overdraft facilities.

At 31 December 2017, the total unutilised amount of the facilities was approximately EUR 91 million.

Banking syndicate credit facility

Pursuant to the terms of the credit facility with the banking syndicate, the Group has agreed to financial covenants relating to the leverage ratio (interest bearing debt / EBITDA) and interest coverage (EBITDA / interest costs). In accordance with these covenants, the leverage ratio should remain below 3.0, which can under certain circumstances be temporarily increased to a maximum of 3.5. The interest coverage should always exceed 4.0. Both covenants are tested quarterly on a 12-month rolling basis. The actual leverage ratio at year-end was 1.0 (2016: 1.1) and the actual interest coverage at year-end was 34.0 (2016: 24.5).

Security provided

The Group has provided a mortgage on its premises in Malente, Germany for a EUR 3.7 million loan. No security is provided in relation to the EUR 150 million revolving Credit Facility.

Interest-rate sensitivity

Interest on the EUR 4.4 million other loans is based on fixed-term interest rates. Interest amounts payable on the EUR 150 million revolving Credit Facility are based on short-term interest rate (mainly three months). See note 15 and accounting policy r for further details.

Financial lease liabilities

The financial lease liabilities are payable as follows:

EUR million	2017			2016		
	Minimum lease	Interest	Principal	Minimum lease	Interest	Principal
‹ 1 year	0.1	0.0	0.1	0.3	0.0	0.3
1 – 5 years	–	–	–	0.0	0.0	0.0
› 5 years	–	–	–	–	–	–
	0.1	0.0	0.1	0.3	0.0	0.3

The financial lease liabilities mostly relate to financial leases for various items of equipment in Germany.

11 Employee benefits

EUR million	2017	2016
Present value of unfunded obligations	14.6	16.0
Present value of funded obligations	1.5	6.6
Fair value of plan assets	(0.9)	(4.4)
Recognised net liability for defined benefit obligations	15.2	18.2
Liability for long-service leave and anniversaries	3.9	3.2
Total employee benefits	19.1	21.4

Movement in net liability for defined benefit obligations recognised in the statement of financial position

EUR million	2017	2016
Recognised net liability for defined benefit obligations at 1 January	18.2	17.3
Expense recognised in the consolidated statement of comprehensive income	(1.0)	(0.7)
Benefits paid	(1.0)	(1.0)
Other movements (including currency differences and employer contributions paid)	(0.2)	(0.1)
Actuarial (gains) losses in other comprehensive income	(0.8)	2.7
Recognised net liability for defined benefit obligations at 31 December	15.2	18.2

Movement in plan assets

EUR million	2017	2016
Fair value of plan assets at 1 January	4.4	5.6
Contributions paid employer	0.1	0.1
Contributions paid participants	0.0	0.1
Benefits paid	(0.1)	(0.1)
Assets distributed on settlements and curtailments	(3.5)	(1.1)
Return on plan assets	0.0	0.1
Actuarial gains (losses) in other comprehensive income	0.0	(0.3)
Fair value of plan assets at 31 December	0.9	4.4

Expense recognised in the consolidated statement of comprehensive income regarding defined benefit arrangements

EUR million	2017	2016
Current service costs	0.2	0.2
Past service costs including losses/(gains) on settlements and curtailments	(1.4)	(1.2)
Net interest	0.2	0.3
	(1.0)	(0.7)
Effective return on plan assets	0.0	(0.2)

The expenses relating to the defined benefit pension arrangements are included in the following line items of the statement of comprehensive income:

EUR million	2017	2016
Staff costs	(1.2)	(1.0)
Net finance costs	0.2	0.3
	(1.0)	(0.7)

Principal actuarial assumptions (expressed as weighted averages)

	2017	2016
Discount rate at 31 December	1.5%	0.9%
Future salary increases	0.2%	0.6%
Future pension increases	1.7%	1.7%

Historical information

EUR million	2017	2016	2015	2014	2013
Net liability for defined benefit obligations	16.1	22.6	22.9	22.3	20.6
Fair value of plan assets	0.9	4.4	5.6	5.0	4.8
Deficit in plan	15.2	18.2	17.3	17.3	15.8

Actuarial calculations of employee benefits have not been materially influenced by amendments based on historical experience or by variable assumptions.

Composition plan assets

EUR million	2017	2016
Bonds	0.8	1.8
Equity	0.0	0.9
Real estate	0.0	0.8
Government loans	0.1	0.1
Other	0.0	0.8
Total	0.9	4.4

Sensitivity analysis

	Defined benefit obligation	
EUR million	0.5 percent point increase	0.5 percent point decrease
Discount rate	(0.8)	0.9
Future salary growth	0.0	(0.0)
Future pension	0.6	(0.6)

Liabilities arising from employee benefits

The pension plans included defined contribution plans as well as defined benefit plans. In the case of defined contribution plans, the contribution is charged to the year to which it relates. With defined benefit plans, benefit obligations are calculated using the projected unit credit method. Calculations are made by qualified actuaries. The pension liability shown in the statement of financial position represents the present value of the defined benefit obligation at the financial position date minus the fair value of the plan assets at this date. The discount rate methodology for accounting long-term employee benefits in accordance with IAS 19 is determined by the Executive Board. Significant judgement is required when setting the criteria for bonds to be included in the population from which the yield curve is derived. The most significant criteria considered for the selection of bonds include the issue size of the corporate bonds, quality of the bonds and the identification of outliers which are excluded. The discount rate used to calculate the defined benefit obligation is based on the yield on AA-rated high-quality corporate bonds issued in Euros.

Since the pension arrangements involve long-term obligations and uncertainties, it is necessary to make assumptions in order to estimate the amount that the Group needs to invest to fund its pension obligations. External actuaries calculate the obligation for defined benefit plans partly on the basis of information provided by the Executive Board, such as future pay rises, the return on plan assets, mortality tables and the probable extent to which pension scheme members will leave the scheme because they have reached retirement age, become incapacitated or left the Group.

The greater part of the defined benefit obligation at year-end 2017 relates to post employment arrangements in Germany. The group companies account individually for the pension schemes. The individual group company is fully liable for its benefit obligation. A portion for the German group companies is reinsured. All pension arrangements accounted for as defined benefit obligations are not open for new participants (< 15% active participants) except for the pension arrangement of Kendrion Switzerland. This pension arrangement is a contribution-based plan and pension premiums paid to the multi-employer fund are vested rights for plan participants. Under EU-IFRS the pension arrangement of Kendrion Switzerland is qualifed as a defined benefit plan as Kendrion Switzerland is liable for any shortfall (if any) of the multi-employer fund in which Kendrion Switzerland participates. In 2016 the Group decided to close the manufacturing facility in Switzerland. Closure of the manufacturing facility and corresponding termination of employment contracts qualified as a curtailment in 2016. The curtailment gain amounted to EUR 1.2 million and is recognised as past service credit in 2016, see also note 21. In 2017 the pension arrangement of Kendrion Switzerland is settled and resulted in a settlement gain of EUR 1.4 million. This settlement gain is recognised as service cost credit in 2017, see also note 21.

Liabilities arising from employee benefits also include liabilities relating to long-service, early retirement and service anniversaries of EUR 3.9 million (2016: EUR 3.2 million) in Germany and Austria.

12 Share-based payments

At 31 December 2017, the Group had the following share-based payment arrangements.

Share plan for the Executive Board (equity settled)

Details of the remuneration of the Executive Board are provided in note 26.

Loyalty bonus (equity settled)

The Group had a share incentive programme, which entitled certain managers to purchase shares in the Company for an amount up to 50% of their respective net cash bonuses. Employees who retain these shares for three years and remain in service for three years become entitled to a number of shares equal to the number of shares they individually purchased. Pursuant to this incentive programme, a total of 2,479 shares was issued in 2017, resulting from shares granted in 2014. Expenses recognised in profit or loss for the shares amount to EUR 0.2 million.

Terms & conditions of the share programme (loyalty bonus)

Grant date	Number of instruments	Vesting conditions
Shares granted to key management in 2015	2,160	3 years of service
Shares granted to key management in 2016	1,817	3 years of service
Shares granted to key management in 2017	3,523	3 years of service
Total shares	7,500	

13 Provisions

EUR million	2017	2016
Balance at 1 January	1.2	0.8
Provisions made during the period	0.6	0.8
Provisions transferred/used during the period	(1.0)	(0.4)
Provisions released during the period	–	–
Balance at 31 December	0.8	1.2
Non-current portion	–	–

14 Trade and other payables

EUR million	2017	2016
Trade payables	43.8	41.3
Other taxes and social security contributions	0.9	4.7
Derivatives used for hedging	0.1	0.5
Non-trade payables and accrued expenses	27.5	21.9
	72.3	68.4

15 Financial instruments

Credit risk

The carrying amount of the financial assets represents the maximum credit risk. The maximum credit risk on the reporting date was as follows:

EUR million	2017	2016
Cash and cash equivalents	7.6	12.4
Other long term investments	0.2	0.4
Current income tax	1.0	1.2
Trade and other receivables	58.1	54.5
Total	66.9	68.5

Impairment losses

Aging analysis of the trade and other receivables

EUR million	2017		2016	
	Gross	Provision	Gross	Provision
Within the term of payment	45.8	–	47.3	–
0 – 30 days due	8.9	–	5.7	–
31 – 60 days due	1.5	–	0.7	–
> 60 days due	2.2	(0.3)	0.9	(0.1)
Total trade and other receivables	58.4	(0.3)	54.6	(0.1)

The provision for trade receivables is used to absorb impairment losses, unless the Group is certain that collection of the amount owed is impossible, in which case the amount is treated as a bad debt and written off against the financial asset in question.

At 31 December 2017 the provision for impairment losses on trade and other receivables relates to several customer invoices that the Group believes to be non-collectible, in whole or in part. Based on historic payment behaviour and financial information currently known all receivables that are not impaired at 31 December 2017 are collectible. EUR 3.7 million of trade receivables are 30 days overdue, of which EUR 0.3 million is provided for. The Group has written off less than EUR 0.1 million receivables in 2017 (2016: less than EUR 0.1 million), which are recognised under other operating expenses in the statement of comprehensive income.

The customer with the largest trade receivables outstanding accounted for 6% of the trade and other receivables at 31 December 2017. At 31 December 2016 the largest customer accounted for 7% of total receivables. The geographical credit risk from the Group's direct customers is largely concentrated in Germany. However, as the Group's most important customers in the various segments of the German market are multinational or global players this reduces the Group's dependency on the German market.

Liquidity risk

The contractual terms of the financial obligations, including the estimated interest payments and repayment obligations, are set out below.

31 December 2017 EUR million	Carrying amount	Contractual cash flows	0 – 6 months	6 – 12 months	1 – 2 years	2 – 5 years	› 5 years
Non-derivative financial liabilities							
Bank syndicate loans	46.0	(47.2)	(0.3)	(0.3)	(46.6)	–	–
Finance lease liabilities	0.1	(0.1)	(0.1)	(0.0)	–	–	–
Bank overdrafts	11.7	(11.7)	(11.7)	–	–	–	–
Other loans and borrowings	4.3	(4.9)	(0.6)	(0.6)	(1.2)	(2.5)	–
Trade and other payables	72.3	(72.3)	(72.3)	–	–	–	–
Tax liabilities	1.4	(1.4)	(1.4)	–	–	–	–
Derivative financial liabilities							
Interest rate swap contracts	0.1	(0.1)	(0.0)	(0.0)	(0.1)	(0.0)	–
Forward exchange contracts	–	–	–	–	–	–	–
Total	135.9	(137.7)	(86.4)	(0.9)	(47.9)	(2.5)	–

31 December 2016 EUR million	Carrying amount	Contractual cash flows	0 – 6 months	6 – 12 months	1 – 2 years	2 – 5 years	› 5 years
Non-derivative financial liabilities							
Bank syndicate loans	58.0	(60.1)	(0.4)	(0.4)	(0.8)	(58.5)	–
Finance lease liabilities	0.3	(0.3)	(0.2)	(0.1)	–	–	–
Bank overdrafts	2.7	(2.7)	(2.7)	–	–	–	–
Other loans and borrowings	5.4	(6.1)	(0.6)	(0.6)	(1.2)	(2.9)	(0.8)
Trade and other payables	68.4	(68.4)	(68.4)	–	–	–	–
Tax liabilities	0.7	(0.7)	(0.7)	–	–	–	–
Derivative financial liabilities							
Interest rate swap contracts	0.2	(0.2)	(0.0)	(0.1)	(0.1)	–	–
Forward exchange contracts	0.3	(0.3)	(0.2)	(0.1)	–	–	–
Total	136.0	(138.8)	(73.2)	(1.3)	(2.1)	(61.4)	(0.8)

It is not expected that the cash flows included in the maturity analysis should occur significantly earlier, or at significantly different amounts.

Within the scope of the Group's risk management the Group has hedged the currency and interest risks with derivatives, whereby the hedges have been designated as cash flow hedges. The following table lists the value of these derivatives at financial position date, and when the derivatives will influence profit or loss and cash flows.

Cash flow hedges (in statement of cash flows)

The following table indicates the periods in which the cash flows associated with derivatives that are cash flow hedges are expected to occur.

2017 EUR million	Carrying amount	Contractual cash flows	0 – 6 months	6 – 12 months	1 – 2 years	2 – 5 years	› 5 years
Interest rate swap contracts							
Assets	–	–	–	–	–	–	–
Liabilities	(0.1)	(0.1)	(0.0)	(0.0)	(0.1)	(0.0)	–
Forward exchange contracts							
Assets	0.4	0.4	0.4	0.0	–	–	–
Liabilities	–	–	–	–	–	–	–
Total	0.3	0.3	0.4	0.0	(0.1)	(0.0)	–

2016 EUR million	Carrying amount	Contractual cash flows	0 – 6 months	6 – 12 months	1 – 2 years	2 – 5 years	› 5 years
Interest rate swap contracts							
Assets	–	–	–	–	–	–	–
Liabilities	(0.2)	(0.2)	(0.0)	(0.1)	(0.1)	–	–
Forward exchange contracts							
Assets	–	–	–	–	–	–	–
Liabilities	(0.3)	(0.3)	(0.2)	(0.1)	–	–	–
Total	(0.5)	(0.5)	(0.2)	(0.2)	(0.1)	–	–

Cash flow hedges (in statement of comprehensive income)

The following table indicates the periods in which the cash flows associated with derivatives that are cash flow hedges are expected to impact the result.

2017 EUR million	Carrying amount	Contractual cash flows	0 – 6 months	6 – 12 months	1 – 2 years	2 – 5 years	› 5 years
Interest rate swap contracts							
Assets	–	–	–	–	–	–	–
Liabilities	(0.1)	(0.1)	(0.0)	(0.0)	(0.1)	(0.0)	–
Forward exchange contracts							
Assets	0.4	0.4	0.4	0.0	–	–	–
Liabilities	–	–	–	–	–	–	–
Total	0.3	0.3	0.4	0.0	(0.1)	(0.0)	–

2016 EUR million	Carrying amount	Contractual cash flows	0 – 6 months	6 – 12 months	1 – 2 years	2 – 5 years	› 5 years
Interest rate swap contracts							
Assets	–	–	–	–	–	–	–
Liabilities	(0.2)	(0.2)	(0.0)	(0.1)	(0.1)	–	–
Forward exchange contracts							
Assets	–	–	–	–	–	–	–
Liabilities	(0.3)	(0.3)	(0.2)	(0.1)	–	–	–
Total	(0.5)	(0.5)	(0.2)	(0.2)	(0.1)	–	–

Interest-rate risk

Part of the Group's loans is governed by a floating interest rate (usually 3-month EURIBOR). In view of the Treasury Policy, the Group hedges at least 50% of the floating interest rate exposure. To this extent the Group has outstanding interest rate swaps with a notional amount of in total EUR 50 million. The aggregate fair value of the outstanding interest rate swaps at 31 December 2017 was negative EUR 0.1 million (2016: negative EUR 0.2 million).

The following table shows the interest rates prevailing at the financial position date for interest-bearing financial liabilities. The majority of all interest

expenses relate to senior bank loans. The effective interest rate of these loans equalise the nominal interest rate. The EUR 3.7 million mortgage loan was acquired through business combinations in 2013 and initially recorded at fair value. The effective interest rate of the loan is 3.7%.
Other loans are not provided at an upcount or discount and no incremental transaction costs were incurred when the loans were drawn.

					2017		2016
	Currency	Nominal interest	Year of redemption	Fair value	Carrying amount	Fair value	Carrying amount
Banking syndicate loans	EUR	IBOR + 1.35%	2019	46.0	46.0	58.0	58.0
Mortgage loan	EUR	6.4%	2022	3.9	3.7	4.7	4.4
Other loans	EUR	3.5%	2019	0.6	0.6	1.0	1.0
Bank overdrafts	Various	IBOR + 1.35%	2018	11.7	11.7	2.7	2.7
Finance lease liabilities	EUR	3.0% - 6.5%	2018	0.1	0.1	0.3	0.3
Total interest-bearing debt				62.3	62.1	66.7	66.4

Sensitivity analysis interest

Financial assets and liabilities with a fixed interest rate are not recognised at fair value by processing the value changes in profit or loss.
For this reason a movement in interest rates across the yield curve at 1 January 2017 would not have had a material effect on the 2017 profit for the period.

The Group has hedged a considerable part of the floating interest rate exposure by means of interest rate swaps. When taking into account these swaps and the loans with a fixed rate, in total EUR 54.4 million of the EUR 62.1 million long-term and short-term loans at financial year-end have an interest rate which is fixed for one year or longer. Based on the interest bearing debt levels at year-end and expected cash flow development, a 1% point increase in the interest rate across the yield curve as from 1 January 2018, will have an increasing effect on interest expenses in 2018 of maximum EUR 0.1 million.

Exchange rate risk

The aggregate fair value of the outstanding forward exchange rate contracts concluded to hedge anticipated transactions was positive EUR 0.4 million at 31 December 2017 (2016: negative EUR 0.3 million).

A 10% point appreciation of the currencies listed hereafter against the euro would increase shareholders' equity at 31 December 2017 and the result for 2017 by the amounts shown in the following table. A 10% point depreciation of the listed currencies against the euro would have had the opposite effect. The same analysis was performed for 2016. The same test was done for the profit or loss, where the sensitivities for a 10% appreciation or depreciation on 31 December would have had an impact as is shown below.

31 December 2017	Equity	Result
US dollar	4.7	(0.0)
Czech koruna	0.2	(0.2)
Chinese yuan	0.4	0.1
Rumanian lei	1.2	0.5

31 December 2016	Equity	Result
US dollar	5.1	0.0
Czech koruna	0.2	(0.1)
Chinese yuan	1.2	0.1
Rumanian lei	0.7	0.1

Principal exchange rates during the reporting period were as follows:

Applicable currency rates

Value of EUR	At 31 December 2017	At 31 December 2016	Average over 2017
Pound sterling	0.8872	0.8562	0.8734
Swiss franc	1.1702	1.0739	1.1115
Czech koruna	25.5350	27.0212	26.3331
Chinese yuan	7.8044	7.3202	7.6218
US dollar	1.1993	1.0541	1.1277
Mexican peso	23.6614	21.7718	21.4523
Romanian lei	4.6585	4.5390	4.5703
Swedish krona	9.8438	9.5525	9.6296

Fair values of financial instruments

The following table shows the fair values and carrying amounts of the financial instruments:

EUR million	2017		2016	
	Carrying amount	Fair value	Carrying amount	Fair value
Assets carried at amortised costs				
Receivables (including current tax assets)	59.1	59.1	55.7	55.7
Cash and cash equivalents	7.6	7.6	12.4	12.4
Held to maturity investments	0.2	0.2	0.4	0.4
	66.9	66.9	68.5	68.5
Liabilities carried at amortised costs				
Banking syndicate loans	(46.0)	(46.0)	(58.0)	(58.0)
Mortgage loan	(3.7)	(3.9)	(4.4)	(4.7)
Other loans	(0.6)	(0.6)	(1.0)	(1.0)
Finance lease liabilities	(0.1)	(0.1)	(0.3)	(0.3)
Bank overdraft	(11.7)	(11.7)	(2.7)	(2.7)
Trade and other payables (including current tax liabilities)	(73.7)	(73.7)	(69.1)	(69.1)
	(135.8)	(136.0)	(135.5)	(135.8)
Assets and liabilities carried at fair value				
Interest derivatives	(0.1)	(0.1)	(0.2)	(0.2)
Forward exchange contracts	0.4	0.4	(0.3)	(0.3)
	0.3	0.3	(0.5)	(0.5)

The Group has no available-for-sale financial assets and all liabilities at fair value were designated as such upon initial recognition. The loans and receivables consist of the trade and other receivables, including the current tax assets in the statement of financial position. The held-to-maturity investments are included in the other investments, including derivatives in the statement of financial position. The interest derivatives and forward exchange contracts are included in the trade and other payables in the statement of financial position.

Interest rate used in measuring fair value

The interest rate used for discounting estimated cash flows, where applicable, is based on the swap curve at 31 December 2017, augmented by the prevailing credit mark-up, and is as follows:

	2017	2016
Derivatives	0.0%	0.0%
Leases	1.4%	1.5%
Banking syndicate loans	1.4%	1.5%
Mortgage loans	1.8%	1.8%
Other loans	1.8%	1.8%

Fair value hierarchy

In estimating the fair value of an asset or a liability, the Group uses market-observable data to the extent it is available. The fair value calculation method of all assets and liabilities carried at amortised costs is categorised in level 2 of the fair value hierarchy. The table below analyses financial instruments carried at fair value, by valuation method. The different levels have been defined as follows:

level 1 quoted prices (unadjusted in active markets for identical assets or liabilities);

level 2 inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices);

level 3 inputs for the asset or liability that are not based on observable market data (unobservable inputs).

	Level 1	Level 2	Level 3	Total
31 December 2017				
Derivative contracts used for hedging	–	0.3	–	0.3
Total	–	0.3	–	0.3
31 December 2016				
Derivative contracts used for hedging	–	(0.5)	–	(0.5)
Total	–	(0.5)	–	(0.5)

Master netting

The Company has no master netting agreement in place. All derivative instruments are presented individually as either an asset or liability.

16 Operating lease agreements

Lease contracts for which the Group acts as lessee

The sums payable on non-redeemable operating lease and rental contracts are as follows:

EUR million	2017	2016
< 1 year	4.3	4.4
1 – 5 years	7.3	6.0
> 5 years	3.6	4.8
	15.2	15.2

In the 2017 financial year a charge of EUR 0.5 million was recognised in profit or loss in respect of operating leases (2016: EUR 0.5 million). The operating lease agreements mostly relate to buildings.

17 Capital commitments

As at 31 December 2017 the Group had capital commitments totalling to EUR 7.4 million (2016: EUR 3.9 million).

18 Contingent assets and liabilities

Contingent assets

Kendrion started a court case against the European Union to claim compensation for damages suffered by Kendrion as a result of a breach by the court in the so-called Fardem case of the requirements concerning reasonable time limits for court cases. An amount of EUR 2.3 million was claimed for material damages and an amount of EUR 11 million (being 10% of the penalty for each year of unreasonable delay). Secondary an amount of EUR 1.7 million (being 5% of penalty, in line with another case) was claimed for non-pecuniary damages. On 1 February 2017 the court ruled that the Union must compensate Kendrion in an amount of EUR 588,769 for material damages and an amount of EUR 6,000 for non-pecuniary damages. The Union, represented by the Court of Justice of the European Union, appealed against this decision. Kendrion submitted its defence and also appealed as a response. The Union responded to Kendrion's appeal. In accordance with the procedural requirements, Kendrion requested a court hearing to substantiate its position. The request for a court hearing is still pending.

Contingent liabilties

The Group had guarantees in particular with regard to rentals, financing facilties and post employee benefits totalling to EUR 1.5 million (2016: EUR 1.5 million).

The Group has divested itself of a number of companies in the past. The customary representations and warranties for transactions of this nature are included in the relevant share or asset purchase agreements. The Group, as is customary for transactions of this nature, also issued representations and warranties for potential (tax) claims relating to periods prior to the various divestment dates.

19 Operating segments

The Group, in accordance with IFRS 8, has included general and entity-wide disclosures in these consolidated financial statements.

Geographical segments based on physical location of the Group operating companies

The revenue and non-current assets per geographic area are specified below.

EUR million	Germany		Other European countries		Asia	
	2017	2016	2017	2016	2017	2016
Revenue from transactions with third parties	275.2	274.8	103.5	84.0	21.1	23.4
Other non-current assets	163.9	164.1	22.8	20.3	2.2	1.8
Deferred tax assets	6.5	8.2	4.2	5.1	0.0	0.0
Net liability for defined benefit obligations	14.4	15.9	0.8	2.3	–	0.0

EUR million	The Americas		Consolidated	
	2017	2016	2017	2016
Revenue from transactions with third parties	62.0	61.2	461.8	443.4
Other non-current assets	19.6	24.2	208.5	210.4
Deferred tax assets	1.6	2.7	12.3	16.0
Net liability for defined benefit obligations	–	0.0	15.2	18.2

Revenue segmented by customer location

EUR million	2017	2016
Germany	231.9	223.3
Other European countries	112.1	104.2
Asia	39.4	39.4
The Americas	76.4	74.0
Other countries	2.0	2.5
Total	461.8	443.4

Information about reportable segments

Kendrion has split all activities over two segments: Automotive and Industrial. Based on the structure of the Group and the criteria of IFRS 8 - Operating segments, Kendrion has concluded that within this structure the Kendrion business units are the operating segments within the Group. Based on the aggregation criteria of IFRS 8, these operating segments have been aggregated into two reportable segments: Automotive and Industrial. The automotive activities of the business units Passenger Cars and Commercial Vehicles focus on developing and manufacturing innovative high-quality electromagnetic components, solutions and applications for customers in the automotive industry. These business units have similar economic characteristics and display a number of similarities with respect to their technology, production processes, equipment and customers. The industrial activities of the business units Industrial Magnetic Systems, Industrial Control Systems and Industrial Drive Systems focus on developing and manufacturing electromagnetic systems and components for industrial applications. These business units also have similar economic characteristics and display a number of similarities with respect to their technology, production processes, equipment and customers.

EUR million	Industrial		Automotive		Corporate activities		Consolidated	
	2017	2016	2017	2016	2017	2016	2017	2016
Revenue from transactions with third parties	162.5	152.3	299.3	291.1	–	–	461.8	443.4
Inter-segment revenue	0.1	0.1	0.5	0.8	–	–	0.6	0.9
EBITA	15.9	9.8	16.7	16.5	(0.7)	(0.9)	31.9	25.4
EBITA margin	9.8%	6.4%	5.6%	5.7%	–	–	6.9%	5.7%
EBITA*	16.9	11.6	20.8	19.9	(0.7)	(0.4)	37.0	31.1
EBITA margin*	10.4%	7.6%	6.9%	6.8%			8.0%	7.0%
Reportable segment assets	116.0	113.1	214.6	213.4	14.2	20.6	344.8	347.1

Major customers

Three customers (Volkswagen, Daimler and ThyssenKrupp Bilstein) individually account for more than 5% of the company's total revenue.

20 Other income

EUR million	2017	2016
Net gain on disposal of property, plant and equipment	0.0	0.0
Other	0.0	0.1
	0.0	0.1

* Excluding one-off costs related to the simplyfing measures. The bridge from reported to normalised figures can be found on page 35.

21 Staff costs

EUR million	2017	2016
Wages and salaries	107.5	106.5
Social security charges	19.5	19.5
Temporary personnel	4.7	3.6
Contributions to defined contribution plans	0.4	0.4
Expenses related to defined benefit plans	(1.2)	(0.9)
Increase in liability for long-service leave	0.1	0.1
Other costs of personnel	3.2	3.4
	134.2	132.6
Total number of employees and temporary workers at 31 December (FTE)	2,645	2,578

The staff costs 2017 include EUR 3.2 million one-off costs related to the simplifying measures (2016: EUR 3.4 million).

22 Other operating expenses

EUR million	2017	2016
Lease expenses	0.5	0.5
Increase in provision for doubtful debts	0.1	(0.1)
Premises costs	8.9	8.1
Maintenance expenses	6.5	5.7
Transport expenses	1.7	1.7
Consultancy expenses	5.6	5.8
Sales and promotion expenses	1.9	3.2
Car, travel and representation costs	3.9	4.1
Other	5.2	5.7
	34.3	34.7

The other operating expenses 2017 include EUR 1.7 million one-off costs related to the simplifying measures (2016: EUR 1.7 million).

Research & Development expenses (including staff and other operating expenses) for 2017 totalled EUR 28.3 million (2016: EUR 27.6 million).

23 Net finance costs

EUR million	2017	2016
Interest income	0.1	0.1
Net exchange gain	–	–
Finance income	0.1	0.1
Interest expense	(2.2)	(2.5)
Interest expense related to employee benefits	(0.2)	(0.3)
Net exchange loss	(0.6)	(0.4)
Finance expense	(3.0)	(3.2)
Net financing costs	(2.9)	(3.1)

On the closure of our operation in Brazil in 2016, the cumulative amount of translation differences in equity were reclassified from equity to profit or loss. This had a negative impact of EUR 0.4 million on the net exchange loss.

24 Income tax

EUR million	2017	2016
Current tax charge on year under review	(6.3)	(3.7)
Total corporation tax expenses in the income statement	(6.3)	(3.7)

25 Reconciliation of effective tax rate

	Reconciliation effective tax rate		Reconciliation in EUR million	
	2017	2016	2017	2016
Profit before income tax			25.8	18.6
Income tax expense at local corporation tax rate	25.0%	25.0%	6.5	4.7
Non-deductible expenses	1.1%	1.9%	0.3	0.3
Effect of tax rates in foreign jurisdictions	(0.8)%	(3.0%)	(0.2)	(0.6)
Tax exempt income	(2.9)%	(4.5%)	(0.8)	(0.8)
Changes in estimates related to prior years	0.2%	1.4%	0.1	0.3
Utilisation of previously unrecognised tax losses	(0.8)%	(3.2%)	(0.2)	(0.6)
Current-year losses for which no deferred tax asset is recognised	1.3%	1.8%	0.3	0.3
Other movements	1.3%	0.4%	0.3	0.1
	24.4%	19.8%	6.3	3.7

26 Related parties

Identity of related parties

A related-party relationship exists between the Company and its subsidiaries, their managers and executives. The Company has a number of agreements with its subsidiaries relating to the charging of central costs to and from the business units, including management, development, information technology and marketing costs, as well as agreements in respect of Group financing and use of intellectual property. Internal supplies are also obtained within the business units. Intercompany transactions are effected at arm's length market prices. As all subsidiaries are fully consolidated and reflected in these financial statements, the amounts of these transactions are not further specified. For a list of the principal subsidiaries, see pages 163 and 164.

Compensations of key management personnel

The remuneration of the Executive Board and Supervisory Board is as follows:

EUR thousand	2017	2016
Short-term benefits	1,098.7	1,098.0
Post-employment benefits	150.0	150.0
Other long-term benefits	–	–
Share-based payments	423.6	331.5*
Termination benefits	–	–
	1,672.3	1,579.5

The total remuneration is included in staff costs (see note 21). For a description of the remuneration policy of the members of the Executive Board, see pages 73 to 75.

The achievement of the performance criteria set for 2017 was 90% for the CEO (2016: 97%). CEO will, based on this performance, receive a variable remuneration of 36% of his gross fixed remuneration. The CEO's gross variable remuneration amounts to EUR 170,748 (2016: EUR 180,420) of which EUR 56,916 (2016: EUR 60,140) will be paid in cash. An amount of EUR 113,832 (2016: EUR 120,280) is awarded conditionally in shares on the basis of the closing share price on 9 April 2018. The vesting period ends in 2019 and the holding period ends in 2021.

The achievement of the performance criteria set for 2017 was 90% for the CFO (2016: 97%). CFO will, based on this performance, receive a variable remuneration of 32% of his gross fixed remuneration. The CFO's gross variable remuneration amounts to EUR 102,251 (2016: EUR 108,042) of which EUR 34,084 (2016: EUR 36,014) will be paid in cash. An amount of EUR 68,167 (2016: EUR 72,028) is awarded conditionally in shares on the basis of the closing share price on 9 April 2018. The vesting period ends in 2019 and the holding period ends in 2021. 2/3 of the gross annual variable remuneration is invested in shares. The number of shares granted to the CFO in 2015 is 1,451 net (3,024 shares gross). The variable remuneration is supplemented with a share match. On the basis of the long-term variable remuneration policy

* Revised to include the impact of the long-term variable share based payment compensation expense of the Executive Board.

applicable Kendrion will, depending on the long-term performance criteria, increase the number of shares awarded in 2015 on a gross basis by 50% net (a matching ratio of 1:2). The Supervisory Board has decided that the CFO achieved 100% of his long-term performance criteria for the period 2015-2017. This means that 1,512 shares will be matched (3,024 x 0.5 x 100%). The holding period of these shares ends in 2019. The amount charged to the profit or loss regarding the long-term variable remuneration policy was EUR 241,570 (2016: EUR 139,269).

The vesting and holding periods for shares awarded to the CEO and CFO are specified as follows:

Description	Number of shares	Vesting period	Holding period
Shares granted to the CFO (variable remuneration 2013)	1,044	–	End of 2017
Shares granted to the CFO (variable remuneration 2014)	1,451	–	End of 2018
Shares granted to the CFO (variable remuneration 2015)	2,083	End of 2017	End of 2019
Shares granted to the CFO (share match 2014-2016)*	816	–	End of 2018
Shares granted to the CEO (variable remuneration 2016)	3,970	End of 2018	End of 2020
Shares granted to the CFO (variable remuneration 2016)	2,377	End of 2018	End of 2020
Shares granted to the CFO (share match 2015-2017)	1,512	–	End of 2019

Pensions

The Executive Board participates in the defined contribution plan of the Company. The contribution was EUR 32,473 (2016: EUR 30,138) for the CEO, Mr Van Beurden and EUR 32,515 (2016: EUR 29,048) for the CFO, Mr Sonnemans.

Transactions with shareholders

There were no transactions with shareholders.

27 Post-balance sheet events

There were no post-balance sheet events that have to be taken into account in the consolidated financial statements for the year ended 31 December 2017.

28 Other notes

The subsidiary Kendrion Holding Germany GmbH, Villingen-Schwenningen, Germany included in these consolidated financial statements makes use of § 264b HGB (German Commercial Code). In accordance with that rule, the financial statements of Kendrion Holding Germany GmbH as of 31 December 2017 were not published.

The subsidiary Kendrion (UK) Ltd. (registration number 1124810), Bradford, United Kingdom included in these consolidated financial statements is exempt from the requirements of section 479A (audit of accounts) of the Companies Act 2006.

* The number of shares granted under the LTI scheme for 2014-2016 was increased from 392 to 816 to correctly account for the tax gross-up effect.

COMPANY BALANCE SHEET AT 31 DECEMBER

(before profit appropriation)

Note	EUR million	2017	2016
	Non-current assets		
	Property, plant and equipment	0.0	0.1
	Intangible assets	–	0.0
	Other investments, including derivatives	0.1	0.2
1.3	Financial assets	211.4	210.7
	Total non-current assets	**211.5**	**211.0**
	Current assets		
1.4	Receivables	0.6	0.8
	Cash and cash equivalents	0.0	0.0
	Total current assets	0.6	**0.8**
	Total assets	**212.1**	**211.8**
1.5	**Equity**		
	Share capital	27.0	26.8
	Share premium	49.6	56.4
	Legal reserves	7.0	12.9
	Other reserves	77.2	67.1
	Retained earnings	19.5	14.9
	Total equity	**180.3**	**178.1**
1.6	**Current liabilities**		
	Loans and borrowings	29.8	29.1
	Payables	2.0	4.6
	Total current liabilities	**31.8**	**33.7**
	Total equity and liabilities	**212.1**	**211.8**

COMPANY INCOME STATEMENT

Note	EUR million	2017	2016
	Revenue	–	–
1.8	Other income	4.2	22.6
	Total revenue and other income	**4.2**	**22.6**
1.9	Staff costs	3.0	3.6
	Depreciation and amortisation	0.0	0.0
	Other operating expenses	1.8	2.1
	Result before net finance costs	**(0.6)**	**16.9**
	Finance income	0.1	0.2
	Finance expense	(1.0)	(1.3)
	Net finance costs	**(0.9)**	**(1.1)**
	Profit before income tax	**(1.5)**	**15.8**
	Income tax expense	(0.3)	(4.1)
	Profit for the period	**(1.8)**	**11.7**
	Share in results of Group companies after tax	21.3	3.2
1.10	**Net profit**	**19.5**	**14.9**

1 Notes to the company financial statements

1.1 General

The Company financial statements are part of the 2017 financial statements of Kendrion N.V. (the ‘Company’). The Company is registered at the Chamber of Commerce in The Netherlands under number: 30113646.

1.2 Principles of valuation of assets and liabilities and determination of results

In selecting the principles employed in the company financial statements for the valuation of assets and liabilities and determination of results, Kendrion N.V. has made use of the option provided by Section 362, subsection 8, of Book 2 of the Netherlands Civil Code. Consequently, the principles employed in the Company financial statements of Kendrion N.V. for the valuation of assets and liabilities and determination of results (the ‘accounting policies’) are identical to those employed in the consolidated EU-IFRS financial statements. Interests in entities in which Kendrion N.V. has significant influence are measured using the equity method. The consolidated EU-IFRS financial statements have been prepared in accordance with the standards adopted by the International Accounting Standards Board as endorsed for use in the European Union (hereinafter referred to as ‘EU-IFRS’). These policies are discussed in notes a – r.

1.3 Financial fixed assets

EUR million	Interest in Group companies	Loans to Group companies	Deferred tax	Total 2017	Total 2016
Carrying amount at 1 January	193.6	16.0	1.1	210.7	194.9
Results of Group companies	21.3	–	–	21.3	3.2
Movements in loans and borrowings	–	(13.9)	–	(13.9)	13.9
Movements in deferred tax assets	–	–	(0.2)	(0.2)	(4.1)
Other movements	(6.5)	–	–	(6.5)	2.8
Carrying amount at 31 December	208.4	2.1	0.9	211.4	210.7

The main portion of the loans to Group companies has a duration of over one year.

The investments in the principal subsidiaries and associates are disclosed on pages 159 and 160 of the Annual Report.

1.4 Receivables

EUR million	2017	2016
Receivables from Group companies	0.4	0.5
Prepayments and accrued income	0.2	0.3
	0.6	0.8

All receivables are due within one year.

1.5 Equity

EUR million	Share capital	Share premium	Translation reserve	Hedge reserve	Reserve for participations	Reserve for own shares	Other reserves	Retained earnings	Total 2017	Total 2016
Balance at 1 January	26.8	56.4	11.6	(0.3)	1.6	–	67.1	14.9	178.1	169.9
Appropriation of retained earnings	–	–	–	–	–	–	14.9	(14.9)	–	–
Foreign currency translation differences	–	–	(7.6)	–	–	–	–	–	(7.6)	1.3
Net change in fair value of cash flow hedges, net of income tax	–	–	–	0.6	–	–	–	–	0.6	(0.2)
Issue of ordinary shares	0.2	3.5	–	–	–	–	–	–	3.7	4.2
Own shares repurchased	–	–	–	–	–	(4.5)	–	–	(4.5)	–
Share-based payment transactions	0.0	0.2	–	–	–	–	0.2	–	0.4	0.2
Dividend payment	–	(10.5)	–	–	–	–	–	–	(10.5)	(10.3)
Other	–	–	–	–	1.1	–	(0.5)	–	0.6	(1.9)
Total recognised income and expenses	–	–	–	–	–	–	–	19.5	19.5	14.9
Balance at 31 December	27.0	49.6	4.0	0.3	2.7	(4.5)	81.7	19.5	180.3	178.1

1.5.1 Share capital

The authorised capital of the Company amounts to EUR 80 million, divided into 40 million ordinary shares of EUR 2.00, of which 13,517,620 ordinary shares have been issued.

1.5.2 Share premium

The share premium represents revenue from shares issued at more than their nominal value (issued above par). The issued and paid share capital, including share premium, is fiscally recognised capital.

1.5.3 Translation reserve

The translation reserve comprises all foreign currency differences arising from the translation of the financial statements of associates outside the euro zone. Gains and losses relating to the translation risk are recognised in equity. The build-up of the cumulative figure commenced on 1 January 2004.

1.5.4 Hedge reserve

The hedge reserve comprises the effective share of the cumulative net movement in the fair value of cash-flow hedging instruments relating to hedged transactions that have not yet been executed.

1.5.5 Statutory reserve for participations

This reserve pertains to participating interests that are accounted for according to the equity accounting method. The reserve represents the difference between the participating interests' retained profit and direct changes in equity, as determined on the basis of the Company's accounting policies, and the share thereof that the Company may distribute. It is shown as the share in the undistributed results of the subsidiaries since they were first valued using the equity method. The amount of any dividend – from these subsidiaries – to which there is an entitlement on adoption of the financial statements is deducted from this reserve.

1.5.6 Reserve for own shares

The reserve for the Company's own shares comprises the cost of the Company shares that are held by the Company for the remuneration package for the Executive Board. At 31 December 2017, the Company held 121,586 of its own shares (2016: none).

1.5.7 Other reserves

Other reserves are all the reserves other than those shown separately and comprise primarily the cumulative, undistributed profits from previous financial years.

1.5.8 Retained earnings

In 2017, the full result for 2016 was included in other reserves. Retained earnings consequently consist solely of the result for 2017.

1.6 Current liabilities

EUR million	2017	2016
Debts to Group companies	29.8	29.1
Trade payables	0.6	0.3
Other payables and accrued expenses	1.4	4.3
	31.8	33.7

1.7 Financial instruments

See note 15 to the consolidated financial statements for details on financial instruments.

1.8 Other income

EUR million	2017	2016
Management fee	4.2	5.4
Logo fee	–	2.7
Other	–	14.5
	4.2	22.6

The amount of EUR 14.5 million refers to the transfer of the Kendrion brand name to Kendrion Marketing B.V.

1.9 Staff costs

EUR million	2017	2016
Wages and salaries	2.4	2.9
Social security charge	0.1	0.1
Pension costs	0.3	0.3
Other costs of personnel	0.2	0.3
	3.0	3.6
Total number of employees and temporary workers at 31 December (FTE)	11	11

The average number of FTEs during the year was 11 (2016: 11). The Company has only defined contribution plans for its employees.

1.10 Profit appropriation

Appropriation of net profit

EUR million	2017	2016
Net profit	19.5	14.9

The Executive Board has decided, with the approval of the Supervisory Board, that the net profit of EUR 19.5 million will be added to the other reserves.

1.11 Commitments not appearing on the balance sheet

1.11.1 Joint and several liability and guarantees

The Company and its Group companies have issued guarantees mainly in the context of the financing by financial institutions.
The Company has issued declarations of joint and several liability, as referred to in Section 403 of Book 2 of the Netherlands Civil Code, for:

- Combattant Holding B.V., Zeist;
- Kendrion Finance B.V., Zeist.

1.11.2 Fiscal unity

The Company and its Dutch subsidiaries excluding Landfort II B.V. and Kendrion Marketing B.V. form a tax group for corporation tax purposes. According to the standard terms, each of the companies is jointly and severally liable for corporation tax payable by all the members of the fiscal unity.

1.12 Post balance sheet events

There were no post-balance sheet events that have to be taken into account in the consolidated financial statements for the year ended 31 December 2017.

1.13 Fees to the auditor

With reference to Section 2:382a of the Netherlands Civil Code, the following fees have been charged by Deloitte Accountants B.V. and its member firms and affiliates in 2017 and 2016 to the Company, its subsidiaries and other consolidated entities:

EUR thousand			2017			2016
	Deloitte Accountants B.V.	Other Deloitte member firms and affiliates	Total Deloitte	Deloitte Accountants B.V.	Other Deloitte member firms and affiliates	Total Deloitte
Audit of financial statements	161.1	266.3	427.4	163.0	268.8	431.8
Other assurance services	32.5	–	32.5	46.5	–	46.5
Tax advisory services	–	–	–	–	–	–
Other non-audit services	–	–	–	–	4.0	4.0
Total	193.6	266.3	459.9	209.5	272.8	482.3

1.14 Remuneration of and share ownership by the Executive Board and Supervisory Board

Remuneration of the Executive Board

The remuneration of current Executive Board members charged to the Company and Group companies, including pension expenses as referred to in Section 383, subsection 1, of Book 2 of the Netherlands Civil Code, amounted to EUR 1,486,300 (2016: EUR 1,426,500). This remuneration is as follows:

EUR thousand			2017			2016
	J.A.J. van Beurden	F.J. Sonnemans	Total	J.A.J. van Beurden	F.J. Sonnemans	Total
Fixed remuneration	474.3	324.6	798.9	465.0	318.2	783.2
Short-term variable remuneration	170.7	102.3	273.0	180.4	108.0	288.4
Long-term variable remuneration	35.7	205.9	241.6	46.5	92.8	139.3*
Total remuneration	680.7	632.8	1,313.5	691.9	519.0	1,210.9
Pension and other expenses	87.3	85.5	172.8	130.4	85.2	215.6
	768.0	718.3	1,486.3	822.3	604.2	1,426.5

The 2017 short-term variable remuneration will be granted directly after the General Meeting of Shareholders to be held on 9 April 2018. Part (1/3) of the variable remuneration will be paid in cash after income tax and other part (2/3) will be covered conditionally for in shares against the prevailing closing share price of 9 April 2018.

For more information on the long-term variable remuneration see pages 136 and 137.

* Revised to include the impact of the long-term variable share based payment compensation expense of the Executive Board.

Remuneration of the Supervisory Board

The total remuneration of current and former Supervisory Board members in 2017 amounts to EUR 186,000 (2016: EUR 153,000). This remuneration is as follows:

EUR thousand	2017	2016
H. ten Hove	50	45
M.J.G. Mestrom (appointed as of 11 April 2016)	41	35
J.T.M. van der Meijs (appointed as of 31 October 2016)	41	9
T.J. Wünsche (appointed as of 31 October 2016)	40	20
R.L. de Bakker (stepped down as from 10 April 2017)	14	35
M.E.P. Sanders (stepped down as from 11 April 2016)	–	9
	186	153

No loans, advances or related guarantees have been given to the Executive Board or Supervisory Board members.

Share ownership by the Executive Board and the Supervisory Board

		31 December 2017	31 December 2016
Executive Board	J.A.J. van Beurden	21,233	20,773
	F.J. Sonnemans	2,995	1,082
Supervisory Board		–	–

Zeist, 20 February 2018

Executive Board	**Supervisory Board**
J.A.J. van Beurden	H. ten Hove
F.J. Sonnemans	M.J.G. Mestrom
	J.T.M. van der Meijs
	T.J. Wünsche

Provisions in the Articles of Association governing the appropriation of profit

Under article 35.1 and 35.2 of the Articles of Association of the Company, the Executive Board shall, with the approval of the Supervisory Board, determine which part of the profits is added to the reserves. The profit remaining after transfer to the reserves is available to the General Meeting of Shareholders. The Company can only make payments to the shareholders and other parties entitled to the distributable profit insofar as the shareholders' equity exceeds the paid-up and called-up part of the capital plus the statutory reserves and exceeds the amounts resulting from the distribution test, performed by the Executive Board at the date of each dividend payment.

To: the Shareholders and Supervisory Board of Kendrion N.V.

Independent auditor’s report

Report on the audit of the financial statements 2017

Our opinion

We have audited the financial statements 2017 of Kendrion N.V. (‘the Company’), based in Zeist. The financial statements include the consolidated financial statements and the company financial statements as set out on the pages 77 up to and including 146.

In our opinion:

- The consolidated financial statements give a true and fair view of the financial position of Kendrion N.V. as at 31 December 2017 and of its result and its cash flows for 2017 in accordance with International Financial Reporting Standards as adopted by the European Union (‘EU-IFRS’) and with Part 9 of Book 2 of the Dutch Civil Code.
- The company financial statements give a true and fair view of the financial position of Kendrion N.V. as at 31 December 2017 and of its result for the year 2017 in accordance with Part 9 of Book 2 of the Dutch Civil Code.

The consolidated financial statements comprise:

- The consolidated statement of financial position as at 31 December 2017;
- The following statements for 2017: the consolidated statement of comprehensive income, the consolidated statement of changes in equity and the consolidated statement of cash flows; and
- The notes to the consolidated financial statements, comprising a summary of the significant accounting policies and other explanatory information.

The company financial statements comprise:

- The company balance sheet as at 31 December 2017;
- The company income statement for 2017; and
- The notes to the company financial statements comprising a summary of the significant accounting policies and other explanatory information.

Basis for our opinion

We conducted our audit in accordance with Dutch law, including the Dutch Standards on Auditing. Our responsibilities under those standards are further described in the ‘Our responsibilities for the audit of the financial statements’ section of our report.

We are independent of Kendrion N.V. in accordance with the EU Regulation on specific requirements regarding statutory audit of public-interest entities, the Wet toezicht accountantsorganisaties (Wta, Audit firms supervision act), the Verordening inzake de onafhankelijkheid van accountants bij assurance-opdrachten (ViO, Code of Ethics for Professional Accountants, a regulation with respect to independence) and other relevant independence regulations in the Netherlands. Furthermore we have complied with the Verordening gedrags- en beroepsregels accountants (VGBA, Dutch Code of Ethics).

We believe the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion

Materiality

Misstatements can arise from fraud or error and are considered material, if individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements. The materiality affects the nature, timing and extend of our audit procedures and the evaluation of the effect of identified misstatements on our opinion.

Based on our professional judgement we determined the materiality for the financial statements as a whole at EUR 1.4 million (2016: EUR 1.4 million). The materiality is based on 7.5 percent of 2016 profit before taxation. We reassessed the group materiality level based on the 2017 actual profit before tax and alternative benchmarks. We have also taken into account misstatements and/or possible misstatements that in our opinion are material for the users of the financial statements for qualitative reasons.

Audits of group entities (components) were performed using materiality levels determined by the judgement of the group audit team, having regard to the materiality of the consolidated financial statements as a whole. Component materiality did not exceed 60% of group materiality and for most components, materiality is significantly less than this.

We agreed with the Supervisory Board that misstatements in excess of EUR 70 thousand, which are identified during the audit, would be reported to them, as well as smaller misstatements that, in our view, must be reported on qualitative grounds.

Scope of the group audit

Kendrion N.V. is at the head of a group of entities. The financial information of this group is included in the consolidated financial statements of Kendrion N.V.

Because we are ultimately responsible for the opinion, we are also responsible for directing, supervising and performing the group audit. In this respect we have determined the nature and extent of the audit procedures to be carried out for the group entities (components). Decisive were size and/or risk profile of the components. On this basis, we selected components for which an audit or review had to be carried out on the complete set of financial information or specific items.

Kendrion N.V. is divided into two reportable segments, as disclosed in note 19 of the consolidated financial statements. These two reportable segments encompass 36 reporting entities (‘components’). The most significant components are Kendrion (Eibiswald) GmbH, Kendrion (Villingen) GmbH, Kendrion (Donaueschingen/Engelswies) GmbH, Kendrion Kuhnke Automotive GmbH and Kendrion (Shelby) Inc. which on a combined basis contribute approximately 65% of the consolidated revenue.

Our group audit mainly concentrated on significant components in terms of size and financial interest or where significant risks or complex activities were present, leading to full scope audits performed for 13 components.

We have performed audit procedures ourselves at corporate entities and we have carried out full scope audit procedures on Kendrion (Shelby) Inc. Furthermore, we performed audit procedures at group level on areas such as consolidation, reporting, goodwill and taxation. Specialists were involved amongst others in the areas of information technology, tax, pensions and valuation.

For all relevant foreign components, the group audit team provided detailed written instructions, which, in addition to communicating the requirements of component audit teams, detailed significant audit areas and information obtained centrally relevant to the audit of individual components including awareness for risk related to management override. Furthermore, we developed a plan for overseeing each component audit team based on its relative significance to the Company and certain other risk characteristics. This included procedures such as visiting components and/or component teams in Germany and the United States, performing file reviews, holding conference calls, attending meetings and reviewing component audit team deliverables to gain sufficient understanding of the work performed. For smaller components we have performed review procedures or specific audit procedures.

Considering their share in consolidated revenue, 95% of the components is subject to audit procedures. Desk-top review procedures have been performed in respect of the components that have not been audited.

By performing the procedures mentioned above we have been able to obtain sufficient and appropriate audit evidence on the group's financial information to provide an opinion on the consolidated financial statements.

Our key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial statements. We have communicated the key audit matters to the Supervisory Board. The key audit matters are not a comprehensive reflection of all matters discussed.

These matters were addressed in the context of our audit of the financial statements as a whole and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Key audit matter – decentralized operations	How the key audit matter was addressed in the audit
Kendrion is a group with all operating activities taking place outside The Netherlands. These decentralized operations require adequate monitoring activities from an internal control perspective. Also in our role as group auditor it is essential that we obtain an appropriate level of understanding of the components and the component audit work.	We have evaluated the group's internal controls, including centralized monitoring controls that exist at both group and segment level. The group has developed an internal control framework with control activities that are required to be implemented by the components. Compliance with this framework is monitored through Kendrion In Control (KIC) procedures, performed by experienced staff from the finance and control team, notably at head office level. As explained in the 'Risk and risk management' paragraph of the Executive Board report, KIC procedures were performed at several locations with limited control deficiencies revealed. In our audit approach we have specifically focused on risks in relation to decentralized structure and we have been closely involved in the audits performed at the most significant components. Members of the group team performed the audit of Kendrion (Shelby) Inc. and also reviewed reporting deliverables and selected files from the component audit teams. We also performed tests on consolidation adjustments and manual journal entries, both at group and component level to obtain an understanding of significant entries made. We believe that the scope of our procedures was appropriate and sufficient to address the key audit matter.

Key audit matter – reallocation of goodwill and valuation of goodwill

The Simplify, Focus, Grow strategy, announced on May 2016, resulted in a further integration of Kendrion's business units. The changes in the organization have affected the Cash Generating Units (CGU) structure and a re-assessment of the CGU structure has been performed by the Company resulting in a reallocation of goodwill.

The Company performed the annual goodwill impairment test during the fourth quarter of 2017. The outcome of the annual goodwill impairment test did not lead to an impairment charge. The assumptions and sensitivities in the impairment test are disclosed in note 2 to the consolidated financial statements. These sensitivities analysis are significant to our audit procedures audit because the assessment process is complex and requires management judgement, and is based on assumptions that are affected by expected future market conditions.

How the key audit matter was addressed in the audit

We have reviewed the impairment model and involved valuation experts in understanding the models used and the key assumptions applied. We tested the allocation of goodwill to the new CGUs and ensured that his related appropriately to the new CGUs.

We have evaluated the internal controls related to the preparation of the impairment model and the review of the forecasted cash flows, growth rates, discount rates and other relevant assumptions. In our audit procedures we also compared actual performance to previous assumptions applied to understand the quality of the estimates and address the risk of bias. Furthermore we compared the input with financial plans, applicable FX rates and other available information. Our valuation specialists assisted us evaluating and challenging the assumptions and metholodigies applied by Kendrion N.V. in its impairment model.

Finally we have assessed the adequacy of disclosure notes including those relating to the sensitivity of management's assumptions. Reference is made to note 2 of the consolidated financial statements. Our audit procedures are deemed appropriate and sufficient to address the risks of material misstatements.

Report on the other information included in the Annual Report
In addition to the financial statements and our auditor's report, the annual report contains other information that consists of:

- Report of the Executive Board;
- Report of the Supervisory Board;
- Other Information pursuant to Part 9 of Book 2 of the Dutch Civil Code; and
- Other information included in the Annual Report.

Based on the following procedures performed, we conclude that the other information:

- Is consistent with the financial statements and does not contain material misstatements; and
- Contains the information as required by Part 9 of Book 2 of the Dutch Civil Code.

We have read the other information. Based on our knowledge and understanding obtained through our audit of the financial statements or otherwise, we have considered whether the other information contains material misstatements.

By performing these procedures, we comply with the requirements of Part 9 of Book 2 of the Dutch Civil Code and the Dutch Standard 720. The scope of the procedures performed is less than the scope of those performed in our audit of the financial statements.

Management is responsible for the preparation of other information, including the Report of the Executive Board in accordance with Part 9 of Book 2 of the Dutch Civil Code and other information pursuant to Part 9 of Book 2 of the Dutch Civil Code.

Engagement
We were appointed by the Annual General Meeting as auditor of Kendrion N.V. on 13 April 2015 for the audit of the years 2015, 2016 and 2017 and have operated as statutory auditor since that financial year.

No prohibited non-audit services
We have not provided prohibited non-audit services as referred to in Article 5(1) of the EU Regulation on specific requirements regarding statutory audit of public-interest entities.

Responsibilities of the Executive Board and the Supervisory Board for the Financial Statements
The Executive Board is responsible for the preparation and fair presentation of the financial statements in accordance with EU-IFRS and Part 9 of Book 2 of the Dutch Civil Code, and for the preparation of the Report of the Executive Board in accordance with Part 9 of Book 2 of the Dutch Civil Code. Furthermore, the Executive Board is responsible for such internal control as the Executive Board determines is necessary to enable the preparation of the financial statements that are free from material misstatement, whether due to fraud or error.

As part of the preparation of the financial statements, the Executive Board is responsible for assessing the Company's ability to continue as a going concern. Based on the financial reporting frameworks mentioned, the Executive Board should prepare the financial statements using the going concern basis of accounting unless management either intends to liquidate the company or to cease operations, or has no realistic alternative but to do so. The Executive Board should disclose events and circumstances that may cast significant doubt on the Company’s ability to continue as a going concern in the financial statements.

The Supervisory Board is responsible for overseeing the Company’s financial reporting process.

Our responsibilities for the audit of the financial statements

Our objective is to plan and perform the audit assignment in a manner that allows us to obtain sufficient and appropriate audit evidence for our opinion.

Our audit has been performed with a high, but not absolute, level of assurance, which means we may not have detected all errors and fraud.

Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements. The materiality affects the nature, timing and extent of our audit procedures and the evaluation of the effect of identified misstatements on our opinion.

For an overview of our responsibilities we refer to NBA’s website www.nba.nl (standard texts auditor's report).

Amsterdam, 20 February 2018

Deloitte Accountants B.V.

B. E. Savert

To: the Shareholders and Supervisory Board of Kendrion N.V.

Assurance report of the independent auditor with respect to the 2017 Sustainability Information of Kendrion N.V.

Our conclusion

We have reviewed the Sustainability Information in the 2017 Annual Report of Kendrion N.V. at Zeist. A review is aimed at obtaining a limited level of assurance.

Based on our procedures performed nothing has come to our attention that causes us to believe that the sustainability information does not present, in all material respects, a reliable and adequate view of:

- the policy and business operations with regard to sustainability; and
- the thereto related events and achievements for the year 2017

in accordance with the Sustainability Reporting Guidelines of the Global Reporting Initiative (GRI G4 Core option) and the applied supplemental reporting criteria as disclosed in the chapter 'About the CSR review' of the 2017 Annual Report.

The sustainability information consists of performance information regarding Energy consumption, Absolute- and Relative CO_2-emissions, Accidents and Lost Time Injuries, Acceptance of Supplier Code of Conduct and Number of Supplier audits in the section 'Facts and Figures' on page 11 and the section 'Corporate Responsibility Review' on page 41 of the 2017 Annual Report (hereafter: 'the KPIs').

Basis of our conclusion

We have performed our review on the sustainability information in accordance with Dutch law, including Dutch Standard 3810N 'Assurance-opdrachten inzake maatschappelijke verslagen' (Assurance engagements relating to sustainability reports) which is a specified Dutch Standard that is based on the International Standard on Assurance Engagements (ISAE) 3000 'Assurance Engagements other than Audits or Reviews of Historical Financial Information'. This assurance engagement is aimed at obtaining limited assurance. Our responsibilities under this standard are further described in the section 'Our responsibilities for the review of the sustainability information'.

We are independent of Kendrion N.V. in accordance with the EU Regulation on specific requirements regarding statutory audit of public-interest entities, the 'Wet toezicht accountantsorganisaties' (Wta, Audit firms supervision act), the 'Verordening inzake de onafhankelijkheid van accountants bij assurance-opdrachten' (ViO, Code of Ethics for Professional Accountants, a regulation with respect to independence) and other relevant independence regulations in the Netherlands. Furthermore we have complied with the 'Verordening gedrags- en beroepsregels accountants' (VGBA, Dutch Code of Ethics).

We believe that the assurance evidence we have obtained is sufficient and appropriate to provide a basis for our conclusion.

Responsibilities of the Executive Board and the Supervisory Board for the sustainability information
The Executive Board is responsible for the preparation of the sustainability information in accordance with the GRI guidelines (G4 Core option) and the applied supplemental reporting criteria as disclosed in the chapter 'About the CSR review' of the 2017 Annual Report, including the identification of stakeholders and the definition of material matters. The choices made by the Executive Board regarding the scope of the sustainability information and the reporting policy are summarised in the chapter 'About the CSR review' of the 2017 Annual Report.

The Executive Board is also responsible for such internal controls as it determines is necessary to enable the preparation of the sustainability information that is free from material misstatement, whether due to fraud or error.

The Supervisory Board is responsible for overseeing the company's reporting process.

Our responsibilities for the review of the sustainability information
Our responsibility is to plan and perform the assurance engagement in a manner that allows us to obtain sufficient and appropriate assurance evidence for our conclusion.

Procedures performed in an assurance engagement to obtain a limited level of assurance are aimed to determining the plausibility of information and are less extensive than a reasonable assurance engagement. The level of assurance obtained in assurance engagements with a limited level of assurance is therefore substantially less than the assurance obtained in audit engagements.

Misstatements can arise from fraud or errors and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the decisions of users taken on the basis of this Report. The materiality affects the nature, timing and extent of our review procedures and the evaluation of the effect of identified misstatements on our conclusion.

We apply the 'Nadere voorschriften accountantskantoren ter zake van assurance opdrachten (RA/AA)' (Regulations for professional accountants practices on assurance engagements) and accordingly maintain a comprehensive system of quality control including documented policies and procedures regarding compliance with ethical requirements, professional standards and applicable legal and regulatory requirements.

We have exercised professional judgement and have maintained professional scepticism throughout the review, in accordance with the Dutch Standard 3810N, ethical requirements and independence requirements.

Our review engagement included:
- Performing an external analysis and obtaining insight into relevant environmental and social themes and issues, and the characteristics of the organisation.
- Evaluating the appropriateness of the reporting policy and its consistent application, including the evaluation of the results of the stakeholders' dialog and the reasonableness of management's estimates.

- Evaluating the design and implementation of the reporting systems and processes related to the information in the Report.
- Reviewing internal and external documentation to determine whether the information as included in the KPIs, including the presentation and assertions made in the report, is adequately supported.
- Interviewing management and relevant staff at group level responsible for the sustainability strategy and policy.
- Interviewing relevant staff responsible for providing the information in the Report, carrying out internal control procedures on the data and consolidating the data in the Report.
- An analytical review of the data and trends submitted for consolidation at corporate level.
- Assessing whether the Report has been prepared in accordance with the Sustainability Reporting Guidelines (GRI G4 Core option) of the Global Reporting Initiative.

We communicate with the Supervisory Board regarding, among other matters, the planned scope, timing and outcome of the review.

Amsterdam, 20 February 2018

Deloitte Accountants B.V.

B. E. Savert

1 2013 excluding non-recurring costs and earn-out Kuhnke of EUR 2.4 million after tax, 2016 excluding one-off costs relating to simplifying measures of EUR 5.7 million (after tax EUR 4.7 million) and 2017 excluding one-off costs relating to simplifying measures of EUR 5.1 million (after tax EUR 3.8 million).

2 Relates to inventories, receivables minus non-interest bearing debts (2013 is excluding EC fine payable).

3 Total invested capital is property, plant and equipment, intangible assets, other investments and current assets less cash and non-interest bearing debts (2013 is including EC fine).

4 Before cash flow relating to acquisitions and disposals (2013 excluding acquisition expenses, 2014 excluding EC fine payment, 2016 and 2017 excluding one-off costs relating to simplifying measures).

5 2013 is including full year Kuhnke, 2016 and 2017 are excluding one-off costs relating to simplifying measures.

6 The net financing charges exclude foreign exchange differences, the commitment fees for unused facilities and the amortisation of upfront and legal fees.

7 2013 is including full year Kuhnke.

8 2016 and 2017 excluding accruals and provisions related to the simplifying measures.

EUR million, unless otherwise stated	2017	2016	2015	2014	2013
Kendrion N.V. consolidated					
Statement of normalised comprehensive income					
Revenue	461.8	443.4	442.1	428.9	354.0
Organic growth	4.2%	0.3%	3.1%	8.2%	(1.2)%
Operating result before amortisation (EBITA)[1]	37.0	31.1	25.8	32.9	23.9
Depreciation of property, plant, equipment and software	20.3	20.3	19.4	16.4	13.0
Operating result before depreciation and amortisation (EBITDA)[1]	57.3	51.4	45.2	49.3	36.9
Net profit for the period[1]	23.3	19.6	16.8	20.2	14.3
Statement of financial position at 31 December conform financial statements					
Total assets	344.8	347.1	340.9	333.5	334.8
Total equity	180.3	178.1	169.9	153.2	134.1
Net interest-bearing debt	54.5	54.0	69.1	83.0	49.0
Working capital[2, 8]	45.6	41.3	43.4	44.9	40.6
Invested capital[3, 8]	255.1	252.3	254.3	253.1	242.5
Statement of normalised cash flows					
Net cash from operating activities[4]	42.5	45.3	40.9	37.9	30.5
Net investments	28.3	22.9	19.8	20.0	18.5
Free cash flow[4]	14.2	22.3	21.2	17.1	11.7
Ratios					
Return on Sales (ROS)	8.0%	7.0%	5.8%	7.7%	6.8%
Solvency	52.3%	51.3%	49.8%	46.0%	40.1%
Net interest-bearing debt / EBITDA[5] (debt cover)	1.0	1.1	1.5	1.7	1.2
Net interest-bearing debt / equity (gearing)	0.3	0.3	0.4	0.5	0.4
EBITDA[1, 5] / net finance costs (interest cover)[6]	34.1	24.5	20.1	13.9	11.7
Return on Investment (ROI)[1, 3, 7, 8]	14.5%	12.4%	10.2%	13.0%	10.8%
Working capital[2] in % of revenue[7]	9.1%	8.6%	9.8%	10.5%	10.2%
Dividend payout ratio of net profit	50%	53%	61%	50%	50%
Market capitalisation as at 31 December	542.9	358.3	319.7	281.7	309.2
Net interest-bearing debt as at 31 December	54.5	54.0	69.1	83.0	49.0
Theoretic value of the organisation (Enterprise value)	597.4	412.3	388.8	364.7	358.1
Number of employees at 31 December (FTE)	2,645	2,578	2,658	2,713	2,756

At 31 December 2017

Industrial

Industrial Magnetic Systems (Norman Graf)

Kendrion (Donaueschingen/Engelswies) GmbH, Donaueschingen, Germany	Norman Graf
Kendrion (Donaueschingen/Engelswies) GmbH, Engelswies, Germany	Alfons Mattes
Kendrion (China) Co. Ltd, Suzhou, P.R. China	Telly Kuo
Kendrion (Mishawaka) LLC, Mishawaka, Indiana, USA	Corey Hurcomb
Kendrion Industrial (Sibiu) S.R.L., Sibiu, Romania	Mihai Petculescu
Kendrion (Linz) GmbH, Linz, Austria	Erich Holzinger
Kendrion (Italy) S.r.l., Torino, Italy	Vincenzo Leo

Industrial Control Systems (Robert Lewin)

Kendrion Kuhnke Automation GmbH, Malente, Germany	Robert Lewin
Kendrion Industrial (Sibiu) S.R.L., Sibiu, Romania	Mihai Petculescu
Kendrion Kuhnke (Sweden) AB, Kristianstad, Sweden	Ronnie Jennerheim

Industrial Drive Systems (Ralf Wieland)

Kendrion (Villingen) GmbH, Villingen-Schwenningen, Germany	Ralf Wieland
Kendrion (UK) Ltd., Bradford, United Kingdom	Peter McShane
Kendrion (China) Co. Ltd, Suzhou, P.R. China	Telly Kuo
Kendrion (Mishawaka) LLC, Mishawaka, Indiana, USA	Corey Hurcomb
Kendrion (Aerzen) GmbH, Aerzen, Germany	Gregor Langer
Kendrion (Italy) S.r.l., Torino, Italy	Vincenzo Leo

Automotive

Passenger Cars (Bernd Gundelsweiler)

Kendrion (Villingen) GmbH, Villingen-Schwenningen, Germany	Bernd Gundelsweiler
Kendrion Kuhnke Automotive GmbH, Malente, Germany	Bernd Gundelsweiler
Kendrion (Prostějov) s.r.o, Prostějov, Czech Republic	Tomas Soldan
Kendrion Mechatronics Center GmbH, Ilmenau, Germany	Jörg Rönnert
Kendrion (Eibiswald) GmbH, Eibiswald, Austria	Martin Kollmann
Kendrion Automotive (Sibiu) S.R.L, Sibiu, Romania	Andra Boboc
Kendrion (Shelby) Inc., Shelby, North Carolina, USA	Ludger Reckmann
Kendrion (China) Co. Ltd, Suzhou, P.R. China	Telly Kuo

Commercial Vehicles (Manfred Schlett)

Kendrion (Markdorf) GmbH, Markdorf, Germany	Manfred Schlett
Kendrion (Prostějov) s.r.o, Prostějov, Czech Republic	Tomas Soldan
Kendrion (China) Co. Ltd, Suzhou, P.R. China	Telly Kuo
Kendrion (Shelby) Inc., Shelby, North Carolina, USA	Ludger Reckmann
Kendrion Toluca, S.A. de C.V., Mexicaltzingo, Mexico	Alexander Bley

A complete list of all subsidiaries is available from the Chamber of Commerce in Utrecht (number 30113646) and from the Company offices.

Defined benefit plan A pension scheme where the employee is promised a pension the level of which depends on their age, salary and years of service. The commitment carried in the financial position is the cash value of the projected pension benefits on the financial position date, less the fair market value of fund investments.

Defined contribution plan Pension scheme where the employer pays agreed contributions to a fund or insurance company and no obligation arises for the employer to pay supplementary contributions in the event of a shortfall in the fund or insurance company.

Derivatives Derivative financial products which do not represent a direct cash value; they include options, forward exchange contracts and swap contracts.

ERP system Enterprise Resource Planning: an ICT system which supports all the business processes within an organisation, such as purchasing, production, sales, logistics and accounting, with data being exchanged between departments.

Fair value The current value. For assets or liabilities for which there is an active market, this is generally the market value.

FTE Full Time Equivalent: equal to the number of total scheduled person hours divided by the number of hours per week which constitute a full-time person (40 hours). FTE may consist of several part-time individuals whose combined work hours in a week equal the full-time person.

Hedging The covering of financial risks, usually relating to (undesirable) movements in market interest rates, exchange rates and raw material prices.

IFRS International Financial Reporting Standards, also referred to as IAS (International Accounting Standards). With effect from 2005, all listed companies in the European Union must comply with these accounting rules.

Interest rate swap Derivative financial product whereby an agreement is reached with a counterparty (bank) to exchange specific interest payments on a predetermined underlying amount during a predetermined period. A variable interest rate (e.g. three-month EURIBOR) is usually swapped for a fixed interest rate.

Mid-term Plan A plan for the medium term which is drawn up by the Group annually to facilitate the management and control of its organisation in the short to medium term.

Number of employees (FTEs) Number of employees stated in full-time equivalents.

Organic (sales) growth Growth in revenue after eliminating the effects of acquisitions and disposal of activities.

Solvency ratio The ratio of total equity to the financial position total.

Translation risk Translation risk: a change in the value of an asset or liability of a subsidiary as a result of movements in the (non-euro) exchange rate.

TSR Total shareholders return.

Pages 41-57 of this Annual Report 2017 (the 'CSR Review'), in conjunction with the corporate website of Kendrion, have been compiled in accordance with the guidelines of the Global Reporting Initiative GRI G4 'core level'. The GRI index can be found on pages 164-167 of this Annual Report.

The targets in the area of Energy & CO_2 reduction, Health & safety, Supply chain management as described in the Corporate Social Responsibility chapter on pages 41-57, have been subjected to a review by the external auditor Deloitte Accountants B.V. The auditor's report with limited assurance on the relevant targets and the statement in accordance with the guidelines of the Global Reporting Initiative GRI G4 'core level' is included on pages 155-157.

This seventh CSR Review covers all of Kendrion's operating companies in 2017 as listed on pages 159 and 160, unless explicitly stated otherwise.

For the quantitative information on targets associated with economic performance, energy, emissions, occupational health and safety, training and education, non-discrimination, anti-corruption and supplier assessment for impacts on society, Kendrion used the GRI G4 Specific Standard Disclosures G4-EC1, G4-EN3, G4-EN5, G4-EN6, G4-EN15, G4-EN16, G4-LA6, G4-LA9, G4-HR3 and G4-SO5 respectively as further described in the GRI Index on pages 164-167.
Kendrion is partially reporting – on a qualitative basis – about the topic "market presence". This topic was one of the topics identified in the materiality analysis 2017 as included on pages 50 and 51. Kendrion has not selected underlying GRI indicators for the topic "market presence". Following further engagement with Kendrion's stakeholders in the course of 2018, Kendrion will consider to what extent "market presence" continues to be relevant to stakeholders and influence Kendrion's business operations.

The information on energy (G4-EN3 and G4-EN5) is based on the consumption of Kendrion's production facilities (electricity, gas, oil) in Germany, the Czech Republic, Austria, the USA, Suzhou (China) and Romania. For greenhouse gas emissions (G4-EN15 and G4-EN16), Kendrion applies the same reporting scope as for energy. This covers the major production facilities representing approximately 93% of Kendrion's revenues. Internal and external transport under Kendrion's control is very limited, therefore transport emissions are not included.

The relative energy consumption and CO_2 emissions are based on the added value of the relevant production facilities. The added value is the revenue plus other income, minus the changes in inventory and work in progress and minus the raw materials.
The absolute and relative energy consumption and CO_2 emissions are reported during the period from 1 December up to and including 30 November of the relevant calendar year. This means that in this CSR Review the period is 1 December 2016 up to and including 30 November 2017, and for comparison reasons 1 December 2015 to 30 November 2016 is provided. The comparison with 2014 is based on the data for the calendar year 2014.

Calculation of the CO_2 emissions is based on the following conversion factors:

- Electricity generated from renewable sources 0.017 kg/kWh
- Electricity generated from non-renewable sources (average) 0.578 kg/kWh
- Fuel oil and natural gas (average) 0.200 kg/kWh

Kendrion reports the total number of work-related accidents during working time or on the way to or from work for its own employees and independent contractors under supervision of Kendrion. Only the accidents that the group entity had to report to an external institution are reported. As of 2017, Kendrion reports accidents from all group entities that caused an absence of more than three calendar days, not including the day of the accident. This definition is based on regulations applicable in Germany.

In addition, Kendrion reports the absence resulting from work-related accidents. The Lost Time Injury (LTI) is time ('scheduled working days') that could not be worked (and is thus 'lost') as a consequence of an employee being unable to perform the usual work due to an occupational accident ('at work accident' as well as 'way-to-work accident') or disease. There is no difference in whether the salaries or wages were paid by Kendrion or by an external institution during that time.

Operations in Brazil and India were discontinued and the facility in Nanjing (China) was closed. These locations are therefore not included in the 2017 scope for the targets concerning work-related accidents and LTI rates. The abovementioned locations were included in the 2015 and 2016 scope.

A return to limited duty or alternative work for the same organisation does not count as 'lost days'. Counting of 'lost days' begins with the first scheduled working day of full absence (e.g. the day after the accident). A lost day counts as one full day regardless of whether the employee has a part-time or a full-time contract. Kendrion does not specify LTI data per region, worker type or gender as Kendrion considers this information not relevant to its current operations. Kendrion evaluated the definition of the LTI rate to enable better benchmarking.

For reporting on the number of signed Supplier Code of Conduct documents and the number of supplier audits, Kendrion makes use of GRI indicator G4-SO9 in conjunction with the number of suppliers that signed the Supplier Code of Conduct and underwent a supplier audit. The supplier audits are internal audits by Kendrion employees based on standardised interview questionnaires. For more information about the Supplier Code of Conduct, Kendrion refers to its website (Supplier Code of Conduct). The 'percentage of top 30 suppliers that signed the Supplier Code of Conduct' in 2017 is based on the 30 biggest suppliers in terms of procurement value (in euros) in the respective calendar year.

During 2016, the internal management information system and internal controls for CSR reporting were further improved. They are designed to facilitate the collection and consolidation of relevant CSR information from all Kendrion's operating facilities. This is required for the preparation of reliable periodic internal and external reports about the KPIs. Kendrion realises that the figures and data presented in this CSR Review are not always fully comparable with those of other companies. There are two main reasons for this. Firstly, companies do not always select the same targets or apply different definitions. Secondly, due to the nature and spread of Kendrion's activities it is not easy to make one-on-one comparisons with other industrial companies. Other information used in this CSR Review was collected from the existing management and reporting systems. Any estimates or forecasts included are explicitly referred to as such.

GENERAL STANDARD DISCLOSURES

	Page number (or link) Information related to Standard Disclosures required by the 'in accordance' options may already be included in other reports prepared by the organization. In these circumstances, the organization may elect to add a specific reference to where the relevant information can be found.	External Assurance Indicate if the Standard Disclosure has been externally assured. If yes, include the page reference for the External Assurance Statement in the report.
Strategy and analysis		
G4-1	9, 52 and website: www.kendrion.com; Taking Responsibility section	
Organizational profile		
G4-3	6 and 7	
G4-4	Cover, 4-7, 28-33, see also www.kendrion.com for more information about the brands Kuhnke, Linnig and Binder	
G4-5	67, 83 and back cover	
G4-6	14, 47, 159 and 160	
G4-7	16-18	
G4-8	14, 28-33	
G4-9	14, 35-40, 54	
G4-10	54-57	
G4-11	57	
G4-12	46 and 47	
G4-13	10, 16, 28-33, no significant changes regarding suppliers	
G4-14	47, 48, 58-66	
G4-15	41 and 42	
G4-16	NIVE, NGB, VEUO, UN Global Compact, GRI	
Identified material aspects and boundaries		
G4-17	41, 159 and 160, 162 and 163 (About the CSR Review)	
G4-18	41-44, 162 and 163 (About the CSR Review)	
G4-19	44, 50 and 51	
G4-20	162 and 163 (About the CSR Review); the material aspects are material to all group entities	
G4-21	50 and 51	
G4-22	162 and 163 (About the CSR Review)	
G4-23	162 and 163 (About the CSR Review)	

GENERAL STANDARD DISCLOSURES

	Page number (or link) Information related to Standard Disclosures required by the ‘in accordance’ options may already be included in other reports prepared by the organization. In these circumstances, the organization may elect to add a specific reference to where the relevant information can be found.	External Assurance Indicate if the Standard Disclosure has been externally assured. If yes, include the page reference for the External Assurance Statement in the report.
Stakeholder engagement		
G4-24	42-44	
G4-25	42-44	
G4-26	42-44	
G4-27	42-44	
Report profile		
G4-28	Calendar year 2017, 162 and 163 (About the CSR Review) describes the reporting period for Energy and Emissions	
G4-29	22 February 2017	
G4-30	Annual (cover)	
G4-31	Back cover	
G4-32	155-157 (assurance report), 162 and 163 (About the CSR Review)	
G4-33	26, 41, 155-157 (assurance report), 162 and 163 (About the CSR Review)	
Governance		
G4-34	22-26, 67-72	
Ethics and integrity		
G4-56	49 and 50, 59-62	

SPECIFIC STANDARD DISCLOSURES					
DMA and indicators	**Page number (or link)** Information related to Standard Disclosures required by the 'in accordance' options may already be included in other reports prepared by the organization. In these circumstances, the organization may elect to add a specific reference to where the relevant information can be found.	**Identified omission(s)** In exceptional cases, if it is not possible to disclose certain required information, identify the information that has been omitted.	**Reason(s) for omission(s)** In exceptional cases, if it is not possible to disclose certain required information, provide the reason for omission.	**Explanation for omission(s)** In exceptional cases, if it is not possible to disclose certain required information, explain the reasons why the information has been omitted.	**External Assurance** Indicate if the Standard Disclosure has been externally assured. If yes, include the page reference for the External Assurance Statement in the report.
CATEGORY: ECONOMIC					
Material aspect: economic performance					
G4-DMA	12 and 13, website: www.kendrion.com				
G4-EC1	14, 35-40, 50, 72	Payments to government by country	The information is not available	Payments to government by country will be reported if required	
CATEGORY: ENVIRONMENTAL					
Material aspect: energy					
G4-DMA	website: www.kendrion.com; section Taking Responsibility				
G4-EN3	48	Data regarding renewable resources and sold energy	The information is not available	The underlying data are currently unavailable. It will be considered if and when to report these in the future	yes, 155-157
G4-EN5	48, 162 and 163 (About the CSR Review), energy used inside organisation				yes, 155-157
G4-EN6	48, 162 and 163 (About the CSR Review)	The amount of energy reduction as a direct result of individual efficiency initiatives is not available	The information is not available	The underlying data are currently not available	yes, 155-157
Material aspect: emissions					
G4-DMA	website: www.kendrion.com; section Taking Responsibility				
G4-EN15	48, 162 and 163 (About the CSR Review)	Global Warming Potential data	The information is not available	The underlying data are currently not available	yes, 155-157
G4-EN16	48, 162 and 163 (About the CSR Review)	Global Warming Potential data	The information is not available	The underlying data are currently not available	yes, 155-157

SPECIFIC STANDARD DISCLOSURES					
DMA and indicators	**Page number (or link)** Information related to Standard Disclosures required by the 'in accordance' options may already be included in other reports prepared by the organization. In these circumstances, the organization may elect to add a specific reference to where the relevant information can be found.	**Identified omission(s)** In exceptional cases, if it is not possible to disclose certain required information, identify the information that has been omitted.	**Reason(s) for omission(s)** In exceptional cases, if it is not possible to disclose certain required information, provide the reason for omission.	**Explanation for omission(s)** In exceptional cases, if it is not possible to disclose certain required information, explain the reasons why the information has been omitted.	**External Assurance** Indicate if the Standard Disclosure has been externally assured. If yes, include the page reference for the External Assurance Statement in the report.
CATEGORY: SOCIAL					
SUB-CATEGORY: LABOR PRACTICES AND DECENT WORK					
Material aspect: occupational health and safety					
G4-DMA	48 and 49, website www.kendrion.com; section Taking Responsibility				
G4-LA6	48 and 49	Info per regio and gender	The information is not available	Distinction based on gender is in the view of Kendrion not appropriate	yes, 155-157
Material aspect: training and education					
G4-DMA	54				
G4-LA9	54	Info per gender and per employee category.	The information is not available	Distinction based on gender is in the view of Kendrion not appropriate	
SUB-CATEGORY: HUMAN RIGHTS					
Material aspect: non-discrimination					
G4-DMA	22 and 23, 56, 70				
G4-HR3	70; no reports				
SUB-CATEGORY: SOCIETY					
Material aspect: anti-corruption					
G4-DMA	49 and 50				
G4-SO5	25, 60				
Material aspect: supplier assessment for impacts on society					
own indicator: Number of CSR supplier audits	46 and 47, 162 and 163 (About the CSR Review)				yes, 155-157
own indicator: number of signed Supplier Code of Conduct	46 and 47, 162 and 163 (About the CSR Review)				yes, 155-157

Contact information

Any questions or comments about this Annual Report or Kendrion's activities can be raised with:

Mrs Wilma Stuiver
Utrechtseweg 33
3704 HA Zeist, the Netherlands
P.O. Box 931
3700 AX Zeist, the Netherlands
Telephone: + 31 (0) 30 699 72 50
Fax: +31 (0) 30 695 11 65
Email: ir@kendrion.com
www.kendrion.com

Kendrion N.V.
Euronext code 0000383511
ISIN code 0000383511
Chamber of Commerce 30113646