

# Financially Ship-Shape and Technologically Pioneering: Continental in Top Form and Growing Quickly and Profitably

Statements by the Chairman of the Executive Board

Dr. Elmar Degenhart

Continental Aktiengesellschaft, Hanover, Germany

at the

Annual Shareholders' Meeting

on April 28, 2017, in Hanover, Germany

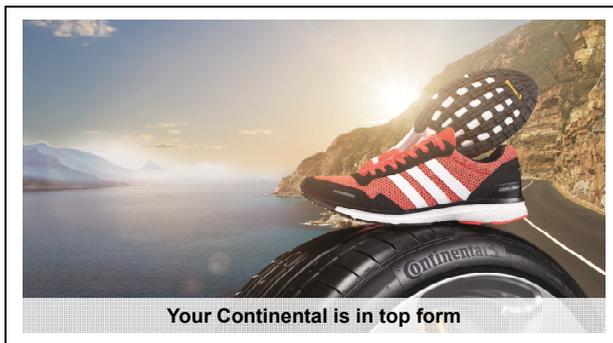
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**Check against delivery**



Ladies and gentlemen!

I am delighted to see you here today.



Financially ship-shape and technologically pioneering: the Continental you see is in top form!

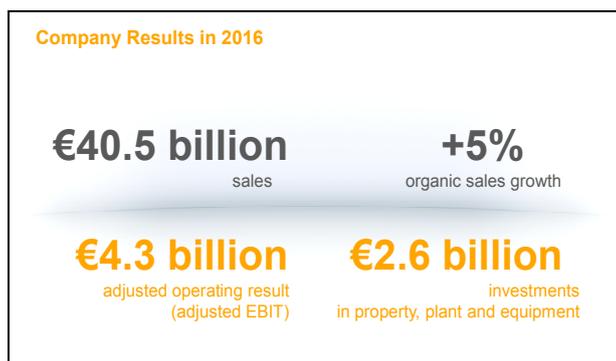
At precisely the moment we need it to be, since the political environment and our industries are undergoing change faster than ever before. Seldom has there been such an exciting and promising time for Continental to shape the future.

This is why our global team and I would like to express our sincerest thanks for investing in us - on behalf of millions of people. After all, with your investment, you are fostering groundbreaking technologies and helping to protect millions of road users around the world from accidents and their consequences. You are contributing to cleaner air, and you are paving the way for intelligent, convenient, and connected driving.

Backed by your support, we are designing future mobility to be sustainable.

By working together, we are thus creating immense value.

## Review of 2016



We continued on our successful trajectory in 2016. We comfortably achieved all the targets we adjusted last October.

Here are the key figures:

- › **Sales:** €40.5 billion, an increase of 3 percent. Discounting exchange rate effects and assuming the same number of consolidated companies as last year, this figure was even as high as 5 percent. This means that we grew at a stronger pace than the market.
- › Adjusted **earnings before interest and taxes:** €4.3 billion: nearly as high as in 2015.
- › This puts our **adjusted EBIT margin** at 10.8 percent of adjusted sales.
- › Our **total equity** is at an all-time high of €14.7 billion, resulting in an **equity ratio** of almost 41 percent.
- › We made investments of around €2.6 billion in property, plant, and equipment. This equates to roughly 6.5 percent of sales and is in line with our strategic objectives.

- › Our **Tire division** posted an exceptional performance. In 2016 for the first time it sold over 150 million passenger-car and truck tires – a new record!
- › At 9.7 percent, the adjusted return on sales of our **ContiTech division** was considerably higher than in the previous year.
- › Our **automotive business** developed well! We are anticipating continued above-average growth in the years to come, given that our customers placed **global orders** worth over €35 billion with us in 2016, representing a year-on-year increase of more than 15 percent.

## Strong team of employees worldwide



Our employees were once again what guaranteed our success. We thank them for their tremendous passion and outstanding commitment!

In light of our successful year, we regret the necessary profit warning issued in October 2016 all the more. It was the first in seven years.

Altogether, we are talking about negative effects of approximately €480 million, which can be explained primarily by provisions for warranty cases and pending antitrust proceedings.

Without these necessary revisions, we would have had another record year.

Ladies and gentlemen,

I would like to stress once again in explicit terms that while the circumstances behind most of these incidents may well have taken place some time ago, they are still unacceptable!

We will continue to do everything in our power to avoid incidents like these. Meeting the highest quality standards and acting within ethical bounds are non-negotiable for us. We punish violations against this with absolute consistency.

The early warning mechanisms we have in place today, which are triggered by non-compliance with regulations, function exceptionally well. They do so because we investigate and pursue each and every violation in detail and use our findings to improve our control mechanisms.

We will, of course, promptly inform you, our shareholders, about the conclusion of the current cases.

## Earnings per share, dividend, and total shareholder return



In 2016, our profit after taxes amounted to €2.8 billion – despite the aforementioned additional expenses. This surpassed last year's figure of €2.7 billion, which corresponds to €14.01 per share. Compared with the excellent year before, this increase is just under 3 percent.

By contrast, we were not satisfied with the performance of our share price in 2016.

As shareholders, you are investing your money in the lasting success of your Continental.

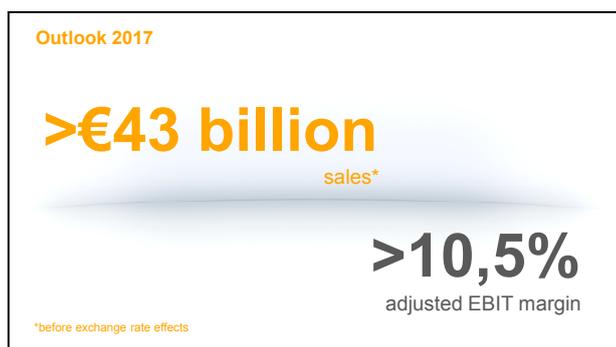
We thank you for your loyalty.

Our successful performance is what's allowing the Executive Board and Supervisory Board to propose a dividend of €4.25 per share.

This means that we will have increased the payout for the sixth time in a row!

And we promise you that we will continue to work hard this year to justify your trust.

## Outlook for 2017



Our successful start to 2017 proves that we are continuing to grow profitably and at a faster rate than our markets!

- › We anticipate a moderate rise in global vehicle production of more than 1 percent to around 94 million passenger cars and light commercial vehicles.

There is a slight decline in growth on the American market. But growth in China and Europe in particular is likely to more than compensate for this decline. Stabilizing markets in Brazil and Russia are likely to help as well.

- › For fiscal 2017, we expect an increase in sales of 6 percent to over €43 billion not taking into account fluctuations in exchange rates.
- › For the current year, we anticipate increased raw material costs. The Tire and ContiTech divisions are expecting this to have an additional negative impact of around €500 million in total.
- › For 2017, we want to achieve an adjusted EBIT margin of 10.5 percent.

In other words, we are aiming to reach new performance heights in an extremely challenging environment.

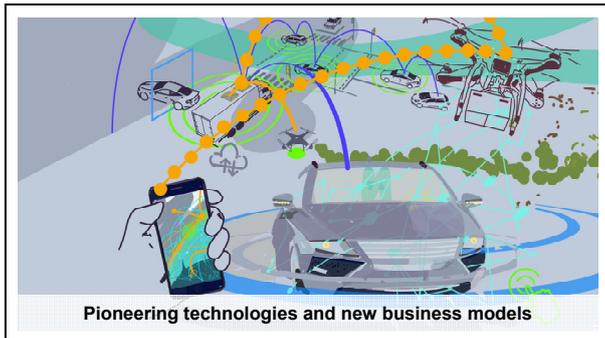


We continued our successful trajectory in the first quarter.

- › Sales were €11 billion, an increase of 11.7 percent year-on-year.
- › Adjusted EBIT amounted to roughly €1.2 billion - 7 percent more than in the first quarter of 2016.
- › The adjusted EBIT margin was 10.7 percent.
- › We will publish our full key financial figures for the first quarter on May 9, 2017.

Our successful trajectory gives us cause to believe that we will surpass total sales of €50 billion in 2020.

## Six levers for profitable growth and value creation

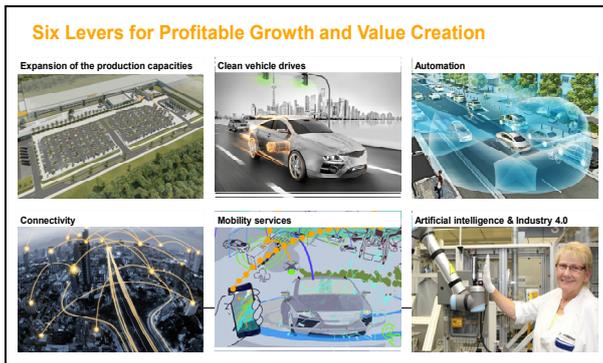


Ladies and gentlemen,

Our industries and markets are undergoing a fundamental transformation. This transformation is not stopping at established technologies and proven business models.

Electrification, automation, and digitalization – the inner workings of the car as we know it will be made up completely differently in 10 to 15 years' time. Our industry is experiencing new impetus on a vast scale in terms of innovation and efficiency. Mobility and the way in which it is delivered is becoming more sustainable as a result. In other words: safer, cleaner, and more convenient.

The car is currently undergoing the greatest transformation process in its history of more than 130 years. With vigor and purpose, we continue to shape its future. We are enhancing value sustainably with pioneering technologies and new business models.



With this aim in mind, we are activating six levers:

1. We are expanding our production capacities and our business areas. We are also acquiring companies where necessary.
2. We are ensuring clean vehicle drives.
3. We are digitalizing mechanical systems and automating driving.
4. We are making the vehicle part of the Internet and connecting it to the new mobility ecosystem.
5. We are also generating additional growth with innovative mobility services.
6. We are enhancing our competitiveness with artificial intelligence and Industry 4.0.

Lever number one: our investments in production and business areas

Have you met the new star in our summer tire range? Here it is!



Our new PremiumContact 6: A test winner right from the start. Safe, strong and environmentally conscious: our guardian angel that helps you stay safely in the lane and brings you to a safe stop.

Many things will be different about the car of the future. But one thing will be exactly the same: safe contact with the road.

This is ensured by our premium tires, the demand for which increases with each passing year. This can be explained by their outstanding quality and our strong brand image. What's more, we are seeing vehicle numbers on the roads worldwide grow year on year along with our production capacities.



Since 2011, we have invested over €4 billion in establishing globally balanced production structures. This has included a number of new tire plants such as in the USA. We have expanded existing production facilities. Starting in 2019, we will establish passenger car tire production operations in Thailand for the Southeast Asian market.

We want to gradually increase our share of sales with industrial customers and end users.

Growth in tire business is contributing to this, but our ContiTech division is playing a key role, too. The division continued to pursue its growth strategy with acquisitions in 2016. A prominent example is the purchase of the Hornschuch Group, a leading manufacturer of film and artificial-leather surfaces for car parts, furnishings and components.

## Lever number two: clean vehicle drives



Cars of the future will feature electric drives, which will be fully connected and automated.

But the combustion engine is evolving, too. It actually still has its peak ahead of it. We don't expect to see a gradual decline in volumes until after 2025.

Up until this point, we can make it even more efficient, for example with our "people's hybrid" for wide-ranging vehicle segments. Our 48-volt system is making the combustion engine quieter and the air cleaner. We are a trailblazer in this respect, having been the first to bring this system into production for the market.

We strongly believe in fully electric driving. This is the market of the future. This is why we have invested a total of more than €1 billion in it over the past few years. We are currently working on some 20 production projects worldwide.

Our components and systems for electric cars are opening up new growth opportunities for our company. We are able to generate greater revenues per vehicle with them than with solutions for combustion engine drive systems.

In the eyes of car buyers, the electric vehicle still requires two key elements to finally break through: greater range and lower acquisition costs.

Both of these requirements could be met with, above all, a leap forward in battery-cell technology. And we expect to see this by 2025.

We are investing on an increasingly bigger scale in the research and development of electric drives. Demand for our products and systems for hybrid and electric vehicles is growing. In the past year alone, our orders were worth more than €1.2 billion, up 17 percent on 2015.

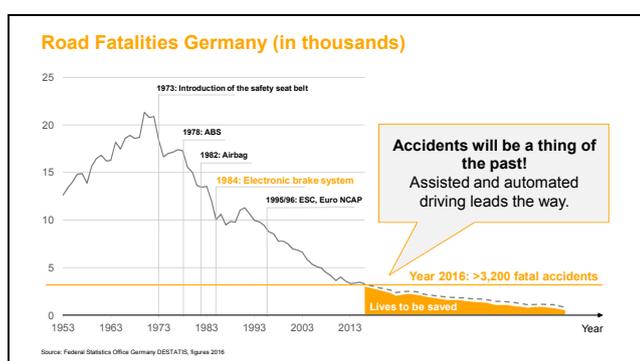
By the same token, we want our combustion drive business to remain competitive globally. We want to help set the tone of the industrial transition in the next 15 years from a position of strength. We want to create momentum in this demanding market – with additional innovative solutions such as exhaust-gas aftertreatment systems.

We have every reason to be confident. This year, our powertrain business is expected to continue to grow at a much faster pace than global vehicle production.

This year, we are expecting to achieve an adjusted EBIT margin of 9 percent followed by around 10 percent annually in the years to come. This is not taking into account hybrid and electric drive business.

We still anticipate powertrain sales to be around the €10 billion mark in 2019.

### Lever number three: digitalized mechanical systems and automated driving



Our first electronic brake system went into production 33 years ago. It prevents the wheels from locking during braking. Millions of road users owe their lives to this and to electronic stability control.

We have started off the digitalization of mobility by improving mechanical systems with electronics and software. Today, we have over 13,500 software developers worldwide who are successfully driving this process forward.

Our additional 18,500 engineers are making vehicles safer, engines cleaner, and driving itself more relaxed.

We now already generate 60 percent of our sales in the automotive sector with digital products. And this figure is rapidly increasing.



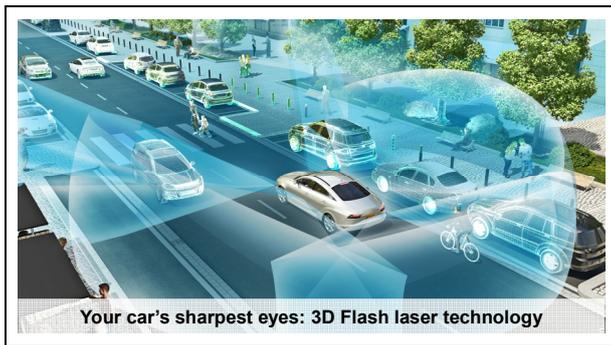
Particularly strong growth was recorded by our **advanced driver assistance systems**. In 2016, our sales here amounted to over €1.2 billion.

The number of new orders simultaneously increased to over €3 billion.

As such, we are anticipating sales of considerably more than €2 billion by 2020.

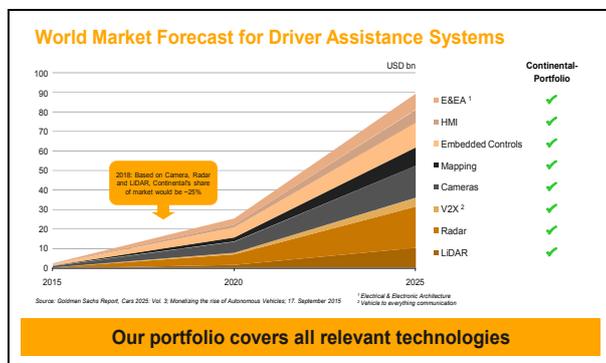
The assisted driving of today is the preliminary stage on the way to the automated driving of tomorrow.

For assisted driving pre-2020, a vehicle requires up to ten sensors. For automated driving thereafter, it will require as many as 20 sensors or more, and we expect this to trigger a further boost in our sales.



One of our drivers of growth is our pioneering laser technology. It will be ready for production by 2020. The technology incorporates a core optical system, which works using pulses of light, in a similar way to a series of flash photos. This provides an exceptionally accurate and distortion-free three-dimensional map of the vehicle's surroundings.

Dim light, darkness, glare, heavy rain? Your vehicle's extremely good vision is created by our laser beams, which guide you safely onward.



Automated driving is an evolutionary development, and our innovations are accelerating this development.

Studies indicate that the overall market for assisted and automated driving is growing at an ever faster rate. Sales in this market are expected to develop from their current level of around €12 billion to approximately €90 billion in 2025.

Your Continental is right at the forefront of shaping this growth.

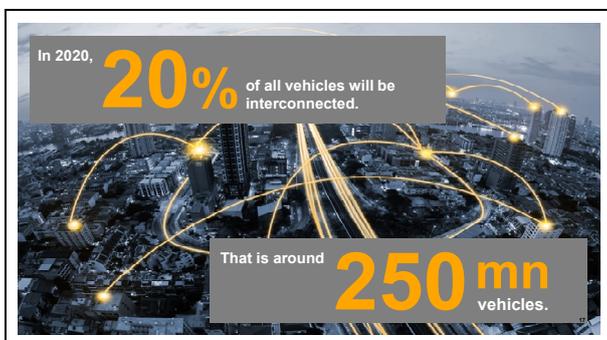
Experience this exciting development for yourself! Come to the International Motor Show Commercial Vehicles in Frankfurt in September! Visit our stand there in Hall 5.1!

## Lever number four: the vehicle as part of the Internet within the new mobility ecosystem

Our first telematics modules rolled off the production line at the start of 1996. This allowed people to make a wireless emergency call from their car. Nowadays, over 28 million vehicles are equipped with our connectivity systems.

Right now, we have transmission power of a few hundred megabits per second available. As of 2022, several gigabits per second are expected here in this country.

This is the next milestone on the road to the intelligent mobility of the future. Because a rapid data connection means the ability to take advantage of collective intelligence across connected vehicles.



In 2020, there will be more than 250 million vehicles connected to each other and to traffic facilities. That's around a fifth of total global vehicle stock.

They will all collect and exchange data, and communicate via the Internet - and this will bring about a brand new market for mobility-related services worth billions.

This connectivity will be particularly relevant for inner-city mobility. After all, by 2050 more than two-thirds of all people will be living in cities. Today, this number is just over half.



The city of the future will need more robot taxis: an automated fleet of small computers on wheels. These will be electrically powered and extremely efficient. After all, they will be ready to go wherever and whenever people need them. They will automatically navigate the roads. They will chauffeur individuals or groups of people. They will run day and night. They will be reliable, remotely maintained, and – above all – on time.

In this way, future mobility will be made more cost-effective, environmentally friendly, convenient, and safe. Our systems will make them part of the Internet. They will connect them to this new mobility ecosystem and to the people that use it.

Our integrated sensors will record all the data people need during their journeys including any permanent roadworks, the weather conditions, the charge level of the battery, the gross vehicle weight, and the condition of the units. Not only this, but also traffic flow, traffic jams, diversions, slippery road surfaces, icy roads, new traffic signs, road markings, changed traffic light phases, or road damage.

The swarm of vehicles will record data like this while on the road. It will send it in anonymous format to our database in the Continental cloud, where it will be available to everyone else. Practically in real time.

We estimate that in the future roughly two-thirds of all passenger cars in cities will be fleet cars. If so, more than half of all cars manufactured worldwide in 2050 would be part of a large fleet.

Companies that specialize in fleets like these will make their money especially not from cars but from services.

This is why carmakers are investing particularly heavily in vehicle fleets and rental services. Internet companies are, too.

Internationally leading suppliers like your Continental will be in the driving seat! Not only with our products and functions, but increasingly with our services as well.

### Lever number five: additional growth with innovative mobility services



We're already marketing a range of services right now. Some of them either enhance our products' functionality or augment it. And others are standalone products because they consist purely of software like the apps you are familiar with on your cell phone.

#### Example #1: ContiConnect tire-monitoring system

We're currently launching our intelligent tire-monitoring system **ContiConnect** on the market. This product will augment our tires' functionality for fleet use with additional services.

Our tire sensors measure truck tire pressure and temperature throughout the journey. We analyze and interpret this data with the help of our software. This is how we identify impending tire damage in advance. Drivers, mechanics, and fleet managers thus receive pointers for preventive maintenance, which results in lower fuel consumption, fewer interruptions to the journey, longer tire life, and more reliable deliveries.

Who has ever got annoyed by a broken-down truck out on the freeway? It's funny how something like that always happens when you're in a rush.

### **Example #2: Fleet management by Zonar**

**Zonar** is the solution here. We acquired a majority stake in this U.S. company at the end of 2016. Its software programs and apps for commercial vehicles monitor driving times, service intervals, driving style and fuel economy, and compliance with speed limits. They establish a constant connection between the vehicle and the fleet manager, resulting in lower fuel consumption and fewer emissions. Trucks also spend less time at the mechanic's and break down less often. This all saves time and money.

Preventive maintenance is also extremely relevant for our customers outside the automotive industry, such as in the extraction of raw materials.

### **Example #3: Preventive maintenance in industries**

Conveyor belts in this industry are tough cookies. They transport substances like rare earths for the latest electronics, ores for copper smelters or glowing hot slag over hundreds of kilometers. Built-in sensors allow us to notify mine operators of what condition these belts are in, enabling them to adjust their belt's load until an optimum repair time presents itself.

### **Example #4: Digital car key**

My next example is a pure service: the digital car key. Car rental companies want it and so do their customers.

Let's imagine that you want to rent a car quickly right now. What do you do?

Look for a rental station? That takes too long.

Why don't you get your cell phone to rent the car instead!

Is this a utopia? Not at all!

Our programming can do just that.

The Continental app on your cell phone looks for the right vehicle in your local area and books it at the same time. The necessary information is sent over the Internet, and stored on your cell phone's SIM card in an encrypted and forgery-proof format.

The car is equipped with the necessary readers. The digital key is checked and verified, then the engine is started and you can set off on your journey.

Right now, we're filling 12 orders for this system, which come from rental companies and fleet operators.

The demand for services like these is growing tremendously. But we're growing right along with it - especially in China. A few days ago, we arranged the formation of a joint venture with China Unicom. We will have a 50-percent stake in this joint venture. China Unicom is one of the largest telecommunications companies. We want to work together to develop a platform for intelligent and connected vehicle rental services.



Our Intelligent Transportation Systems business unit in Silicon Valley has precisely this task of providing intelligent solutions for the management of interconnected transportation systems in cities.

We have just opened an R&D center in San José, California, with this aim in mind. Up to 300 software engineers, programmers, designers, and researchers will collaborate closely at this location. They will develop pioneering services for mobility of the future across all our business areas.

### **Example #5: Electronic horizon**

The fifth example is our digital map stored locally in the vehicle. We call it eHorizon, which stands for electronic horizon.

It gains an accurate picture of the route profile during the journey. We connect it permanently to the database in the Continental cloud.

We are enabling anticipatory driving using maps and up-to-date information from the cloud. Warnings are sent virtually in real time - and not when you're already stuck in a traffic jam. Reliable alternative routes are suggested to you in advance. This makes your driving more eco-friendly and saves time, fuel, and stress.

We are currently working on major production orders for our eHorizon with manufacturers in Europe, the U.S.A., and Japan.

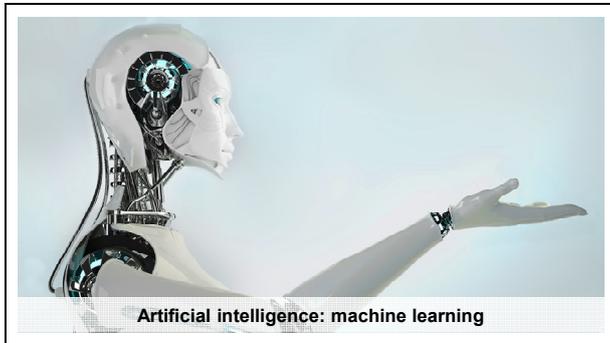
### **Sales expectations with mobility-related services**

This year, our sales with mobility-related services will total over €500 million. This figure includes services that enhance or augment the functionality of our components, and also pure software products.

By 2020, we expect our sales to have more than doubled to over €1 billion.

And this is only the beginning! This billion-dollar global market is just beginning to take off. Its enormous potential and rapid growth present us with unique opportunities.

## Lever number six: greater competitiveness thanks to artificial intelligence and Industry 4.0



We are currently in the process of leveraging the full potential of artificial intelligence – for the benefit of all our business areas and all divisions of our company. This will help us to dramatically increase our efficiency and effectiveness.

By artificial intelligence we mean mechanisms with which machines or computers can develop intelligent behavior, allowing them to perform functions that usually require human intelligence autonomously. One example of this is responses derived from a bank of stored experiences. This includes intelligent speech recognition whereby the computer memorizes my pronunciation and vocabulary thus progressively improving its understanding of my instructions.



We have 100 experts working all over the world in 14 research disciplines to exploit the opportunities of artificial intelligence.

We are collaborating in this field with excellent institutions, including the University of Oxford and the technical universities in Darmstadt and Munich.

We are using artificial intelligence to make our products more intelligent.

We are equipping one of our new camera generations with deep neural networks. This is an artificial, simulated nervous system designed to recognize and classify images. In our case, these are images of road scenarios and the elements within them such as roads, people, and objects. The system learns to classify all the elements into categories when driving. The advantages associated with this are accurate recording of reality, less programming, and enhanced road safety.

Let me show you how it works.

*(First film clip AI).*

- › Our system is able to recognize people and tell them apart. In our first film clip, visibility is good. An adult is leaning against a wall far away from the road. The risk of an accident is low. A regular speed is maintained. The system keeps an eye on the person merely for safety's sake.

*(End of film)*

*(Second film clip)*

- › This scene is different: a pedestrian is close to the roadside. The person is not on the phone and is probably not distracted from the road traffic. Such a person is not likely to suddenly step out onto the road. The car's artificial intelligence has learned this already. It also recognizes that the person's backpack is suitable for an adult.

Given that the pedestrian is walking so close to the road, it keeps them firmly in view. The car drives more slowly, just in case.

*(End of film)*

*(Third film clip)*

- › In the third scene, pay attention to the backpack in the pedestrian's hand. A small detail, but a major change to the road conditions for the artificial intelligence. It has learned that this kind of backpack belongs to a child, not an adult.

For the electronics, this means caution! A child might be nearby; adjust your speed and be ready to brake.

And there is the child. Our system identified the potential danger in advance based only on a small detail: the child's backpack.

*(End of film)*

The anticipatory and reliable response of artificial intelligence makes road traffic safer for all.



We are using artificial intelligence to expand the possibilities of our Production 4.0.

One way we are doing this is through quality analyses in electronics manufacturing. We use image assessment systems for this. Our inspection machines must not overlook any errors with X-ray images, for example.

This is why they are calibrated with such high sensitivity. But unfortunately this means that every now and again they report pseudo-errors and our employees then need to spend a lot of time doing follow-up checks.

Using machine learning, we can convert the X-ray images to operands. Then we compare the numbers. This results in fewer pseudo-errors and genuine errors are no longer overlooked.

We will be putting this intelligent check into widespread use later on this year.

My second and concluding example involves our value chains from the supplier right through to the customer. We are using artificial intelligence to create greater transparency so that we know which components and systems are being processed and delivered from which supplier at all times. This enables us to improve supply chain management.

Self-learning and self-controlling systems are not just allowing us to respond quicker.

- › We are also handling order modifications more flexibly.
- › We are enhancing our quality.
- › We are cutting storage costs.
- › We are meeting individual customer requirements more easily.
- › We are understanding our production operations better and making more reliable predictions.

The dimensions of this neuronal production network with our suppliers and customers are enormous. Last year alone, our three automotive divisions supplied our customers with around 1.8 billion products. This required us to purchase around 122 billion components. They were processed in more than 100 of our plants.

Artificial intelligence in production also involves using collaborative robots, known as cobots. They work side by side with humans and work consistently to the same set of procedures with absolutely zero errors. We have more than 200 cobots in our employ today. Their number will increase at least fivefold in the next four years.

Your Continental is one of leading companies shaping Industry 4.0, according to a recent study of 235 German companies. My examples showed you a few exciting reasons why.



Ladies and gentlemen,

As you can see, your Continental is all set for the mobility of the future.

We once grew with horsepower and hoof buffers. Now we are growing progressively with billions of bits and bytes.

This is called changing tack: Continental the tire manufacturer, automotive supplier and industrial partner has become Continental the producer of leading technology and provider of services.

There are opportunities for us in this process of constant change. We are more determined than ever to systematically seize these opportunities.

You are well aware:

- › If you invest too early you lose millions.
- › But if you invest too late, you will lose out on the market!

With us, you will make gains on both fronts: money and the future!

So why don't you take the fast lane to success - with us - now!

We are looking forward to it!