SIEMENS

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Another strong quarter – profitable growth continuing

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Check against delivery.

[Ralf P. Thomas]

The geopolitical environment of the past few months continued to be characterized by uncertainties. So it's all the more striking that Siemens maintained the momentum of the beginning of the fiscal year and again delivered a strong quarter.

In particular, the short-cycle business surged in the second quarter. I'd like to explain the key data:

- Orders – on a comparable basis and excluding currency translation and portfolio effects – grew one percent to €22.6 billion. In view of the high order volume in the prior-year quarter resulting from the megaproject in Egypt, this is a truly strong performance. With Egypt orders excluded, order growth would total 17 percent.
- Revenue grew five percent to €20.2 billion, supported by growth in all industrial businesses.
- The book-to-bill ratio – the ratio between orders and revenue – was therefore a gratifying 1.12. The Industrial Business order backlog hit an all-time high of €117 billion – and this without changing the high margin quality.
- Eight out of nine Divisions are within or above their respective margin ranges.
- The Industrial Business profit margin expanded by 120 basis points to 12.1 percent, primarily due to operational improvements in our Divisions. There were also positive effects related to amendments to foreign pension plans.
- At €1.5 billion, our net income was at the prior-year level despite higher tax rates. Basic earnings per share were €1.79.
- Free cash flow from our Industrial Business was €2 billion, up 32 percent. In the first half of the year, free cash flow across the company increased by €1.4 billion year-over-year.

Let's take a look now at the individual Divisions.

The Power and Gas Division executed its orders reliably and rigorously in an intensively competitive market environment marked by enormous price pressure. The Division's revenue rose moderately. The level of orders, in contrast, was lower compared to the prior-year quarter due to the previously mentioned Egypt orders. Power and Gas achieved a profit of nearly half a billion euros.

The year-over-year decline was primarily due to a one-time effect: in the second quarter of 2016, the lifting of the Iran sanctions had a positive effect on the Division's profit, as reported at the time.

Power and Gas won major orders for four turnkey gas-fired power plants in Argentina with a total volume of around USD570 million. With an additional capacity of nearly 700 megawatts (MW), the plants will significantly improve the power supply for the country and its industry.

We also succeeded in booking a very satisfying major order in Germany. Siemens will build a new cogeneration plant in Berlin-Marzahn for customer Vattenfall Europe Wärme AG. The electrical output of the plant will be 260 MW, and the thermal output will be around 230 MW.

The plant will thus contribute to sustainably reducing CO_2 emissions in Berlin. The order for Siemens also includes a long-term service contract. Incidentally, the gas turbine for the plant will also be built in Germany's capital, at our factory in Berlin-Moabit.

Due to the postponement of projects, primarily in the Middle East, we expect to see an overall decline in the market for large gas turbines in the current fiscal year as a whole.

Wind Power and Renewables will be reported this quarter for the last time as a Division. As of the third quarter, we will instead report the financial data for Siemens Gamesa Renewable Energy, which – as you know – will be fully consolidated in Siemens' financial statements.

Our wind business delivered a convincing performance in the second quarter – that is, prior to the merger with Gamesa – with an exceptionally strong margin of 10.3 percent, revenue growth of four percent and a sharply higher order volume.

Wind Power won a number of major orders – including an order for the EnBW "Hohe See" wind farm worth €1.4 billion, including services. Siemens Wind Power currently has orders worth nearly €17 billion on its books. This fact once again underscores the excellent job our Wind Power team is doing.

Siemens holds a 59 percent stake in Siemens Gamesa Renewable Energy.

In view of its well balanced geographical footprint and a large installed base of 75 gigawatts, the new company has the ideal prerequisites for outstanding success. We're convinced that this combination will yield *the* No. 1 provider of renewable energies worldwide.

The Energy Management Division was able to accelerate its growth. New orders grew by 17 percent, revenue climbed 9 percent, and profit was up by nearly one-third. Energy Management is within its margin range.

We achieved notable successes in the past quarter with two major orders booked in the Middle East. These two orders alone have a total volume of around €1 billion.

The Building Technologies Division delivered another excellent quarterly performance. Both orders and revenue were up ten percent year-over-year.

With a profit margin of 14.7 percent, Building Technologies turned in an impressive performance that was positively influenced by amendments to foreign pension plans. Yet even without this one-time effect, the Division would again be within its margin range at 8.8 percent and well above its prior-year level.

Let me turn now to Digital Factory, which again performed exceptionally well in the past quarter. Development of its short-cycle businesses was outstanding thanks to strong demand from the automotive and machine-building industries. In the short-cycle businesses, we were able to achieve double-digit revenue growth in important markets: a plus of 29 percent in China, ten percent in the U.S. and 11 percent in Germany.

Digital Factory was once again one of our top performers and contributed €482 million to our gross profit, one-third more than in the prior-year quarter. It accomplished this even though we continued to drive the further development and rollout of our MindSphere platform with targeted investments – exactly as we had previously announced.

In addition, there were transaction costs related to the acquisition of Mentor Graphics.

I'd like to emphasize that we're already up to full speed with the integration of Mentor Graphics. We can draw on our extensive experience from earlier acquisitions here – such as with CD-adapco, where we continue to make even better progress than originally planned, win new customers and leverage synergies in sales arising from the existing customer base of our PLM software business.

Our customers want to join us on our journey to the industry of the future. We've just announced a collaboration with adidas of which we're especially proud.

As part of our joint research and development activities, we'd like to further drive the digitalization of production in the so-called adidas Speedfactory. How are we doing this? With the help of a digital twin – a virtual image of the Speedfactory – we will simulate, test and optimize the entire production process.

This means that production at adidas will be more flexible, more efficient and more resource-conserving. And it means that the company's end customers will be able to individualize sport shoes according to their own measurements, tastes and preferences in the future.

At Process Industries and Drives, we're seeing the first signs of stabilization. Orders and revenue remained roughly at the prior-year level.

Growth in our short-cycle process automation business was again offset by declines in our businesses with customers in the commodity-related markets. Jürgen Brandes, Thomas Schaffer and their team are making continual progress and further implementing the initiated restructuring program as planned.

Our Mobility business also continued its positive development in the second quarter. Driven primarily by orders for rolling stock and rail infrastructure, the Division increased orders by 19 percent compared to the prior-year quarter.

As the Division's equally satisfying seven percent increase in revenue shows, we've succeeded in executing our often ambitious projects professionally and, above all, to the satisfaction of our customers.

In profitability, Mobility proved once again that it's operating very successfully in its competitive arena. Included in the profit margin of 10.5 percent are €28 million from the previously mentioned amendments to pension plans. But even without this one-time effect, profitability increased from eight to about nine percent year-over-year. That's a great success for our global Mobility team.

At Healthineers, we saw very solid figures in the second quarter, following an outstanding first-quarter performance. Orders rose in all Healthineers businesses, with the strongest contribution coming from the diagnostic imaging and advanced therapies businesses. Revenue was also up slightly. The Division's profit climbed six percent to €588 million.

Our centrally managed portfolio activities made a small positive contribution to profit, primarily due to a gain of €314 million from an adjustment to the expected inflation rate related to the asset-retirement obligation in Hanau that we've already informed you about.

A negative effect resulted from an impairment of €230 million relating to Siemens' equity in Primetals Technologies Ltd. due to ongoing unfavorable conditions in its market environment. Since this impairment is not tax deductible, our tax rate in the second quarter was also higher.

I'd now like to turn the floor over to my Managing Board colleague, Roland Busch, who'll tell you about our latest acquisition, the highlights of the Hannover Messe and Siemens as a leading digital company.

[Roland Busch]

Last Friday, we announced our intention to acquire HaCon, which is headquartered in Hanover, Germany. The company has nearly 300 employees and is a leading international supplier of planning, disposition and information systems for public transportation, mobility and logistics.

With this acquisition, we're expanding our offerings with industry-specific software in transportation and rigorously implementing our digitalization strategy. The deal, which is still subject to antitrust approval, is expected to close in the first half of calendar year 2017.

We'll manage the company as a legally separate, wholly owned subsidiary within our Mobility Division. The decision to acquire HaCon will enable us to tap a new market. We're growing our portfolio through the addition of timetabling and trip planning for travelers, including apps for mobile devices.

More than 100 transport companies in 25 countries already use trip planning software from HaCon as the centerpiece of their travel information systems and applications.

For example, Deutsche Bahn uses this software for its DB Navigator app, which is certainly familiar to many of us. More than 30 million downloads make the Navigator the most widespread mobility app in Germany.

The HaCon acquisition will also enable us to expand our intermodal, digital mobility offerings: we'll now be able to provide suppliers of transportation services with software solutions for train and train-path planning, timetable information systems, advanced fare payment systems and intermodal mobility platforms – all from a single source.

Ralf Thomas has already mentioned the successful closing of our acquisition of Mentor Graphics.

Measured in terms of revenue and according to the market analysts at the consultant firms PWC and Gartner, Siemens is one of the ten largest software companies worldwide.

To strengthen our digital portfolio, we've invested around €10 billion in the acquisition of software firms since 2007.

Our business with software and digital services, which has been developing very positively for years, is growing sustainably. In the past year, revenue grew by 12 percent to €4.3 billion. Digitalization is a key growth driver for Siemens. And we're solidly positioned in this field:

We combine years of expertise in our markets with digital offerings. In mobility, for instance. Trains from Siemens are operating throughout the world and our customers expect maximum fleet availability.

By employing predictive maintenance and data analytics, our Railigent service platform enables train availability of over 99 percent – as we've proven in rail projects in Spain, Russia and the United Kingdom, for example.

We're the world leader in the field of automation. Around 30 million automation systems from Siemens are now helping customers worldwide increase their productivity and manufacturing efficiency. The connectivity of these systems will continue to grow as will the possibilities it offers. We'll be partnering with our customers in this development.

"Network" and "partnerships" are two key words we feel are essential for digitalization.

They are also essential for MindSphere, our open, cloud-based operating system for the Internet of Things. It's the backbone of our digital offerings.

MindSphere is an open network for partners who make their own various contributions. In the area of infrastructure, we're cooperating, for instance, with Amazon Web Services, among others. The programming of industrial applications is being done, for example, by Evosoft, a Siemens subsidiary that offers software and IT solutions, while Accenture is providing systems integration.

We've been working closely with Atos for more than five years. When it comes to a holistic approach to digital solutions, our two companies complement one another in a variety of ways.

We're profiting from this collaboration across all our business units. And our success is also reflected in our figures: from 2011 to 2016, Atos and Siemens jointly generated revenue of roughly €1.9 billion.

And we want to continue our joint growth. Atos is an important partner for MindSphere. For example, it programs industrial applications and sector-specific solutions, implements them and provides additional services for the MindSphere infrastructure.

Together, Atos and Siemens have now made some €230 million available for joint research and development activities.

IT security and digital services – the focuses of this research partnership – will continue to develop into attractive markets. And both our companies can profit even more from these trends if we bundle our strengths.

Another example is our cooperation with SAP. In the future, we'll work together to support power utilities in processing their meter data in real-time so they can gain a better understanding of processes in the grid.

Only recently, we signed a global reseller agreement that will enable SAP to market our EnergyIP meter data management system together with SAP's enterprise software.

We're bundling our positions on the market: our EnergyIP software will soon enable us to monitor more than 70 million electricity meters worldwide. For power utilities, SAP is often the standard for enterprise software. As partners, we'll reach nearly half of all power utilities.

Our goal is to ensure reliable and efficient power supplies – a major challenge in times of a changing energy landscape and an ever-increasing number of decentralized energy systems.

This brings me to the Hannover Messe. Last week, at the world's biggest industrial trade fair, we impressively proved once again that there's no way around Siemens when it comes to *Industrie 4.0*.

We were particularly pleased to welcome German Chancellor Angela Merkel and Polish Prime Minister Beata Szydlo to our stand.

It was a record-setting event. We welcomed more than 100,000 visitors to our

3,500-square-meter stand. Nearly every tenth visitor was a prospective customer who will now be contacted by our sales team. Compared to last year, we increased the number of these leads by 50 percent.

We showed how we see the future of industry – one in which digital twins, networking, artificial intelligence, autonomous machines and 3D printing will play an important role.

Siemens stands for *Industrie 4.0*. In fact, there's no other company worldwide that is driving the merger of the virtual and real worlds of manufacturing so comprehensively.

And digitalization is not only moving Siemens. It's also moving Dubai and thus one of the largest logistics hubs in the world.

The Emirate, which has been thriving economically for years, is well known for its receptiveness to new trends and changes.

This also applies to the World Exhibition that will be held in Dubai in 2020. Siemens will accompany Expo 2020 as a technology partner. MindSphere will guarantee the operation of the Expo's critical infrastructures – in particular the energy management systems and building technology on the Expo grounds.

In addition, Siemens is supplementing its energy concept with an innovative energy storage system. Our solution will store electricity in the form of hydrogen. Energy storage plays a key role in energy systems since both generation and feed-ins are becoming increasingly decentralized. The share of renewable energies is growing massively – and in the Emirates as well.

We've decided to expand our logistics business in Dubai and later use the Expo grounds as our business location.

With this decision, we will build up key parts of the value chain for our business with airports, cargo infrastructures and ports in the Emirates in the near future. We'll also expand our team of on-site experts to handle airport digitalization. The Emirates have created very favorable conditions for this: their universities have earned a very good reputation for IT-centered studies. This is one of the reasons why talented people from throughout the world are finding their way to Dubai.

There were three reasons why we selected Dubai:

First, Dubai has established itself as a global hub in the transportation and logistics sectors. Some of the biggest airlines and ports operate from Dubai or in its immediate vicinity.

Second, public- and private-sector customers from the Emirate have been doing business with Siemens for many years. We enjoy very good, trust-based relationships there.

And third, we've been impressed by Dubai's infrastructure. The Expo grounds will be state-of-the-art, in part because their transportation links and buildings will be unmatched worldwide.

As you can see, Siemens is *the* industrial company driving digitalization. And across all its businesses and activities. We think and act in partnerships and are banking on innovations. And we're absolutely certain: this development will benefit our customers above all since they can use our solutions to increase their own productivity and efficiency.

[Ralf P. Thomas]

Siemens is making outstanding progress in every respect in executing its Vision 2020 strategy program.

Let me give you a few concrete examples. Our successful company-wide program for reducing costs – 1by16 – has helped us simplify our organization and improve our processes.

We completed the 1by16 program faster than originally planned, and it's brought us significant productivity gains. But we're not content with these accomplishments.

As you know, we're striving to achieve productivity gains of three percent to five percent a year. This is a must in order to remain a nose ahead of competitors over the long term. Following our productivity gain of over five percent in fiscal 2016, we're right on track at the half-year mark to improve again this year by at least four percent.

We're now taking a close look at all our businesses and functions in order to find out where we can achieve efficiency gains, also through the digitalization of our internal business processes.

By 2020, for example, we aim to digitally execute roughly 80 percent of all transactions related to invoice processing.

In supply chain management, too, we're setting a good example and have firmly established cost and value engineering methods. This means we make sure right at the outset of a product's development that we get our suppliers involved at an early stage and optimize materials costs.

We also have a firm grasp on another lever we can use to improve our profitability: improvements in businesses that, to date, have been underperforming their competitors. Here, too, we're progressing as planned.

We are especially proud of the sustained improvements we've achieved in project execution: we've again delivered a quarter – the sixth in a row – without net burdens from project execution.

We've drawn the right conclusions from the mistakes we made here in the past. Now, at a very early stage in major project acquisition, we systematically analyze risks, determine how to eliminate or mitigate them, and then rigorously implement the appropriate measures.

Especially important here is our employees' wealth of experience. We have now identified around 100 experienced project managers and experts in all parts of the company who can be deployed in particularly challenging projects. Within the company, we refer to this group as the "Silverback Community" – not because of their age, but because of their bundled experience.

What's now in store for our company?

There are plenty of rumors: I can only say "no comment" with regard to the most recent media speculations about a merger between Siemens' rail business and that of one of our competitors. You're all familiar with the global competitive situation since the merger of the worldwide No. 1 and No. 2 in the rail market to form the gigantic China Railway Rolling Stock Corporation Limited (CRRC).

Further consolidation of the market has been expected for a long time now, and antitrust evaluations of such deals should take a global view of changes in the industry.

As our most recent announcement of the acquisition of HaCon and the continuous improvement of our competitiveness in our Mobility business show, we intend to actively shape the markets' challenges from a strong position.

There have also been occasional rumors about the future of Siemens as a whole. There's been talk of a *"holding company"* or a "*mere investment company"* – and some have even commented completely unrealistically about a *"breakup."*

None of this is the case. It's clear that we're focusing our businesses and taking a very close look at how we can best drive the development of each one. This means: we'll continue to optimize our businesses' value chains and get even closer to our customers under the strong and world-renowned brand of Siemens.

Those businesses that are closely intertwined through their market access and technologies will also remain closely tied to one another in the future. Others – like Healthineers – we're aligning even more effectively with customer requirements by giving them greater flexibility.

With a flexible approach to further developing our businesses, we're creating a new form of corporate leadership that does an even better job of serving Siemens as a whole and our customers around the world.

We continue to determine what is to belong to Siemens by posing five strategic questions:

- Is it an area of sustainable growth?
- Is the profitability in order?
- Are we really the best owner?
- Is the synergy potential big enough and for the long term?
- Are there signs of larger changes in the technology or business models on the horizon?

The answers to these questions provide the strategic imperative on which we base our business decisions.

In the second quarter, we delivered another strong team performance, and we continue to outperform the markets and our competitors. In the second half of the fiscal year, the careful integration of Mentor Graphics and ensuring a successful start for Siemens Gamesa Renewable Energy will be major priorities. At the same time, we'll keep a close eye on our operational performance. And there is still more work to do.

Now to our outlook, which reflects the highly successful development of the first half-year. As we noted in the outlook, potential burdens related to pending portfolio matters are excluded, since these are difficult to predict.

Now there is greater clarity here, since we closed the acquisition of Mentor Graphics and the Gamesa merger by the middle of the year. From today's perspective, the two transactions will have a negative effect of around 40 to 60 euro cents on the basic earnings per share from net income this fiscal year, and we expect the Industrial Business margin to be burdened in the range of 30 to 50 basis points. Integration and amortization costs (PPA), in particular, will have an impact here.

Despite these effects, however, we confirm our previous expectations for fiscal 2017. In particular:

We continue to expect modest growth in revenue, net of effects from currency translation and portfolio transactions, and anticipate that orders will exceed revenue for a book-to-bill ratio above 1.
We expect the profit margin of our Industrial Business in the range of 11.0 percent to 12.0 percent, and basic EPS from net income in the range of €7.20 to €7.70.