



**REPORT**  
**MR. BERNARDO VELÁZQUEZ**

**CHIEF EXECUTIVE OFFICER**

**GENERAL SHAREHOLDERS' MEETING**

**Madrid, 10 May 2018**

# GENERAL SHAREHOLDERS' MEETING

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Dear Shareholders,

Once again I have the honour of addressing you to report on Acerinox's results in the 2017 financial year and to endeavour to explain the context within which we conducted our work in the stainless steel sector and within the global economy.

One year ago we remarked that, despite the numerous uncertainties in the political and geostrategic fields, we could perceive the overall improvement in the economy, and that we were going through a period of growth rather than simply beginning a phase of recovery, a view which has ultimately been confirmed. As has always been acknowledged, our sector lies one step ahead of the cycle.

In 2017, we witnessed how the process of economic recovery became firmly established, being boosted chiefly by the consumer goods sectors, given that, for one reason or another, there is still little investment in infrastructure or capital goods, which are highly dependent on the uncertainties emanating from the political situations in many countries.

Practically all the regions experienced growth. The Spanish GDP rose by 3.1% in 2017, while there were respective upturns in the European Union (2.5%), the United States (2.3%), the ASEAN area (5.3%) and China (6.9%), thus putting an end to the doubts concerning the ability of this huge country to manage its economy. The emerging countries also experienced growth, as demonstrated by the figures of 1.3% in South Africa and 1.0% in Brazil. It has been a long time since we witnessed homogeneous growth in all the important economic areas, and the moderation of the rates leads us to predict that this positive cycle will last longer, something companies and countries require for planning long-term strategies.

Important sectors in the use of stainless steel recorded positive performances. Just one example was the manufacture of household appliances, which grew by 3.7% in the European Union, 5.8% in the United States and 10.9% in China. In addition, car manufacturing continues at a healthy pace. Construction is growing again, even in southern Europe, boosted by the residential sector, and the food production and processing industry is going through a very good period.

Practically all the sectors related to consumer goods are growing, and we can only hope that the stability and confidence will attract investments in infrastructures and large projects, such as those beginning to emerge in the chemical industry, encouraged by greater visibility.

While the apparent consumption of flat products in the United States prior to the crisis was exceeded as early as 2014 and now stands 6.5% above, we continue to pursue this goal in Europe, and we were just 1.4% away from exceeding it in 2017. Unfortunately, a large part of the industrial fabric was destroyed in Spain and the lack of investment and budgets still keeps our apparent consumption 15% below the maximum level recorded in 2006.

Global stainless steel consumption has continued to rise, and we can see that it has done so in recent years with even more impetus than in the past. Since we were founded we have prided ourselves on manufacturing a good product, one which has maintained an annual growth rate of 5.9% since 1950 (the highest among metals and industrial alloys), but this rhythm of growth was surpassed in the 2008-2017 period, rising to 7.1%.

Similarly, in the 1999-2017 period the annual stainless steel growth rate stood at 2.4 times that of the global Gross Domestic Product, while in the 2008-2017 period this ratio increased to 2.8, proving that it is still a material undergoing expansion, its use of which substitutes that of other materials.

Stainless steel continues to be incorporated into new applications in the advanced economies, particularly those related to technology and sustainability, thanks to its exceptional mechanical properties and resistance to corrosion and, above all, the length of its life cycle, its low maintenance and its ability to be eternally recycled. These characteristics make it even more convenient when it comes to analysing its long-term cost, and it forms part of the circular economy, vital for preserving our planet's resources. Acerinox, like the rest of the companies in the Spanish steel industry, has been one of the first to join the Pact for the Circular Economy promoted by the Ministry of Agriculture and Fisheries, Food and Environment.

In addition, stainless steel continues to gain ground in terms of everyday usage in the emerging countries, keeping pace with a growing middle class which needs to consume food processed in a hygienic and healthy manner, enjoying the convenience provided by household appliances and, therefore, requiring more efficient vehicles to transport them and an increasingly developed industry.

This is good news for the sector, given that, thanks to the above growth, it will soon absorb the surplus capacity around the world caused by the huge proliferation of factories in China, a country which manufactured just 3% of the world's stainless steel in 2001 but produced as much as 54% in 2017.

Those of you who faithfully await this date will remember that, year after year, we have drawn your attention to the threat of overcapacity and unfair competition, which has now been popularised by the so-called "steel war" resulting from the imposition of tariffs or duties in the United States to protect domestic manufacturing of steel and aluminium.

Although it is true that the decision by the United States to impose tariffs on all imports of steel products is a cause for concern and may have unforeseen consequences, it is also true that the problem of excess production capacity has finally become a priority issue during trade negotiations between states and will be

decisively addressed within the major global economic forums such as the G-20 and the World Trade Organization.

China was conscious of the strategic nature of steel when it decided to promote its production, and it now manufactures more than half the world's steel and a large number of steel products with this material. Now, other regions are becoming aware that they cannot dispense with local industry and have to promote it and the latter must not succumb to the competition generated as a result of changing the rules of the game.

The United States is not the first country to have protected its steel industry, as we are also faced with protectionist measures in many other countries like Brazil, India, Indonesia and China. Europe was even the first to settle an anti-dumping case against China and Taiwan.

We trust that the greater awareness of the problem will lead to a rapid solution. The restriction of licences to build new plants in China, together with the higher demands in combating pollution and the evolution of its economy towards transparency and the elimination of public subsidies will lead to a restoration of the balance in the world stainless steel trade (and that of steel in general), thus rendering unnecessary the trade wars and barriers emerging all over the world.

We are supporters of free trade, as could not be otherwise in view of our global nature, but to maintain a balance it is necessary to impose a level playing field in terms of a free market, subsidies, care for the environment, people development and sustainability in general.

Although we are highly active and are closely monitoring everything related to the tariff barriers, it is still too early to draw conclusions. For the time being, the United States has imposed a 25% tariff on steel imports and only the negotiations regarding exclusions of some products and countries, including the European Union, Mexico, Canada, Argentina and Australia, remains pending. Negotiations with Japan did not come to fruition, while Brazil and South Korea have agreed to reduce their exports to 70% of the average over the previous three years. For other countries, the deadline for these talks has been extended until 1 June.

These measures have already been reflected in the American market where imports have fallen by 11% in the first two months of the year. Therefore, prices have improved, standing above the European ones.

It remains to be seen what measures other countries will take in view of this situation. Safeguarding measures are being studied in Europe; if successful, they could restrict imports to 100% of the average over the previous three years, being applied by country. The adoption of preliminary measures is expected in June, although we will have to wait until early 2019 to learn more about the definitive measures. This delay is accelerating imports of materials, which rose by 19% in the first quarter, partly driving sales which before headed to the United States, and this is causing a deterioration in prices.

Anti-dumping procedures against China could also be being considered in Taiwan and South Korea, while China could be doing the same against Indonesia. It remains to be seen what repercussions there will be in direct commercial relations between China and the United States.

In any case, with factories on four continents and its far-reaching business network, Acerinox is undoubtedly the group best-positioned in the stainless steel industry to address this new “globalisation with barriers”. Our worldwide network of factories, service centres, warehouses and commercial offices will be joined by a new office in Egypt this year, as a result of which we will increase the number of countries where Acerinox subsidiaries operate to 33.

We have a unique sales network operating on the five continents and more than 900 widely-experienced and well-coordinated people, enabling us to distribute our products in 85 countries and providing us with first-hand and reliable information allowing us to react quickly to market fluctuations.

Focusing on our business in 2017, the good performance of consumption and the excess capacity within the sector were the key factors affecting business throughout the year, bringing about a scenario of an increase in sales at lower prices, which meant that it was essential to implement cost controls to achieve better margins. The third significant factor was the volatility of prices of raw materials, chiefly nickel and chrome, which, as you well know, directly influence setting the price of stainless steel, which is transparent for our clients.

The price of nickel underwent a positive evolution in 2016, ending the year at 10,095 USD/tonne which contributed to improving the market in early 2017. It subsequently maintained a downward trend during the first half of the year, due partly to doubts concerning the satisfactory performance of the Chinese economy and partly to the relaxation of the measures imposed by the Indonesian government to prevent exports of minerals in order to encourage manufacturing within the country. These circumstances led to this metal being priced on the London Metal Exchange at the annual low of 8,700 USD/tonne recorded in June.

In contrast, in the second half of the year the improved economic mood, together with the expectations for use of this metal in electric car batteries, reversed the trend, meaning that it was priced at 12,200 USD/tonne at the end of the year, having reached the annual high of 12,800 USD/tonne in November. In other words, the price variation was almost 50% in 2017.

The effect of nickel on the stainless steel industry has now been combined with the forceful impact of ferrochrome. China is once again the main player, as it has become the largest ferrochrome manufacturer in the world, not because of its domestic chrome reserves, as it does not have any, but due to the ore it imports from other countries, chiefly from South Africa, which is the country with the largest reserves in the world.

China now produces 41% of the world’s ferrochrome, as a result of the 14 million tonnes of ore it exports, of which 72% comes from South Africa. It also needs to import ferrochrome, 56% of which also comes from the above country. In other

words, trade in both ore and ferroalloy between these two countries has become the key to the market and their price negotiations set the international costs.

It just so happened that Chinese stocks of chrome ore and ferrochrome stood at very low levels in late 2016, while demand for stainless steel began to grow for orders in the initial months of 2017. Stocks of stainless steel were not at a sufficient level to meet the purchasing needs, which led to a huge rise in production, sharply increasing both ferrochrome and stainless steel prices. Specifically, the price of ferrochrome increased by 50% to 165 USD/lb, the highest figure since 2008. The Acerinox Group was able to capitalise on these opportunities, in both purchasing raw materials and selling the finished product, which led to excellent results in the first quarter of the year.

In a rapidly-changing market, flexibility is one of the main challenges for production companies and at Acerinox we are progressing at great pace, given that our industry, steelmaking, has always preferred to work with high inventories and sufficient visibility to manufacture long series with constantly functioning equipment.

Our melting production in the first quarter was the highest of the year, standing at 668,000 tonnes, as was the turnover of €1,252 million, the EBITDA of €191 million and the profits after tax and minority interests totalling €98 million.

Once the stocks in the markets were replaced at the end of the first quarter, the situation began to settle down. Prices fell and our sales slowed, as well as our results. Melting production stood at 605,000 tonnes in the second quarter, in anticipation of a further worsening of market conditions which eventually arrived. The EBITDA in the second quarter was €126 million and profits after tax and minority interests totalled €53 million, with sales amounting to €1,191 million.

Once again, doubts concerning the sustainability of the Chinese economy had a marked effect, in view of the sharp 6.8% growth in the first half of 2017 and its potential effects on the world economy. In our market, these uncertainties were reflected in a certain rush to reduce stocks throughout the supply chain, leading to further falls in the prices of raw materials - nickel, and especially, ferrochrome - the latter of which lost all the gains recorded in the first part of the year, falling back to 110 USD/lb.

Stainless steel prices also suffered as a result and our sales fell to €1,067 million in the third quarter, the year's lowest figure. Our melting production, totalling 615,000 tonnes, was not so badly affected, as we had previously made cutbacks, but the reduced prices brought our EBITDA down to €53 million and our profits to barely €7 million, the quarterly lows for the year.

Despite market nervousness, the satisfactory situation of real consumption brought normality back to raw material and stainless steel prices again in the fourth quarter, a circumstance we capitalised on by increasing production to 631,000 tonnes. The turnover for the fourth quarter was €1,116 million, the EBITDA stood at €119 million and profits after tax and minority interests totalled €77 million.

It is noticeable how we suffered from the surpluses of the first quarter in the third, finally achieving an average EBITDA of €122 million per quarter, a value which lies very close to the real ones in the second and fourth quarters and our target for the year. Logically, this tremendous volatility makes daily management difficult, and our full attention is required for raw material purchasing processes, for production and maintenance scheduling of the factories and for the management of our stocks and sales.

For this reason, we are proud to have achieved sales totalling €4,627 million in 2017, 17% more than in 2016, a 49% increase in the EBITDA to €489 million and profits after tax and minority interests amounting to €234 million, which represents an almost threefold increase year on year. These results are the best we have achieved in the last decade, marked by the economic and financial crisis which began in 2008.

Melting production was the second largest in our history, totalling 2,518,919 tonnes, a mere 67,000 tonnes below our historical record, an objective which tempted us, but one we discarded out of prudence, deciding to reduce inventories and take the opportunity to carry out the large maintenance stoppages at the three steelworks. In terms of hot rolling we also achieved the second highest production, 2,230,678 tonnes. In cold rolling we reached a new high of 1,738,240 tonnes, with a good performance of all the units, but particularly that of our factory in Malaysia, Bahru Stainless, which increased its production by 33% and achieved a positive EBITDA for the first time.

All the units recorded good performances. Acerinox Europa improved its EBITDA by 67%, NAS did so by 60%, Roldán multiplied the figure obtained in 2016 by 11.5 times and only Columbus recorded a more modest growth of 6%, weighed down by the weakness of the South African market.

Particular mention should be made of the fiscal reform in the United States, our main market, which led to an improvement of US\$74 million in our net profit at the end of the year, as a result of the adjustment of the deferred tax liabilities to the new tax rate. Above all, this will improve our profits and our cash generation in the coming years. We estimate that this saving could amount to more than US\$20 million in 2018.

Despite Acerinox's positive results, the numerous uncertainties, a consequence of political situations which affected the economy and the sector, did not help the company's shares to maintain the good progress displayed in 2016, when their value increased by 34%. The share price dropped by 5% in 2017 and, let there be no doubt, we are devoting all our efforts to improving our figures and conveying the hope that the stability of the economic growth will enable us to display the Company's true value.

In 2017 we started up the new production lines at our US subsidiary, North American Stainless, with a cold rolling mill and a BA-finish bright annealing line, and we were honoured to have them opened by Governor Bevin, Kentucky's highest authority, accompanied at the ceremony by Acerinox's Board of Directors,

local authorities and a large number of company employees. The total investment came to €120 million.

With these new lines we intend to increase our production in the United States with a new range of BA-finish products, which were mostly imported into the country until now. This material has very low surface roughness and is very easy to clean. We will be able to rely on the great experience within the Group, as we have already been supplying the most demanding manufacturers of domestic appliances and equipment for food processing from our factories in Spain and South Africa for years.

Throughout 2017 we also built the new Acerinox Europa lines in Spain, a new cold rolling mill, a longitudinal cutting line and an annealing and pickling line, which underwent their testing phase in the first quarter of 2018. These investments total €140 million and will serve to replace the initial equipment commissioned in 1972, which has fulfilled its function perfectly well.

In both cases we have taken the lead over our competitors, with equipment that makes us a technological benchmark in our sector and placing us in an excellent position to capitalise on the improvement in the economic cycle. This equipment incorporates the latest developments in stainless steel production technology, modern mathematical models to adapt to production requirements and all the sensors required for the precise control of operations, in other words, all the essential foundations for data capture to make the most of the benefits of digital transformation. The new designs, carried out in collaboration with the manufacturers and in which we have used all our experience, will improve the quality and reliability of our products while reducing their costs and environmental impact.

We are major consumers of technology and we look to keep our equipment updated with the latest breakthroughs, and we have also allocated €14 million to our own R&D&I developments, especially to the last part, to innovation in processes and products, areas which have always been priorities at Acerinox and where we have set the pace on many occasions. We are now convinced that the gathering of data on the process and an advanced analysis of them will enable us to continue moving forward in terms of efficiency, quality and the overall pursuit of excellence.

Our business is a basic industry and our products serve other industries as raw materials, they are not intended for the general public. But the fact that we have a limited number of suppliers and customers does not exclude us from the digital transformation. For years we have devoted time to gathering data on the conditions of the processes and the properties and characteristics of our steels, data which we use to control our productivity, costs and quality. We have also automated a large number of functions and applied the latest control technologies by means of artificial vision, laser applications, thermography and spectrometry. The massive use of this information by means of advanced data analysis will now give us access to new improvements, provide correlations that are difficult to infer in any other way and anticipate incidents by means of predictive maintenance and smart quality control. We are confident that these advances will improve the

quality and cost of our products, simplify the programming schedule and make it more flexible and provide us with new impetus in the pursuit of excellence. For this reason, we are setting up a large number of projects, mostly auto financed, related to metallurgical quality, advanced programming, demand forecasts, energy efficiency, line sensorisation and transport optimisation, among many others.

In 2017, we invested €173 million on these improvements in innovation within the main process lines mentioned above and on the updating of our equipment. We invested in all the Group's factories and, in accordance with our Strategic Plan, we continue to undertake rapid return investments enabling us to increase the use of our steelmaking capacity and contribute to improving the Company's quality, service and competitiveness, without losing sight of our financial strength. Among other initiatives, it is worth mentioning the new longitudinal cutting line at Columbus, the coil build-up line for NAS, the improvements to the finishing workshop in Roldán and the amount of €8 million assigned to environmental improvements at Acerinox Europa. In 2018, the Acerinox Board approved the acquisition of a spoon furnace for Columbus and another for Acerinox Europa, with a total investment of €33 million.

The cash flow totalling €366 million generated during the year also allowed us to return the dividend in cash in the amount of €124 million.

Acerinox's net financial debt was reduced by €11 million to €609 million, a figure representing only 1.2 times our EBITDA, enabling us to deal calmly with any potential upheaval.

In 2017, taking advantage of the good condition of the financial market, we refinanced €725 million by extending maturities and reducing the cost of financing, which fell by 35% throughout the year in comparison with 2016.

Our Excellence Plans play a fundamental role in the control of the working capital, the improved efficiency of the productive process, our Group's competitiveness and, ultimately, the improvement of our margins. We continue to insist on this difficult objective of achieving more with less and increasing our sales and results by minimising the resources used. This involves using fewer raw materials, less energy, fewer ancillary materials and fewer financial resources to manufacture our product with quality assurance, providing the best service for our customers.

In the ninth year in which these plans have been implemented (the first year of the 2017-2018 Excellence Plan V), we achieved 49% of our goal of annual recurring savings totalling €50 million, in addition to those recorded in previous years.

We can continue to improve, and these plans are complemented by many other projects to help us to extend our good practices to all the areas of the business because, in short, we are seeking a constant undertaking to rethink the way we do things, to improve in all fields so that the initiatives can be listened to and implemented rapidly if it is appropriate to do so. It is, above all, a cultural process.

All these efforts are currently more important than ever, because we have to offset the increases in the main costs involved in stainless steel manufacture by means

of efficiency and productivity, given the better prospects for the economic situation.

Once again, I feel obliged to draw your attention to the high prices of electrical power in Spain, which are increasingly higher than those enjoyed by our closest European competitors. To put some figures on this problem, the electrical energy consumed at our Spanish factory costs at least €20 million more than it would cost at a similar steel mill located in France or Germany.

If we truly believe in the importance of industry in our country and if we have really learnt that the countries with the strongest industries are those which are better equipped to face difficult times, then we have no choice but to commit to the supply of electrical power at competitive prices.

Spain requires a commitment to industry, and that industry requires competitive electrical power to generate wealth and create jobs. We should not get bogged down on technicalities such as the tariff deficit, the offsetting of renewable energy costs, tolls, insularity, interruptability and marginal production costs. Nor is it our role to comment on the most suitable mix for energy generation in our country. We simply demand a final price which enables us to compete on equal terms, because Acerinox and the Spanish steel industry have already demonstrated that they are among the most efficient players in the world, and it would be a shame to squander these qualities and so much talent.

The year just ended was the first in which we have audited our sustainability report, in which you will be able to find the large number of contributions we made to improving the environment, to supporting the communities we operate in, to cooperating with universities and training and research centres and to furthering our employees' professional development.

By way of example, according to the International Stainless Steel Forum, the global association of stainless steel manufacturers, Acerinox emits 35% less CO<sub>2</sub> in its processes than the worldwide industry average.

It is also well worth mentioning the fact that we have managed to reduce the accident rate within our Group and thereby achieve a new record. When we talk about excellence in our operations, we refer to many concepts such as efficiency, productivity and quality, but none are as important as excellence in terms of safety. No production process can be described as excellent if it is not safe for our workers.

We are proud to offer high-quality, stable and well-paid employment, as demonstrated by the low turnover among our employees and the fact that 90% of our contracts are permanent. We have a high-level team of workers, mostly internally trained but sufficiently motivated to seek external knowledge and, with dedication, loyalty and a sense of belonging, to show their appreciation for the opportunity provided by Acerinox to develop a career within the Company, as is my case and that of many of my colleagues who are with us today.

This strong business culture undoubtedly deserves much of the merit for having made Acerinox one of the leading industrial companies in Spain and one of the

global leaders in the manufacture of stainless steel. For this reason we have sought to extend this way of doing things to the five continents, and one of the qualities characterising those of us who form part of Acerinox in Spain, Europe and all the locations in which we operate is that women and men of all races and all religions share their experiences and knowledge.

Of course, career development requires training and, therefore, we devote many more hours than is legally necessary to this activity. In 2017, the collective of 1,139 university graduates received 28,402 hours of training, 746 administrative positions received 10,985 hours and 5,552 operators received 222,200 hours.

In the university field, engineers from CEDINOX, the Stainless Steel Development Association, gave courses to 1,415 students from 19 engineering and architecture schools during the 2016-2017 academic year in an effort to spread knowledge regarding stainless steel, its characteristics and transformation techniques among those who will make the decisions in the future. The second Acerinox Award was organised for participants and it was won by a student from the Technical School of Industrial Engineering of the Polytechnic University of Madrid for her work on the use of lasers for the characterisation of stainless steel surfaces.

We have also continued to make progress in matters of corporate governance, complying with most of the recommendations of the Code of Good Governance and thus becoming an example of transparency. We trust that the adoption of these practices and its monitoring will allow us to improve our management and will help us to convey the principles of honesty and the culture of endeavour which have formed part of Acerinox since its foundation to our shareholders and all the stakeholders related to the Company and society in general.

We have attempted to reflect all the above in the Annual Report 2017, in which the Non-Financial Information Report, audited for the first time, is included and which I recommend you read. We continue to perform our work in a volatile environment, but we trust that the improved performance of the economy will provide us with more stability and will allow us to enjoy the work we do and achieve better results. That is how we have begun 2018, a year in which we hope to continue progressing and exceed the results recorded in 2017. For the time being, the first quarter has gone by as expected and we are reaching our objectives.

To end, I would like to thank you, our shareholders, for the great support you provide, and I also want to thank the entire Acerinox team for their great efforts, dedication, commitment and enthusiasm in continuing to learn and improve. All this, together with the trust they show me every day, encourages me to continue striving to make Acerinox an industry leader, a company worth making a commitment to and one which contributes to society and to its shareholders.

In particular, I would like to thank the Management and my immediate associates for their unconditional loyalty, support and teamwork, and I hope, with the work and efforts of the whole human team comprising Acerinox, that we continue to deserve the trust shown by all of you - shareholders, directors, customers, suppliers and our friends in general.

Many thanks to all of you.

Yours faithfully,  
Bernardo Velázquez  
Chief Executive Officer