

Vidrala, S.A.
and
Subsidiaries

Consolidated Annual Accounts
31 December 2016

Consolidated Directors' Report
2016

(With Independent Auditor's Report Thereon)

Prepared in accordance with International
Financial Reporting Standards as adopted by the
European Union

(Free translation from the original in Spanish. In
the event of discrepancy, the Spanish-language
version prevails)



KPMG Auditores S.L.

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Independent Auditor's Report on the Consolidated Annual Accounts

(Translation from the original in Spanish. In the event of discrepancy,
the Spanish-language version prevails)

To the Shareholders of
Vidrala, S.A.

Report on the Consolidated Annual Accounts

We have audited the accompanying consolidated annual accounts of Vidrala, S.A. (the "Company") and its subsidiaries (the "Group"), which comprise the consolidated balance sheet at 31 December 2016 and the consolidated income statement, consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and consolidated notes.

Directors' Responsibility for the Consolidated Annual Accounts

The Directors are responsible for the preparation of the accompanying consolidated annual accounts in such a way that they give a true and fair view of the consolidated equity, consolidated financial position and consolidated financial performance of Vidrala, S.A. and subsidiaries, in accordance with International Financial Reporting Standards as adopted by the European Union (IFRS-EU) and other provisions of the financial reporting framework applicable to the Group in Spain, and for such internal control that they determine is necessary to enable the preparation of consolidated annual accounts that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated annual accounts based on our audit. We conducted our audit in accordance with prevailing legislation regulating the audit of accounts in Spain. This legislation requires that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated annual accounts are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated annual accounts. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the consolidated annual accounts, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation of the consolidated annual accounts in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated annual accounts taken as a whole.



We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the accompanying consolidated annual accounts give a true and fair view, in all material respects, of the consolidated equity and consolidated financial position of Vidrala, S.A. and subsidiaries at 31 December 2016 and of their financial performance and consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the European Union and other provisions of the financial reporting framework applicable in Spain.

Report on Other Legal and Regulatory Requirements

The accompanying consolidated directors' report for 2016 contains such explanations as the Directors of Vidrala, S.A. consider relevant to the situation of the Group, its business performance and other matters, and is not an integral part of the consolidated annual accounts. We have verified that the accounting information contained therein is consistent with that disclosed in the consolidated annual accounts for 2016. Our work as auditors is limited to the verification of the consolidated directors' report within the scope described in this paragraph and does not include a review of information other than that obtained from the accounting records of Vidrala, S.A. and subsidiaries.

KPMG Auditores, S.L.

(Signed on original in Spanish)

Cosme Carral López-Tapia

22 February 2017

VIDRALA, S.A. AND SUBSIDIARIES

Consolidated Balance Sheets

31 December 2016 and 2015

(Expressed in thousands of Euros)

(Free translation from the original in Spanish. In the event of discrepancy, the Spanish-language version prevails)

	<u>Note</u>	<u>2016</u>	<u>2015</u>
<u>ASSETS</u>			
Non-current assets			
Property, plant and equipment	6	592,727	656,638
Goodwill	7	59,233	59,233
Other Intangible assets	7	12,010	7,013
Other financial assets		287	8
Deferred tax assets	9	39,768	41,860
Derivative financial instruments	8	4,256	1,556
Other non-current assets		107	102
		<u>708,388</u>	<u>766,410</u>
Current assets			
Inventories	10	180,973	201,010
Trade and other receivables	11	194,456	205,278
Current tax assets		391	5,049
Derivative financial instruments	8	2,777	-
Other current assets	12	8,834	6,736
Cash and cash equivalents		424	15,720
		<u>387,855</u>	<u>433,793</u>
Total assets		<u>1,096,243</u>	<u>1,200,203</u>

The accompanying notes form an integral part of the consolidated annual accounts.

VIDRALA, S.A. AND SUBSIDIARIES

Consolidated Balance Sheets

31 December 2016 and 2015

(Expressed in thousands of Euros)

(Free translation from the original in Spanish. In the event of discrepancy, the Spanish-language version prevails)

<u>EQUITY AND LIABILITIES</u>	Note	2016	2015
Equity	13		
Share capital		25,290	25,290
Other reserves		7,545	5,234
Retained earnings		481,879	431,780
Own shares		(2,824)	-
Other comprehensive income		(22,594)	27,318
Interim dividend distributed during the year		(14,362)	(13,086)
		474,934	476,536
Equity attributed to equity holders of the Parent			
Non-current liabilities			
Deferred income	14	31,535	33,663
Loans and borrowings	15	310,288	415,832
Derivative financial instruments	8	5,263	5,638
Deferred tax liabilities	9	47,866	47,402
Provisions	19	10,684	3,771
Other non-current liabilities		1,145	2,604
		406,781	508,910
Current liabilities			
Loans and borrowings	15	12,402	4,050
Derivative financial instruments	8	50	6,399
Trade and other payables	16	174,506	167,721
Current tax liabilities		5,188	7,039
Provisions	19	1,071	-
Other current liabilities	12	21,311	29,548
		214,528	214,757
Total liabilities		621,309	723,667
Total equity and liabilities		1,096,243	1,200,203

The accompanying notes form an integral part of the consolidated annual accounts.

VIDRALA, S.A. AND SUBSIDIARIES

Consolidated Income Statements
for the years ended
31 December 2016 and 2015

(Expressed in thousands of Euros)

(Free translation from the original in Spanish. In the event of discrepancy,
the Spanish-language version prevails)

	<u>Note</u>	<u>2016</u>	<u>2015</u>
Revenues	22	773,570	803,365
Other income	22	8,456	9,892
Changes in inventories of finished goods and work in progress		(10,362)	(14,713)
Merchandise, raw materials and consumables used		(268,308)	(289,159)
Employee benefits expense	24	(166,131)	(166,115)
Amortisation and depreciation	6 & 7	(75,556)	(75,062)
Impairment of non-current assets	6	(2,116)	90
Other expenses	23	(166,514)	(182,011)
Finance income	25	979	1,650
Finance costs	25	(9,776)	(12,314)
Profit before income tax from continuing operations		84,242	75,623
Income tax expense	9	(16,571)	(14,763)
Profit for the year from continuing operations		67,671	60,860
Profit for the year		67,671	60,860
Profit for the year attributable to equity holders of the Parent		67,671	60,860
Earnings per share (expressed in Euros)			
- Basic and diluted		2.73	2.46

The accompanying notes form an integral part of the consolidated annual accounts.

VIDRALA, S.A. AND SUBSIDIARIES

Consolidated Statements of Comprehensive Income
for the years ended
31 December 2016 and 2015

(Expressed in thousands of Euros)

(Free translation from the original in Spanish. In the event of discrepancy,
the Spanish-language version prevails)

	<u>Note</u>	<u>2016</u>	<u>2015</u>
Profit for the year		<u>67,671</u>	<u>60,860</u>
Other comprehensive income:			
Translation differences	13	(57,397)	34,853
Remeasurements of defined benefit plans		(1,308)	-
Items to be reclassified in profit or loss			
Cash flow hedges	8	12,213	(9,753)
Tax effect		<u>(3,420)</u>	<u>2,731</u>
Other comprehensive income, net of income tax		<u>(49,912)</u>	<u>27,831</u>
Total comprehensive income for the year		<u>17,759</u>	<u>88,691</u>
Profit for the year attributable to equity holders of the Parent		<u>17,759</u>	<u>88,691</u>

The accompanying notes form an integral part of the consolidated annual accounts.

VIDRALA, S.A. AND SUBSIDIARIES

Consolidated Statements of Changes in Equity
for the years ended
31 December 2016 and 2015

(Expressed in thousands of Euros)

(Free translation from the original in Spanish. In the event of discrepancy, the Spanish-language version prevails)

	Equity attributable to equity holders of the Parent								
	Share capital	Other reserves	Retained earnings	Own shares	Cash flow hedges	Translation differences	Defined benefit plans	Interim dividend paid during the year	Total equity
Balances at 31 December 2014	25,290	5,234	386,581	(236)	(513)	-	-	(11,891)	404,465
Total comprehensive income for the year	-	-	60,860	-	(7,022)	34,853	-	-	88,691
Own shares redeemed	-	-	-	(6,498)	-	-	-	-	(6,498)
Own shares sold	-	-	497	6,734	-	-	-	-	7,231
Share capital increase	-	-	-	-	-	-	-	-	-
Share capital reduction	-	-	-	-	-	-	-	-	-
Distribution of 2014 profit	-	-	-	-	-	-	-	-	-
Dividends	-	-	(16,225)	-	-	-	-	11,891	(4,334)
Interim dividend on account of 2015 profit	-	-	-	-	-	-	-	(13,086)	(13,086)
Other movements	-	-	67	-	-	-	-	-	67
Balances at 31 December 2015	25,290	5,234	431,780	-	(7,535)	34,853	-	(13,086)	476,536
Total comprehensive income for the year	-	-	67,671	-	8,793	(57,397)	(1,308)	-	17,759
Revaluation of property, plant and equipment, net of tax (note 13(b))	-	2,311	-	-	-	-	-	-	2,311
Own shares redeemed	-	-	-	(3,757)	-	-	-	-	(3,757)
Own shares sold	-	-	281	933	-	-	-	-	1,214
Share capital increase	-	-	-	-	-	-	-	-	-
Share capital reduction	-	-	-	-	-	-	-	-	-
Distribution of 2015 profit	-	-	-	-	-	-	-	-	-
Dividends	-	-	(17,853)	-	-	-	-	13,086	(4,767)
Interim dividend on account of 2016 profit	-	-	-	-	-	-	-	(14,362)	(14,362)
Balances at 31 December 2016	25,290	7,545	481,879	(2,824)	1,258	(22,544)	(1,308)	(14,362)	474,934

The accompanying notes form an integral part of the consolidated annual accounts.

VIDRALA, S.A. AND SUBSIDIARIES

Consolidated Statements of Cash Flows
for the years ended
31 December 2016 and 2015
(Indirect Method)

(Expressed in thousands of Euros)

(Free translation from the original in Spanish. In the event of discrepancy,
the Spanish-language version prevails)

	Note	2016	2015
Cash flows from operating activities			
Profit for the year		67,671	60,860
<i>Adjusted for:</i>			
Amortisation and depreciation	6 & 7	75,557	75,062
Impairment of non-current assets	6	2,116	(346)
(Reversal of) impairment losses on trade receivables		409	522
(Reversal of) impairment losses on inventories		5,619	5,171
Exchange (gains) / losses	25	(805)	(637)
Changes in provisions	19	9,039	-
Government grants recognised in the income statement		(6,201)	(6,937)
Finance income	25	(174)	(1,650)
Finance costs	25	9,776	11,677
Income tax	9	16,571	14,763
		<u>111,907</u>	<u>97,625</u>
Changes in working capital			
Inventories		14,418	(1,440)
Trade and other receivables		5,422	(44,770)
Trade and other payables		(3,362)	22,302
Application of provisions		(388)	3,188
Other current liabilities		(10,000)	-
Effect of translation differences on operating assets and liabilities of foreign operations		<u>(11,690)</u>	<u>15,138</u>
Cash used in operating activities		(5,600)	(5,582)
Interest paid		(9,776)	(10,313)
Interest received		174	1,650
Income tax paid		(6,772)	(5,790)
Other amounts received		-	67
Net cash from operating activities		<u>157,604</u>	<u>138,517</u>
Cash flows from investing activities			
Proceeds from sale of property, plant and equipment		542	223
Proceeds from sale of intangible assets		-	10
Proceeds from sale of financial assets		-	1,358
Acquisition of property, plant and equipment		(51,364)	(58,931)
Acquisition of intangible assets		(3,540)	(569)
Acquisition of financial assets		(284)	-
Investments in Group companies, associates and jointly controlled entities (notes 3 and 5)		<u>-</u>	<u>(403,191)</u>
Net cash used in investing activities		<u>(54,646)</u>	<u>(461,100)</u>
Cash flows from financing activities			
Proceeds from issue of treasury shares and own equity instruments		1,214	7,231
Proceeds from loans and borrowings		12,808	440,000
Payments to redeem own shares and other own equity instruments		(3,757)	(6,498)
Payments of loans and borrowings		(110,000)	(89,492)
Dividends paid		(18,519)	(16,750)
Grants, donations and bequests received		<u>-</u>	<u>3,750</u>
Net cash from/(used in) financing activities		<u>(118,254)</u>	<u>338,241</u>
Net increase/(decrease) in cash and cash equivalents		(15,296)	15,658
Cash and cash equivalents at 1 December		<u>15,720</u>	<u>62</u>
Cash and cash equivalents at 31 December		<u>424</u>	<u>15,720</u>

The accompanying notes form an integral part of the consolidated annual accounts.

VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

31 December 2016

(Free translation from the original in Spanish. In the event of discrepancy,
the Spanish-language version prevails)

1. Nature, Principal Activities and Composition of the Group

Vidrala, S.A. (hereinafter the Company, the Parent or Vidrala) was incorporated with limited liability under Spanish law. Its principal activity is the manufacture and sale of glass containers and its registered office is in Llodio (Alava, Spain).

Vidrala, S.A. shares are listed on the Madrid and Bilbao stock exchanges.

On 14 January 2015 the Group company Inverbeira Sociedad de Promoción de Empresas, S.A. acquired Encirc Limited, which in turn owns Encirc Distribution Limited (see note 5).

As a result of this acquisition, in addition to the manufacture of glass containers, the Group now carries out beverage packaging activities and offers integrated logistical services for packaged food products within the United Kingdom.

Details of the companies comprising the Vidrala Group, the interest held by the Parent (direct and/or indirect) at 31 December 2016 and the location and activity of each company that forms part of the consolidated group are as follows:

(Continued)

VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

<u>Company</u>	<u>Location</u>	<u>Investment</u>	<u>Shareholder</u>	<u>Activity</u>
<u>Crisnova Vidrio, S.A.</u>	<u>Caudete (Albacete, Spain)</u>	<u>100%</u>	<u>Vidrala, S.A.</u>	<u>Manufacture and sale of glass containers</u>
<u>Inverbeira, Sociedad de Promoción de Empresas, S.A.</u>	<u>Llodio (Alava, Spain)</u>	<u>100%</u>	<u>Vidrala, S.A.</u>	<u>Promotion and development of companies</u>
<u>Aiala Vidrio, S.A.U.</u>	<u>Llodio (Alava, Spain)</u>	<u>100%</u>	<u>Vidrala, S.A.</u>	<u>Manufacture and sale of glass containers</u>
<u>Gallo Vidro, S.A.</u>	<u>Marinha Grande (Portugal)</u>	<u>99.99%</u>	<u>Inverbeira, Sociedad de Promoción de Empresas, S.A.</u>	<u>Manufacture and sale of glass containers</u>
<u>J. Ferreira da Silva, Ltda.</u>	<u>Marinha Grande (Portugal)</u>	<u>100%</u>	<u>Gallo Vidro, S.A.</u>	<u>Transport services</u>
<u>Castellar Vidrio, S.A.</u>	<u>Castellar del Vallés (Barcelona, Spain)</u>	<u>100%</u>	<u>Inverbeira, Sociedad de Promoción de Empresas, S.A.</u>	<u>Manufacture and sale of glass containers</u>
<u>Vidrala Italia, S.R.L.</u>	<u>Corsico (Italy)</u>	<u>100%</u>	<u>Inverbeira, Sociedad de Promoción de Empresas, S.A.</u>	<u>Manufacture and sale of glass containers</u>
<u>MD Verre, S.A.</u>	<u>Ghlin (Belgium)</u>	<u>100%</u>	<u>Inverbeira, Sociedad de Promoción de Empresas, S.A.</u>	<u>Manufacture and sale of glass containers</u>
<u>Omèga Immobilière et Financière, S.A.</u>	<u>Ghlin (Belgium)</u>	<u>100%</u>	<u>Inverbeira, Sociedad de Promoción de Empresas, S.A.</u>	<u>Real estate</u>
<u>Investverre, S.A.</u>	<u>Ghlin (Belgium)</u>	<u>100%</u>	<u>Inverbeira, Sociedad de Promoción de Empresas, S.A.</u>	<u>Holding company</u>
<u>CD Verre, S.A.</u>	<u>Bordeaux (France)</u>	<u>100%</u>	<u>Investverre, S.A.</u>	<u>Commercialisation</u>
<u>Vidrala Desarrollos, S.L.U.</u>	<u>Llodio (Alava, Spain)</u>	<u>100%</u>	<u>Vidrala, S.A.</u>	<u>Promotion and development of companies</u>
<u>Encirc Limited</u>	<u>Derrylin (Northern Ireland)</u>	<u>100%</u>	<u>Inverbeira, Sociedad de Promoción de Empresas, S.A.</u>	<u>Manufacture of glass containers, packaging and logistical services</u>
<u>Encirc Distribution Limited</u>	<u>Ballyconnell (Ireland)</u>	<u>100%</u>	<u>Encirc Limited</u>	<u>Logistical services</u>

2. Basis of Presentation

The accompanying consolidated annual accounts have been prepared on the basis of the accounting records of Vidrala, S.A. and of the consolidated companies. The consolidated annual accounts for 2016 have been prepared in accordance with International Financial Reporting Standards as adopted by the European Union (IFRS-EU), and other provisions of the financial information reporting framework applicable to the Group, to present fairly the consolidated equity and consolidated financial position of Vidrala, S.A. and subsidiaries at 31 December 2016, as well as the consolidated financial performance and changes in consolidated equity and cash flows for the year then ended.

(Continued)

VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

The Group adopted IFRS-EU on 1 January 2004 and applied IFRS 1, "First-time adoption of International Financial Reporting Standards".

The Parent's directors consider that the consolidated annual accounts for 2016, authorised for issue on 21 February 2017, will be approved without changes by the shareholders at their annual general meeting.

(a) Basis of preparation of the annual accounts

These consolidated annual accounts have been prepared on a going concern basis using the historical cost principle, with the exception of derivative financial instruments, which have been recognised at fair value.

(b) Comparative information

The accounting criteria used in preparing these consolidated annual accounts have been applied consistently for the two years presented.

(c) Relevant accounting estimates and relevant assumptions and judgements in the application of the accounting policies

Accounting estimates, judgements and assumptions sometimes have to be made to prepare the consolidated annual accounts in conformity with IFRS-EU. A summary of the items requiring a greater degree of judgement or complexity, or where the assumptions and estimates made are significant to the preparation of the consolidated annual accounts, is as follows:

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VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

(i) Relevant accounting estimates and assumptions

- Goodwill impairment:

The Group tests for impairment of goodwill on an annual basis. The calculation of the recoverable amount of a cash-generating unit to which goodwill has been allocated requires the use of estimates and the application of financial measurement criteria. The recoverable amount is the higher of fair value less costs to sell and value in use. The Group uses cash flow discounting methods to calculate these values. Cash flow discounting calculations are made considering that the activity of cash generating units has an infinite life and free cash flow projections are made based on financial projections approved by management. Cash flows beyond the budgeted period are extrapolated using estimated growth rates (see note 7). The flows take into consideration past experience and represent management's best estimate of future market performance. The key assumptions used to determine value in use include expected growth rates, the weighted average cost of capital and tax rates indicated in note 7. The estimates, including the methodology used, could have a significant impact on values and impairment.

- Useful lives of property, plant and equipment:

Group management determines the estimated useful lives and depreciation charges for its installations. These estimates are based on the historical and projected life cycles of the assets according to their characteristics, available technology and estimated replacement requirements. This could change as a result of technical innovations and initiatives adopted by the competition in response to pronounced cycles. Management will increase the depreciation charge when the useful lives are lower than the lives estimated previously or will depreciate or eliminate technically obsolete or non-strategic assets which are idle or sold.

- Valuation allowances for bad debts

Valuation allowances for bad debts require a high degree of judgement by management and a review of individual balances based on customers' credit ratings, market trends, and historical analysis of bad debts at an aggregated level. This judgement is put into practice through the application of procedurised methodologies developed by the Vidrala Group, mainly based on the detailed analysis of credit ratings and historical sales and payments. Additionally, control over collection solvency is complemented through credit insurance coverage (see note on risks).

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VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

- Income tax

The Group files income tax returns in numerous jurisdictions. Tax legislation applicable to certain group companies means that certain calculations have to be estimated.

Any differences between the final tax calculation and the amount initially recognised have an effect on the profit or loss for the period in question.

Group management estimates that any differences arising from the use of assumptions and judgements in estimating income tax for 2016 will be immaterial.

- Capitalised tax credits

The Group evaluates the recoverability of capitalised tax credits based on estimates of whether sufficient future taxable income will be available against which they can be offset.

(ii) Changes in accounting estimates

Although estimates are calculated by the Company's directors based on the best information available at 31 December 2016, future events may require changes to these estimates in subsequent years. Any effect on the consolidated annual accounts of adjustments to be made in subsequent years would be recognised prospectively.

(d) **Standards and interpretations not applied**

The standards effective as of 1 January 2014 have not given rise to changes in the Group's accounting policies. The IASB has issued new accounting standards (IFRS) and interpretations (IFRIC) which are due to become effective for accounting periods beginning on or after 1 January 2014. Details of the nature of the changes in accounting policy and a summary of Group management's assessment of the impact these new standards could have on the Group's financial statements are as follows:

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VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

IFRS 9 Financial instruments – issued October 2010 (pending adoption by the European Union)

This standard, which partially replaces IAS 39, simplifies the classification and measurement criteria for financial instruments, maintaining a mixed measurement model and establishing only two main financial asset categories: amortised cost and fair value. The classification criteria are based on the entity's business model and the characteristics of the financial asset's contractual cash flows.

The Group will assess the impact of this standard for the first year in which it becomes effective.

This standard is ready to be applied immediately, but is pending adoption by the EU.

Annual improvements to IFRSs project – 2010-2012 Cycle – issued December 2013

The annual improvements project introduces amendments or clarifications that affect a wide range of standards.

The Group will assess the impact of these improvements for the first year in which they become effective.

This standard is effective for periods beginning on or after 1 February 2015.

Annual improvements to IFRSs project – 2011-2013 Cycle – issued December 2013

The annual improvements project introduces amendments or clarifications that affect a wide range of standards.

The Group will assess the impact of these improvements for the first year in which they become effective.

This standard is effective for periods beginning on or after 1 January 2015.

VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

3. Significant Accounting Principles**(a) Subsidiaries**

Subsidiaries are entities over which the Company exercises control, either directly or indirectly through subsidiaries. The Company controls a subsidiary when it is exposed, or has rights, to variable returns from its involvement with the subsidiary and has the ability to affect those returns through its power over the subsidiary. The Company has power over a subsidiary when it has existing substantive rights that give it the ability to direct the relevant activities. The Company is exposed, or has rights, to variable returns from its involvement with the subsidiary when its returns from its involvement have the potential to vary as a result of the subsidiary's performance.

Information on subsidiaries forming the consolidated Group is included in note 1.

The income, expenses and cash flows of subsidiaries are included in the consolidated annual accounts from their acquisition date, which is the date on which the Group obtained effective control of the subsidiaries. Subsidiaries are no longer consolidated once control is lost.

Transactions and balances with Group companies and unrealised gains or losses have been eliminated upon consolidation. Nevertheless, unrealised losses have been considered as an indicator of impairment of the assets transferred.

The subsidiaries' accounting policies have been adapted to Group accounting policies, for like transactions and other events in similar circumstances.

The annual accounts or financial statements of the subsidiaries used in the consolidation process have been prepared as of the same date and for the same period as those of the Parent.

(b) Business combinations

The Group applies the acquisition method for business combinations.

The acquisition date is the date on which the Group obtains control of the acquiree.

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VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

The consideration transferred in a business combination is calculated as the sum of the acquisition-date fair values of the assets transferred, the liabilities incurred or assumed, the equity instruments issued and any consideration contingent on future events or compliance with certain conditions in exchange for control of the acquiree.

The consideration given excludes any payment that does not form part of the exchange for the acquired business. Acquisition costs are recognised as an expense when incurred.

The Group recognises the assets acquired and liabilities assumed at their acquisition-date fair value. Liabilities assumed include any contingent liabilities that represent present obligations arising from past events for which the fair value can be reliably measured.

(c) Property, plant and equipment

Initial recognition

Property, plant and equipment are recognised at cost or deemed cost, less accumulated depreciation and any accumulated impairment losses.

Spare parts for use in installations, equipment and machinery as replacements for similar parts with a warehouse cycle of more than one year are measured using the aforementioned criteria and depreciated over the same period as the related assets. Parts with a warehouse cycle of less than one year are recognised as inventories.

Moulds are considered property, plant and equipment as their period of use exceeds one year, and are depreciated according to the quantities they produce.

At 1 January 2004 the Group applied the exemption permitted by IFRS 1, First-time Adoption of International Financial Reporting Standards, relating to fair value or revaluation as deemed cost, for certain items of property, plant and equipment acquired prior to that date.

Depreciation

The Group determines the depreciation charge separately for each component of an item of property, plant and equipment with a cost that is significant in relation to the total cost of the asset and with a useful life that differs from the remainder of the asset.

(Continued)

VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

Property, plant and equipment are depreciated on a straight-line basis using the following estimated useful lives:

	<u>Estimated years of useful life</u>
Buildings	20 - 30
Technical installations and machinery	
Internal transport and fixed maintenance installations	6 - 10
General installations	10 - 30
Furnaces, installations and production machinery	8 - 16
Workshop machinery	8 - 14
Furniture	6 - 12
Other property, plant and equipment	8 - 12

The Group reviews residual values, useful lives and depreciation methods for property, plant and equipment at each financial year end. Changes to initially established criteria are accounted for as a change in accounting estimates.

Subsequent costs

Subsequent to initial recognition of the asset, only those costs incurred which will generate probable future profits and for which the amount may reliably be measured are capitalised. Costs of day-to-day servicing are recognised in profit or loss as incurred.

Impairment

The Group evaluates and determines impairment losses and reversals of impairment losses on property, plant and equipment in line with the criteria described in section (e).

(d) Intangible assets*(i) Goodwill*

Goodwill corresponds to the excess between the consideration paid plus the value assigned to non-controlling interests and the net amount of assets acquired and liabilities assumed in business combinations made by the Group.

(Continued)

VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

Goodwill is not amortised but is tested for impairment annually or more frequently where events or circumstances indicate that an asset may be impaired. Goodwill on business combinations is allocated to the cash-generating units (CGUs) or groups of CGUs which are expected to benefit from the synergies of the business combination and the criteria described in the note on impairment are applied. After initial recognition, goodwill is measured at cost less any accumulated impairment losses.

(ii) Internally generated intangible assets

Expenditure on research is recognised as an expense when it is incurred.

Costs associated with development activities relating to the design and testing of new and improved products are capitalised to the extent that:

- The Group has technical studies that demonstrate the feasibility of the production process.
- The Group has undertaken a commitment to complete production of the asset, to make it available for sale (or internal use).
- The asset will generate sufficient future economic benefits as, according to management's best estimates, a market exists that will absorb production or the internal use of the asset.
- The Group has sufficient technical and financial resources to complete development of the asset (or to use the asset internally) and has devised budget control and cost accounting systems that enable monitoring of budgetary costs, modifications and the expenditure actually attributable to the different projects.

Expenditure on activities for which costs attributable to the research phase are not clearly distinguishable from costs associated with the development stage of intangible assets are recognised in profit or loss.

VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

(iii) CO2 emission allowances

Emission allowances are recognised when the Group becomes entitled to such allowances and are measured at cost, less accumulated impairment losses. Allowances acquired free of charge or at a price substantially lower than fair value are carried at fair value, which generally coincides with the market value of the allowances at the beginning of the relevant calendar year. The excess between this value and, where applicable, the payment made for the allowance is credited to government grants under deferred income. Amounts recognised under government grants are taken to profit or loss in accordance with the emissions made as a percentage of total emissions forecast for the entire period for which they have been allocated, irrespective of whether the previously acquired allowances have been sold or impaired.

Expenses generated by the emission of greenhouse gases are recognised in line with the use of emission allowances allocated or acquired as these gases are emitted during the production process, with a credit to the corresponding provision.

Emission allowances recognised as intangible assets are not amortised but written off against the corresponding provision upon delivery to the authorities to cancel the obligations assumed. The Group derecognises emission allowances at weighted average cost.

(iv) Other intangible assets

Other intangible assets acquired by the Group are carried at cost, less any accumulated amortisation and impairment losses.

(v) Useful life and amortisation rates

Intangible assets with finite useful lives are amortised by allocating the depreciable amount of an asset on a systematic basis using the straight-line method over its useful life, which is estimated to be a maximum of ten years for computer software and, in the case of development expenses, the period over which profit is expected to be generated from the start of the commercial production of the product.

(Continued)

VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

The Group reviews the residual value, useful life and amortisation method for intangible assets at each financial year end. Changes to initially established criteria are accounted for as a change in accounting estimates.

(vi) Impairment

The Group evaluates and determines impairment losses and reversals of impairment losses on intangible assets in line with the criteria described in section (e).

(e) **Impairment losses of non-financial assets subject to amortisation or depreciation**

The Group tests non-financial assets subject to depreciation or amortisation for impairment with a view to verifying whether their carrying amount exceeds their recoverable amount. The recoverable amount of assets is the higher of their fair value less costs to sell and their value in use determined based on estimated future cash flows.

Negative differences resulting from comparison of the carrying amounts of the assets with their recoverable amount are recognised in profit or loss.

(f) **Leases**

• Lessee accounting

The Group has the right to use certain assets through lease contracts.

• Operating leases

Lease payments under operating leases, net of incentives received, are recognised as an expense on a straight-line basis over the lease term.

(g) **Financial instruments**

(i) Classification of financial instruments

Financial instruments are classified on initial recognition as a financial asset, a financial liability or an equity instrument in accordance with the economic substance of the contractual arrangement and the definitions of a financial asset, a financial liability and an equity instrument in IAS 32 "Financial Instruments: Presentation".

(Continued)

VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

Financial instruments are classified into the following categories: financial assets and financial liabilities at fair value through profit or loss, loans and receivables and financial liabilities at amortised cost. The Group classifies financial instruments into different categories based on the nature of the instruments and management's intentions on initial recognition.

(ii) Offsetting principles

A financial asset and a financial liability are offset only when the Group currently has the legally enforceable right to offset the recognised amounts and intends either to settle on a net basis or to realise the asset and settle the liability simultaneously.

(iii) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than those classified in other financial asset categories.

These assets are recognised initially at fair value, including transaction costs, and are subsequently measured at amortised cost using the effective interest method.

(iv) Impairment and uncollectibility of financial assets

The Group recognises impairment losses and defaults on loans and other receivables in an allowance account for financial assets. Recognition is based on ageing, monitoring, and third party data and reports on the economic circumstances of the debtors. When impairment and uncollectibility are considered irreversible as all avenues for collecting the debt, including the courts, have been exhausted, the carrying amount is written off with a charge to the allowance account. Impairment reversals are also recognised against the allowance account.

VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

- Impairment of financial assets carried at amortised cost

In the case of financial assets carried at amortised cost, the amount of the impairment loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate. The amount of an impairment loss is recognised in profit or loss and may be reversed in subsequent periods if the decrease can be objectively related to an event occurring after the impairment has been recognised. The loss can only be reversed to the limit of the amortised cost of the assets had the impairment loss not been recognised. The impairment loss is reversed against the allowance account.

(v) Financial liabilities at amortised cost

Financial liabilities, including trade and other payables, which are not classified at fair value through profit or loss, are initially recognised at fair value less any transaction costs that are directly attributable to the issue of the financial liability. After initial recognition, financial liabilities are measured at amortised cost using the effective interest method.

(vi) Derecognition of financial assets

Financial assets are derecognised when the contractual rights to the cash flows from the financial asset expire or have been transferred and the Group has transferred substantially all the risks and rewards of ownership.

On derecognition of a financial asset, the difference between the carrying amount and the sum of the consideration received, net of transaction costs, including any new asset obtained less any new liability assumed and any cumulative gain or loss deferred in other comprehensive income, is recognised in profit or loss.

If the Group retains substantially all the risks and rewards of ownership of a transferred financial asset, the consideration received is recognised as a liability. Transaction costs are recognised in profit or loss using the effective interest method.

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VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

(vii) Derecognition of financial liabilities

A financial liability is derecognised when the Group either discharges the liability by paying the creditor, or is legally released from primary responsibility for the liability either by process of law or by the creditor.

If there is an exchange of debt instruments between the Group and the lenders, and the conditions thereof are substantially different, the original financial liability is derecognised and the new financial liability is recognised. If the conditions are not substantially different, the financial liability is not derecognised from the balance sheet and any commission paid is recognised as an adjustment in the carrying amount of the liability. The amortised cost of the financial liability is determined applying the effective interest rate, which is the rate that equates the carrying amount of the financial liability at the audit date with the cash flows to be paid as per the new conditions. In this regard, the conditions of the contracts are considered to be substantially different when the present value of the cash flows of the new financial liability, including net commissions paid or received, is different by at least 10% of the present value of the recurring cash flows of the original financial liability, both updated to the effective interest rate of the latter (see note 15).

The Group has contracted reverse factoring facilities with various financial institutions to manage payments to suppliers. Trade payables settled under the management of financial institutions are recognised under trade and other payables only if the Group has transferred management of the payment to the financial institutions but retains primary responsibility for settling the debt with the trade creditors.

(h) Hedge accounting

Derivative financial instruments which qualify for hedge accounting are initially measured at fair value, plus any transaction costs that are directly attributable to the acquisition, or less any transaction costs directly attributable to the issue of the financial instruments.

(Continued)

VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

The Group has cash flow hedges.

At the inception of the hedge the Group formally designates and documents the hedging relationships and the objective and strategy for undertaking the hedges. Hedge accounting is only applicable when the hedge is expected to be highly effective at the inception of the hedge and in subsequent years in achieving offsetting changes in cash flows attributable to the hedged risk, throughout the period for which the hedge was designated (prospective analysis) and the actual effectiveness, which can be reliably measured, is within a range of 80%-125% (retrospective analysis).

For cash flow hedges of forecast transactions, the Group assesses whether these transactions are highly probable and if they present an exposure to variations in cash flows that could ultimately affect profit or loss.

The structure of hedges in the different cases is as follows:

Interest rate hedges

- Hedged item: variable-rate financing received.
- Hedging instrument: the Group manages interest rate risks in cash flows through derivative instrument swaps or interest rate caps. These derivative hedging instruments convert variable interest rates on borrowings to fixed interest rates (swaps) or limit the cost of variable rate borrowings (caps). In some cases, these are forward start instruments, which means that the flows of the hedged item are only hedged from the time the hedging instrument comes into effect.
- Hedged risk: changes in the cash flows of the hedged item (interest payments) in the event of changes in benchmark interest rates.

Energy price swaps

- Hedged item: variable price of energy referenced to certain fuels.
- Hedging instrument: derivative instrument swaps or purchase option caps through which the Group converts the variable purchase cost of certain fuels to a fixed cost (swaps) or limits the variable cost to a maximum price (caps).

(Continued)

VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

- Hedged risk: changes in the cash flows of the hedged item in the event of changes in benchmark fuel prices.

The Group recognises the portion of the gain or loss on the measurement at fair value of a hedging instrument that is determined to be an effective hedge in other comprehensive income. The ineffective portion and the specific component of the gain or loss or cash flows on the hedging instrument, excluding the measurement of the hedge effectiveness, are recognised with a debit or credit to finance costs or finance income.

The Group recognises in profit or loss amounts accounted for in other comprehensive income in the same year or years during which the forecast hedged transaction affects profit or loss and in the same caption of the consolidated income statement.

(i) Parent own shares

The Group's acquisition of equity instruments of the Parent is recognised separately at cost of acquisition in the consolidated balance sheet as a reduction in equity, regardless of the reason for the purchase. No gain or loss is recognised on transactions involving own equity instruments.

Transaction costs related to own equity instruments are accounted for as a reduction in equity, net of any tax effect.

(j) Distribution to shareholders

Dividends are recognised as a reduction in equity when approved by the shareholders.

(k) Inventories

Inventories are measured at the lower of acquisition or production cost and net realisable value.

The purchase price includes the amount invoiced by the seller, after deduction of any discounts, rebates or other similar items, other costs directly attributable to the acquisition and indirect taxes not recoverable from Spanish taxation authorities.

(Continued)

VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

The Group uses the following measurement criteria to determine the cost of each type of inventory:

- a. Raw materials: at weighted average cost.
- b. Finished goods and work in progress: at actual cost, which includes raw materials, direct labour and direct and indirect manufacturing overheads (based on normal operating capacity).
- c. Auxiliary and production materials: at weighted average cost.

The cost of inventories is adjusted against profit or loss when cost exceeds the net realisable value.

The previously recognised write-down is reversed against profit and loss when the circumstances that previously caused inventories to be written down no longer exist or when there is clear evidence of an increase in net realisable value because of changed economic circumstances. The reversal of the write-down is limited to the lower of the cost and the revised net realisable value of the inventories. Reductions and reversals of the value of inventories are classified under change in inventories of finished goods and work in progress and raw materials and other supplies used in the consolidated income statement.

(l) Cash and cash equivalents

Cash and cash equivalents include cash on hand and demand deposits in financial institutions.

The Group recognises interest received as cash flows from investing activities and interest paid as cash flows used in operating activities. Dividends received are classified under investing activities and dividends paid under financing activities.

(m) Government grants

Government grants are recognised in the balance sheet when there is reasonable assurance that they will be received and that the Group will comply with the conditions attached.

(Continued)

VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

(i) Capital grants

Capital grants awarded as monetary assets are recognised under deferred income in the consolidated balance sheet and allocated to other income in line with the amortisation or depreciation of the assets for which the grants have been received.

The accounting treatment of grants related to emission allowances is described in section (d).

(ii) Operating grants

Operating grants are recognised under other income.

(iii) Interest-rate grants

Financial liabilities comprising implicit assistance in the form of below market interest rates are initially recognised at fair value. The difference between this value, adjusted where necessary for the issue costs of the financial liability and the amount received, is recognised as a government grant based on the nature of the grant awarded.

(n) Employee benefits*(i) Defined benefit plans*

The Group includes plans financed through the payment of insurance premiums under defined benefit plans where a legal or constructive obligation exists to directly pay employees the committed benefits when they become payable or to pay further amounts in the event that the insurance company does not pay the employee benefits relating to employee service in the current and prior periods.

Defined benefit liabilities recognised in the consolidated statement of financial position reflect the present value of defined benefit obligations at the reporting date, minus the fair value at that date of plan assets.

Income or expense related to defined benefit plans is recognised as employee benefits expense and is the sum of the net current service cost and the net interest cost of the net defined benefit asset or liability. Remeasurements of the net defined benefit asset or liability are recognised in other comprehensive income, comprising actuarial gains and losses, return on plan assets and any change in the effect of the asset ceiling, excluding amounts included in net interest on the net defined benefit liability or asset.

(Continued)

VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

The present value of defined benefit obligations is calculated annually by independent actuaries using the Projected Unit Credit Method. The discount rate of the net defined benefit asset or liability is calculated based on the yield on high quality corporate bonds of a currency and term consistent with the currency and term of the post-employment benefit obligations. In determining the appropriate discount rate, management considers the interest rates of corporate bonds in the respective currency with at least AA rating, with extrapolated maturities corresponding to the expected duration of the defined benefit obligation. The underlying bonds are further reviewed for quality, and those having excessive credit spreads are removed from the population of bonds on which the discount rate is based, on the basis that they do not represent high-quality bonds. The mortality rate is based on publicly available mortality tables for the specific country. Future salary increases and pension increases are based on expected future inflation rates for the respective country.

(ii) Defined contributions

The Group has pension plan commitments. Contributions are made to externally managed funds and are classified as defined contributions.

The Group recognises the contributions payable to a defined contribution plan in exchange for a service when an employee has rendered service to the Group. The contributions payable are recognised as an expense for employee remuneration, and as a liability after deducting any contribution already paid.

(Continued)

VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

(iii) Other commitments with employees

“Provisions” in the consolidated balance sheet include a provision for commitments assumed with the employees of one of the Group’s companies in accordance with legal requirements in the country of origin. According to this legislation, companies are obliged to provide for or contribute certain amounts to an externally managed pension plan, calculated on the basis of employees’ remuneration, which are redeemed when an employee’s working relationship with the company terminates.

(iv) Termination benefits

Termination benefits are recognised at the earlier of when the Group can no longer withdraw the offer of those benefits and when the Group recognises costs for a restructuring that involves the payment of termination benefits.

For termination benefits payable as a result of an employee’s decision to accept an offer, the time when the Group can no longer withdraw the offer of termination benefits is the earlier of when the employee accepts the offer and when a restriction on the Group’s ability to withdraw the offer takes effect

For termination benefits payable as a result of involuntary redundancy, the Group can no longer withdraw the offer when: it has communicated the termination plan to the affected employees or their trade union representatives; the actions required to complete the plan indicate that it is unlikely that significant changes will be made to the plan; the plan identifies the number of employees whose employment is to be terminated, their job classifications or functions and their locations and the expected completion date; the plan establishes the termination benefits that employees will receive in sufficient detail that employees can determine the type and amount of benefits they will receive when their employment is terminated.

(v) Short-term employee benefits

The Group recognises the expected cost of profit-sharing and bonus plans when it has a present legal or constructive obligation to make such payments as a result of past events and a reliable estimate of the obligation can be made.

VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

(o) Provisions

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event; it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation; and a reliable estimate can be made of the amount of the obligation.

The amount recognised as a provision is the best estimate of the expenditure required to settle the present obligation at the end of the reporting period, taking into account all risks and uncertainties surrounding the amount to be recognised as a provision and, where the time value of money is material, the financial effect of discounting provided that the expenditure to be made each period can be reliably estimated.

If it is not probable that an outflow of resources embodying economic resources will be required to settle an obligation, the provision is reversed. The provision is reversed against the caption of the consolidated income statement in which the related expense was recognised, and any surplus is accounted for in other income.

(i) Provision for emission allowances

Provision is systematically made under provisions for emission allowances for expenses related to the emission of greenhouse gases at the average price of the allowances expected to be received, and is cancelled through the conveyance of the corresponding allowances, including those purchased to cover the shortfall in allowances received free of charge.

(ii) Provision for defined benefit plans

Income or expense related to defined benefit plans is recognised as employee benefits expense and is the sum of the net current service cost and the net interest cost of the net defined benefit asset or liability. Remeasurements of the net defined benefit asset or liability are recognised in other comprehensive income, comprising actuarial gains and losses, return on plan assets and any change in the effect of the asset ceiling, excluding amounts included in net interest on the net defined benefit liability or asset.

(Continued)

VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

(p) Revenue recognition

Revenue from the sale of goods or services is measured at the fair value of the consideration received or receivable. Volume rebates, prompt payment and any other discounts are recognised as a reduction in the consideration. Revenue is presented net of value added taxes and any other amount or tax which, in substance, corresponds to amounts received on behalf of third parties.

Discounts granted to customers are recognised as a reduction in sales revenue when it is probable that the discount conditions will be met.

Revenue is only recognised when there is evidence of an agreement between the parties, the goods have been delivered or the services rendered, amounts are agreed and collection is reasonably assured

(q) Income tax

The income tax expense or tax income for the year comprises current tax and deferred.

Current tax is the amount of income taxes payable or recoverable in respect of the consolidated taxable profit or tax loss for the period.

Current tax assets or liabilities are measured at the amount expected to be paid to or recovered from the taxation authorities, using the tax rates and tax laws that have been enacted or substantially enacted at the reporting date.

(Continued)

VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

Deferred tax liabilities are the amounts of income taxes payable in future periods in respect of taxable temporary differences, whereas deferred tax assets are the amounts of income taxes recoverable in future periods in respect of deductible temporary differences, the carryforward of unused tax losses and the carryforward of unused tax credits. Temporary differences are considered to be the difference between the carrying amount of the assets and liabilities and their tax base.

Vidrala, S.A. together with Vidrala Desarrollos, S.A., Aiala Vidrio, S.A. and Inverbeira, Sociedad de Promoción de Empresas, S.A. have filed consolidated tax returns since 1 January 2013.

(i) Recognition of deferred tax liabilities

The Group recognises deferred tax liabilities in all cases.

(ii) Recognition of deferred tax assets

The Group recognises deferred tax assets, provided that it is probable that sufficient taxable income will be available against which they can be utilised.

Tax planning opportunities are only considered when assessing the recoverability of deferred tax assets if the Group intends to use these opportunities or it is probable that they will be utilised.

A deferred tax asset is recognised for unused tax losses, tax credits and deductions to the extent that it is probable that future taxable profits will be available against which they can be utilised. Certain deductions for investments in property, plant and equipment or business acquisitions are applied in line with the depreciation period of the assets or business plan of the acquired activities which generated the tax credits with a credit to deferred income (see note 13).

(iii) Measurement

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the years when the asset is realised or the liability is settled, based on tax rates and tax laws that have been enacted or substantively enacted. The tax consequences that would follow from the manner in which the Group expects to recover or settle the carrying amount of its assets or liabilities are also reflected in the measurement of deferred tax assets and liabilities.

(Continued)

VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

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.

Deferred tax assets which do not meet the above conditions are not recognised in the consolidated balance sheet. At the reporting date the Group assesses whether deferred tax assets which were previously not recognised meet the conditions for recognition.

(iv) Offsetting and classification

The Group only offsets current tax assets and liabilities if it has a legally enforceable right to offset the recognised amounts and intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously.

The Group only offsets deferred tax assets and liabilities if it has a legally enforceable right, when they relate to income taxes levied by the same taxation authority and on the same taxable entity and when the taxation authority permits the Group to make or receive a single net payment, or to recover the assets and settle the liabilities simultaneously in each future year in which significant amounts of deferred tax assets or liabilities are expected to be settled or recovered.

Deferred tax assets and liabilities are recognised in the consolidated balance sheet under non-current assets or liabilities, irrespective of the date of realisation or settlement.

(r) Segment reporting

An operating segment is a component of the Group that engages in business activities from which it may earn revenues and incur expenses, whose operating results are regularly reviewed by the Group's chief operating decision maker to make decisions about resources to be allocated to the segment and assess its performance, and for which discrete financial information is available.

(s) Environmental issues

The Group takes measures to prevent, reduce or repair the damage caused to the environment by its activities.

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VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

Expenses derived from environmental activities are recognised as other expenses in the period in which they are incurred. Nonetheless, the Group recognises environmental provisions and, where applicable, reimbursement rights by applying the general criteria described in the note on provisions.

Assets acquired by the Group to minimise the environmental impact of its activity and protect and improve the environment, including the reduction or elimination of future pollution caused by the Group's operations, are recognised in the consolidated balance sheet in line with the recognition, measurement and disclosure criteria detailed in the note on property, plant and equipment.

(t) Foreign currency transactions and balances

The figures disclosed in the consolidated annual accounts are expressed in thousands of Euros, the Parent's functional and presentation currency.

Transactions in foreign currency are translated to the functional currency at the foreign exchange rate prevailing at the date of the transaction.

Monetary assets and liabilities denominated in foreign currencies have been translated into Euros at the closing rate, while non-monetary assets and liabilities measured at historical cost have been translated at the exchange rate prevailing at the transaction date.

In the consolidated statement of cash flows, cash flows from foreign currency transactions have been translated into Euros at the exchange rates prevailing at the dates the cash flows occur.

Exchange gains and losses arising on the settlement of foreign currency transactions and the translation into Euros of monetary assets and liabilities denominated in foreign currencies are recognised in profit or loss.

Exchange gains or losses on monetary financial assets or financial liabilities denominated in foreign currencies are also recognised in profit or loss.

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VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

4. Segment reporting

As described below, the Group is organised internally into operating segments, defined as strategic business units. The different strategic business units have similar products and services (the manufacture and sale of glass containers), which are managed separately and aggregated by geographical market as they require different market strategies. The bottling and logistics services provided in the United Kingdom (note 1) do not entail a separate segment in that they are considered a complementary service to the manufacture and sale of glass containers.

The information used at board and management level and for reporting to third parties is broken down by operating segment.

In 2016, as part of the process of integrating the subsidiary Encirc (note 5), the Group redefined its operating segments as follows:

- Continental Europe
- United Kingdom and Ireland

Segment performance is measured based on the pre-tax profit generated by each segment. The profit generated by each segment is used as a measure of its performance because the Group considers that this is the most relevant information in the assessment of the profits generated by specific segments in relation to other groups which operate in these businesses.

Details of Group sales and services assigned to each segment by geographical location of production companies are as follows:

	<u>Thousands of Euros</u>	
	<u>2016</u>	<u>2015</u>
Continental Europe	459,781	479,502
United Kingdom & Ireland	<u>313,789</u>	<u>323,863</u>
	<u>773,570</u>	<u>803,365</u>

The table above shows details of sales and services rendered to external customers. Consequently, there are no transactions between geographical segments.

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VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

Non-current assets a 31 December are as follows:

	Thousands of Euros	
	2016	2015
Continental Europe	419,329	421,170
United Kingdom & Ireland	<u>289,059</u>	<u>345,240</u>
	<u>708,388</u>	<u>766,410</u>

Profit before income tax from continuing operations and profit for the year after income tax by geographical location of manufacturing companies are as follows:

Area/location	Thousands of Euros			
	2016		2015	
	Profit before income tax from continuing operations	Profit after income tax	Profit before income tax from continuing operations	Profit after income tax
Continental Europe	51,508	43,122	47,847	41,602
United Kingdom & Ireland	<u>32,734</u>	<u>24,549</u>	<u>27,776</u>	<u>19,258</u>
	<u>84,242</u>	<u>67,671</u>	<u>75,623</u>	<u>60,860</u>

Details of finance income and costs by geographical location of manufacturing companies are as follows:

Area/location	Thousands of Euros			
	2016		2015	
	Costs	Income	Costs	Income
Continental Europe	9,632	979	11,365	1,650
United Kingdom & Ireland	<u>144</u>	-	<u>949</u>	-
	<u>9,776</u>	<u>979</u>	<u>12,314</u>	<u>1,650</u>

Finance costs for the Continental Europe segment include Euros 5,469 thousand (Euros 7,283 thousand in 2015) in financing obtained for the acquisition of Encirc Limited (see note 15).

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VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

Details of impairment and reversals of impairment relating to receivables and inventory and changes in provisions by geographical location of manufacturing companies are as follows:

Thousands of Euros				
Area/location	2016		2015	
	Continental Europe	UK & Ireland	Continental Europe	UK & Ireland
Impairment (reversal) of receivables	409	-	(207)	729
Impairment of inventory	1,684	(2,063)	(3,517)	-
Changes in provisions	<u>580</u>	<u>(888)</u>	<u>(1,951)</u>	<u>-</u>
	<u>2,673</u>	<u>(2,951)</u>	<u>(5,675)</u>	<u>729</u>

Information on the main captions in the consolidated annual accounts by geographical location of production assets is as follows:

Thousands of Euros						
Area/location	2016			2015		
	Assets	Liabilities	Investments made	Assets	Liabilities	Investments made
Continental Europe	550,912	135,671	30,407	574,573	167,469	41,154
United Kingdom & Ireland	<u>446,330</u>	<u>67,359</u>	<u>17,193</u>	<u>524,537</u>	<u>89,669</u>	<u>18,346</u>
	<u>997,242</u>	<u>203,030</u>	<u>47,600</u>	<u>1,099,110</u>	<u>257,138</u>	<u>59,500</u>

Segment assets mainly include property, plant and equipment, intangible assets, inventories, accounts receivable and operating cash flow. Deferred tax assets and goodwill are not included.

Segment liabilities comprise non-current and operating liabilities and exclude deferred tax liabilities and borrowings.

Investments for 2016 and 2015 comprise additions of property, plant and equipment (see note 6) and intangible assets (see note 6) and do not reflect the value of emission allowances allocated for the year (see note 6).

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VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

The sum of impairment losses and amortisation and depreciation by segments for 2016 and 2015 is as follows:

Area/location	Thousands of Euros			
	Depreciation/amortisation			
	2016		2015	
	Property, plant and equipment	Intangible assets	Property, plant and equipment	Intangible assets
Continental Europe	45,884	1,243	42,056	1,564
United Kingdom & Ireland	<u>29,302</u>	<u>-</u>	<u>31,352</u>	<u>-</u>
	<u>75,186</u>	<u>1,243</u>	<u>73,408</u>	<u>1,564</u>

5. Business combinations

On 14 January 2015 the Group acquired 100% of the share capital of Encirc Limited through its subsidiary Inverbeira Sociedad de Promoción de Empresas, S.A. Encirc Limited is registered in Northern Ireland (UK) and its principal activity is the manufacture of glass containers for food and beverage products, the bottling of beverages and the rendering of logistics services for the packaging of food products mainly targeted at the UK and Ireland markets. The main reason for this business combination was to enhance the positioning of the Vidrala Group in the European glass container market and to diversify towards markets considered to be strategic.

The acquired business generated revenue and consolidated profit before tax of Euros 323,863 thousand and Euros 27,776 thousand, respectively, between the acquisition date and the date of the 2015 financial statements.

If the acquisition had been made on 1 January 2015, the Group's revenue and consolidated profit for the year ended 31 December 2015 would not have changed significantly compared to the aforementioned amounts.

The Company valued the acquired business at Euros 408.6 million (enterprise value). Additionally, adjustments were made in accordance with the agreed 'locked box' mechanism that raised the amount of cash paid to Euros 415.1 million and made it possible to fully assume the acquiree's existing cash at the payment date, which amounted to Euros 11.9 million. Consequently, the net cash outflow for the acquisition came to Euros 403.2 million.

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VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

The amounts recognised in 2015 by significant class at the date of acquisition of the assets, liabilities and contingent liabilities are as follows:

	<u>Fair value</u>
Property, plant and equipment	317,027
Deferred tax assets	10,964
Other current assets	1,397
Inventories	81,072
Trade and other receivables	51,435
Cash and cash equivalents of the acquiree	<u>11,885</u>
	473,780
 Total assets	
Trade and other payables	53,715
Provisions	1,299
Deferred tax liabilities	<u>3,690</u>
 Total liabilities and contingent liabilities	58,704
 Total net assets acquired	<u>415,076</u>
 Cash paid	415,076
Cash and cash equivalents of the acquiree	<u>(11,885)</u>
 Cash outflow for the acquisition	<u>403,191</u>

The above amount, which was fully paid through new financing obtained for the acquisition (see note 15), comprised the price of the assets and the assumption of all debt (payable by the acquiree exclusively to its former shareholder).

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VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

6. Property, Plant and Equipment

Details of property, plant and equipment and movement during 2016 and 2015 are as follows:

	Thousands of Euros					Balances at 31.12.2016
	Balances at 31.12.2015	Additions	Disposals	Translation differences	Transfers	
2016						
<u>Cost</u>						
Land and buildings	311,488	1,366	(34)	(15,528)	625	297,917
Technical installations and machinery	743,430	29,983	(1,440)	(37,753)	8,225	742,445
Moulds	76,818	10,723	(504)	(3,174)	-	83,863
Furniture	9,427	2,283	(4)	(815)	603	11,494
Other property, plant and equipment	3,547	9	-	-	26	3,582
Work in progress	29,750	15,542	-	(498)	(9,405)	35,389
	<u>1,174,460</u>	<u>59,906</u>	<u>(1,982)</u>	<u>(57,768)</u>	<u>74</u>	<u>1,174,690</u>
<u>Depreciation</u>						
Land and buildings	(81,549)	(7,000)	4	947	-	(87,598)
Technical installations and machinery	(372,689)	(55,878)	1,455	9,720	-	(417,392)
Moulds	(46,790)	(10,459)	-	1,442	-	(55,807)
Furniture	(8,552)	(2,318)	1	80	-	(10,789)
Other property, plant and equipment	(2,980)	(19)	-	-	-	(2,999)
	<u>(512,560)</u>	<u>(75,674)</u>	<u>1,460</u>	<u>12,189</u>	<u>-</u>	<u>(574,585)</u>
<u>Impairment</u>						
Moulds	(5,262)	(2,116)	-	-	-	(7,378)
	<u>(5,262)</u>	<u>(2,116)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(7,378)</u>
<u>Carrying amount</u>	<u>656,638</u>					<u>592,727</u>

(Continued)

VIDRALA, S.A. AND SUBSIDIARIES
Notes to the Consolidated Annual Accounts

	Thousands of Euros						
	Balances at 31.12.2014	Additions consolidated group	Additions	Disposals	Translation differences	Transfers	
2015							
Cost							
Land and buildings	198,982	105,636	200	(306)	6,833	143	311,488
Technical installations and machinery	504,864	199,959	39,479	(18,300)	15,818	1,610	743,430
Moulds	55,202	10,749	10,072	-	795	-	76,818
Furniture	7,260	683	1,260	(2)	45	181	9,427
Other property, plant and equipment	3,541	-	3	-	-	3	3,547
Work in progress	17,792	-	13,694	-	-	(1,736)	29,750
	<u>787,641</u>	<u>317,027</u>	<u>64,708</u>	<u>(18,608)</u>	<u>23,491</u>	<u>201</u>	<u>1,174,460</u>
Depreciation							
Land and buildings	(74,808)	-	(6,594)	4	(151)	-	(81,549)
Technical installations and machinery	(334,944)	-	(54,944)	18,379	(1,180)	-	(372,689)
Moulds	(37,145)	-	(9,499)	-	(146)	-	(46,790)
Furniture	(6,276)	-	(2,268)	2	(10)	-	(8,552)
Other property, plant and equipment	(2,953)	-	(27)	-	-	-	(2,980)
	<u>(456,126)</u>	<u>-</u>	<u>(73,332)</u>	<u>18,385</u>	<u>(1,487)</u>	<u>-</u>	<u>(512,560)</u>
Impairment							
Moulds	(5,609)	-	(725)	1,072	-	-	(5,262)
Carrying amount	<u>325,906</u>						<u>656,638</u>

(a) Government grants received

Deferred income in the consolidated balance sheet includes government grants received for investments made by Group companies in property, plant and equipment. Income pending recognition from these grants amounts to Euros 20,333 thousand at 31 December 2016 (Euros 22,385 thousand at 31 December 2015) (see note 14).

(b) Commitments

Commitments for the acquisition of property, plant and equipment are as follows:

	Thousands of Euros	
	2016	2015
Technical installations and machinery	<u>33,965</u>	<u>18,583</u>

(c) Insurance

The Group has taken out insurance policies to cover the risk of damage to its property, plant and equipment. The coverage of these policies is considered sufficient.

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VIDRALA, S.A. AND SUBSIDIARIES
Notes to the Consolidated Annual Accounts

(d) Fully depreciated assets

At 31 December 2016 the restated cost of fully depreciated property, plant and equipment in use amounts to Euros 182 million (Euros 159 million at 31 December 2015).

7. Intangible Assets

Details of intangible assets and movement during 2016 and 2015 are as follows:

	Thousands of Euros					
	R&D expenditure	Goodwill	Emission allowances	Computer software	Work in progress	Total
2016						
Cost						
Balances at 31 December 2015	2,453	59,233	2,526	11,555	1,661	77,428
Additions	116	-	6,437	4,048	-	10,601
Transfers	401	-	-	204	(679)	(74)
Disposals	-	-	(3,434)	-	(623)	(4,057)
Translation differences	-	-	(35)	(96)	-	(131)
Balances at 31 December 2016	<u>2,970</u>	<u>59,233</u>	<u>5,494</u>	<u>15,711</u>	<u>359</u>	<u>83,767</u>
Amortisation						
Balances at 31 December 2015	(1,618)	-	-	(9,564)	-	(11,182)
Additions	(321)	-	-	(1,021)	-	(1,342)
Disposals	-	-	-	-	-	-
Balances at 31 December 2015	<u>(1,939)</u>	<u>-</u>	<u>-</u>	<u>(10,585)</u>	<u>-</u>	<u>(12,524)</u>
Carrying amount						
At 31 December 2015	<u>835</u>	<u>59,233</u>	<u>2,526</u>	<u>1,991</u>	<u>1,661</u>	<u>66,246</u>
At 31 December 2016	<u>1,031</u>	<u>59,233</u>	<u>5,494</u>	<u>5,126</u>	<u>359</u>	<u>71,243</u>
	Thousands of Euros					
	R&D expenditure	Goodwill	Emission allowances	Computer software	Work in progress	Total
2015						
Cost						
Balances at 31 December 2014	2,425	59,233	3,231	11,722	1,104	77,715
Additions	2	-	3,129	197	430	3,758
Transfers	26	-	-	(364)	137	(201)
Disposals	-	-	(3,834)	-	(10)	(3,844)
Balances at 31 December 2015	<u>2,453</u>	<u>59,233</u>	<u>2,526</u>	<u>11,555</u>	<u>1,661</u>	<u>77,428</u>
Amortisation						
Balances at 31 December 2014	(1,283)	-	-	(8,169)	-	(9,452)
Additions	(335)	-	-	(1,395)	-	(1,730)
Disposals	-	-	-	-	-	-
Balances at 31 December 2015	<u>(1,618)</u>	<u>-</u>	<u>-</u>	<u>(9,564)</u>	<u>-</u>	<u>(11,182)</u>
Carrying amount						
At 31 December 2014	<u>1,142</u>	<u>59,233</u>	<u>3,231</u>	<u>3,552</u>	<u>1,104</u>	<u>68,263</u>
Balance at 31 December 2015	<u>835</u>	<u>59,233</u>	<u>2,526</u>	<u>1,991</u>	<u>1,661</u>	<u>66,246</u>

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VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

(a) Emission allowances

In 2016 Euros 1,130 thousand (Euros 3,955 thousand in 2015) has been paid to public entities with a charge to the provision for emission allowances (see note 19).

The cost of emission allowances for 2016, which has been recorded against the corresponding provision (see note 19), amounted to Euros 3,956 thousand and mainly consists of the estimated surrender of emission allowances for 2016 of 493,265 tonnes (487,614 tonnes in 2015).

Movement in the number of allowances in 2016 and 2015 is as follows:

	<u>Free of charge</u>
Balance at 31 December 2014	<u>706,300</u>
Additions	340,336
Purchases	150,000
Deliveries	<u>(491,347)</u>
Balance at 31 December 2015	<u>705,289</u>
Additions	334,074
Purchases	150,000
Deliveries	<u>(488,777)</u>
Balance at 31 December 2016	<u>700,586</u>

(b) Impairment and allocation of goodwill to CGUs

For impairment testing purposes, goodwill has been allocated to the Group's cash-generating units (CGUs) based on the production unit that generated the cash, as follows:

<u>Cash Generating Unit</u>	<u>Country</u>	<u>Thousands of Euros</u>	
		<u>2016</u>	<u>2015</u>
Gallo Vidro	Portugal	20,799	20,799
Castellar Vidrio	Spain	26,155	26,155
Vidrala Italia	Italy	12,279	12,279

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VIDRALA, S.A. AND SUBSIDIARIES

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The recoverable amount of a CGU is determined based on value in use calculations using the discounted cash flow method. These calculations are based on cash flow projections for a five-year period from the financial budgets approved by management. Cash flows beyond this period are extrapolated using the estimated growth rates indicated below. The growth rate does not exceed the long-term average growth rate for the business in which the CGU operates.

The after-tax discount rates used at 31 December 2016 and 2015 were 8.52% for Gallo Vidro CGU, 8.47% for Castellar Vidrio CGU and 8.81% for Vidrala Italia CGU, and the growth rate was 1.5% per annum for all CGUs.

The key assumptions used were sales and gross margin.

The Group determines budgeted gross margins based on past experience, forecast market performance and production costs. The weighted average growth rates are consistent with the forecasts included in industry reports. The discount rates used are pre-tax values and reflect specific risks related to the relevant segments.

The average projected increase in sales and gross margin is 1.8% and 0.7%, respectively.

Sensitivity analysis

The Group has performed a sensitivity analysis on the main key assumptions, considering variations in these based on differences between the estimations made in the prior year and actual figures.

This analysis shows that an increase or decrease in sales and gross margin in each of the periods considered for the purposes of calculating the valuation, including terminal value, entails an average increase or decrease in the valuation of 7.5% or 5.3%, respectively.

This analysis reflects no impairment in any of the aforementioned CGUs.

Based on the recoverable amounts resulting from the analysis carried out, goodwill is not impaired at 31 December 2016 and 2015. There are deemed to be no reasonably possible changes in the key assumptions which would result in the carrying amount of the CGU exceeding its recoverable amount, thus giving rise to impairment.

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VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

8. Derivative Financial Instruments

Details of derivative financial instruments are as follows:

	Thousands of Euros			
	2016		2015	
	Assets	Liabilities	Assets	Liabilities
Hedging derivatives				
Interest rate swaps	-	5,313	-	3,029
Inflation swaps	72	-	-	-
Foreign currency options	195	-	-	-
Energy price options	<u>6,766</u>	<u>-</u>	<u>1,556</u>	<u>9,008</u>
Total (note 13)	<u>7,033</u>	<u>5,313</u>	<u>1,556</u>	<u>12,037</u>

These financial instruments are classified in accordance with categories established in IFRS 13 using the valuation method, input level 2: unquoted prices obtained from observable markets.

Swaps and options

The Group uses swaps and options on interest rates, inflation, foreign currencies and energy prices to manage its exposure to fluctuations in these variables.

The fair values of these instruments are determined by direct reference to observable market interest rate curves at the measurement date.

The Group applies hedge accounting to these swap and option contracts.

Interest rate hedging instruments contracted in 2015 and 2016 have an accumulated nominal of Euros 405,000 thousand at 31 December 2016 and 2015. Under these contracts, effective until 2022, the Group will pay a fixed interest rate of between 0.1% and 0.67% (between 0.1% and 0.25% in 2015).

Currency hedging instruments contracted in 2016 have an accumulated nominal of GBP 20,000 thousand at 31 December 2016. Under these contracts, effective until 2017, the Group will receive a fixed rate of between Euros 0.815 and 0.889 per GBP.

Inflation hedging instruments contracted in 2016 have an accumulated nominal at 31 December 2016 of Euros 18,500 thousand for each of the four years hedged up to 2019. Under these contracts, effective until 2019, the Group guarantees a maximum increase in certain costs relating to salaries of between 0.85% and 0.955%.

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Energy price hedging instruments have an accumulated nominal of Euros 51,200 thousand at 31 December 2016. As a result of these contracts, effective until 2019, the Group estimates that it has hedged approximately 50% of its expected exposure to fluctuations in energy markets over the aforementioned period.

Total cash flow hedges recognised in equity and taken to other comprehensive income under finance costs, are as follows:

	Thousands of Euros Income/(Expenses)	
	2016	2015
Other comprehensive income	10,324	(11,204)
Reclassification to finance costs	<u>1,889</u>	<u>1,451</u>
	<u>12,213</u>	<u>(9,753)</u>

The classification of cash flow hedges by reporting periods in which the cash flows are expected to occur, which coincides with those expected to impact the consolidated income statement, is as follows:

	Thousands of Euros							
			2016					
	Carrying amount	Expected cash flows	Occurrence of cash flows					
		2017	2018	2019	2020	2021	2022	
Interest rate swaps	<u>(5,313)</u>	<u>(5,397)</u>	<u>(1,352)</u>	<u>(1,075)</u>	<u>(1,370)</u>	<u>(781)</u>	<u>(481)</u>	<u>(338)</u>
Foreign currency swaps	<u>195</u>	<u>195</u>	<u>195</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Inflation swaps	<u>73</u>	<u>73</u>	<u>73</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Energy price options	<u>6,766</u>	<u>6,766</u>	<u>2,583</u>	<u>3,444</u>	<u>739</u>	<u>-</u>	<u>-</u>	<u>-</u>

	Thousands of Euros							
			2015					
	Carrying amount	Expected cash flows	Occurrence of cash flows					
		2016	2017	2018	2019	2020	2021	
Interest rate swaps	<u>(3,029)</u>	<u>(3,102)</u>	<u>(978)</u>	<u>(948)</u>	<u>(373)</u>	<u>(643)</u>	<u>(83)</u>	<u>(77)</u>
Energy price options	<u>(7,452)</u>	<u>(7,452)</u>	<u>(5,421)</u>	<u>(2,031)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>

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Notes to the Consolidated Annual Accounts

9. Income Tax

Details of deferred tax assets and liabilities by type of asset and liability are as follows:

Deferred tax liabilities	Thousands of Euros					Total
	Goodwill	Property, plant and equipment	Depreciation and amortisation	Financial assets	Other	
At 31 December 2014	19,492	13,793	1,642	12	4,131	39,070
Debit (credit) to income statement	1,132	4,916	-	-	(1,930)	4,118
Additions consolidated group	-	3,690	-	-	-	3,690
Translation differences	-	524	-	-	-	524
At 31 December 2015	20,624	22,923	1,642	12	2,201	47,402
Debit (credit) to income statement	1,140	2,442	(2,956)	-	(3,460)	(2,834)
Debit (credit) to other comprehensive income	-	-	-	1,701	-	1,701
Translation differences	-	-	-	-	1,597	1,597
At 31 December 2016	21,764	25,365	(1,314)	1,713	338	47,866

Deferred tax assets	Thousands of Euros					Total
	Tax loss carryforwards	Provisions for personnel	Rights to tax deductions and credits	Financial liabilities	Other	
At 31 December 2014	6,871	297	16,943	200	8,237	32,548
(Debit) credit to income statement	-	-	(5,126)	-	(138)	(5,264)
Debit (credit) to other comprehensive income	-	-	-	2,731	-	2,731
Additions consolidated group	-	-	-	-	10,964	10,964
Translation differences	-	-	-	-	881	881
At 31 December 2015	6,871	297	11,817	2,931	19,944	41,860
(Debit) credit to income statement	(2,211)	43	(1,006)	-	1,553	(1,620)
Debit (credit) to other comprehensive income	-	362	-	(720)	-	(358)
Translation differences	-	-	-	-	(114)	(114)
At 31 December 2016	4,660	702	10,811	2,211	21,383	39,768

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Notes to the Consolidated Annual Accounts

Other mainly includes temporary differences arising upon the acquisition of Encirc (see note 5). The directors consider that the current level of profits ensure the recoverability of the full amount of deferred tax assets.

In 2013 the Company restated its balance sheet in accordance with Law 16/2012 of 27 December 2012, and Regulatory Decree 15/2012 of 28 December 2012 on urgent tax measures applicable to Group companies registered for tax in Alava, which introduced several fiscal measures to consolidate public finances and boost economic activity. Restating its balance sheet, which had no effect for accounting purposes, raised the tax base of property, plant and equipment by Euros 5,991 thousand. Consequently, the Group recognised a deferred tax asset of Euros 1,758 thousand under 'other', with a charge to income tax for 2013, net of the 'one-off tax charge' of Euros 299 thousand.

As permitted by Decree Law 66/2016 published by the Portuguese government on 3 November 2016, the Company revalued certain assets of its Portuguese subsidiary for tax purposes in 2016. As a result of this revaluation, the tax value of the assets has increased by Euros 8,887 thousand, giving rise to a deferred tax asset of Euros 2,311 thousand.

Details of deferred tax assets and liabilities that are expected to be realised or reversed in periods exceeding 12 months, are as follows:

	Thousands of Euros	
	<u>2016</u>	<u>2015</u>
Deferred tax assets	31,928	32,797
Deferred tax liabilities	<u>(46,726)</u>	(40,460)
	<u>(14,798)</u>	<u>(7,663)</u>

Deferred taxes on items debited/(credited) directly to other comprehensive income in 2016, corresponding to hedging operations, amounted to Euros 3,420 thousand (Euros 2,731 thousand at 31 December 2015).

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Details of the income tax expense are as follows:

	Thousands of Euros	
	<u>2016</u>	<u>2015</u>
Current tax		
Present year	16,670	16,522
Prior year adjustments	<u>83</u>	<u>305</u>
Deferred tax		
Source and reversal of temporary differences	(129)	3,403
Expense for reduction in deferred tax assets	2,211	-
Income from reduction in deferred tax liabilities	-	(1,048)
Prior year adjustments	-	(2,155)
Deferred income taken to income tax (note 14)	<u>(2,264)</u>	<u>(2,264)</u>
Total	<u>16,571</u>	<u>14,763</u>

Details of the income tax expense related to profit from continuing operations are as follows:

	Thousands of Euros	
	<u>2016</u>	<u>2015</u>
Profit for the year before income tax from continuing operations	<u>84,242</u>	<u>75,623</u>
Tax calculated at the tax rate of each country	18,943	19,087
Deductions for the year	(236)	(711)
Capitalisation of deductions for shortfall in income tax		
Prior year adjustments	525	(1,963)
Expense for reduction in deferred tax assets	2,112	-
Income from reduction in deferred tax liabilities	-	(1,048)
Deferred income taken to income tax (note 14)	<u>(2,264)</u>	<u>(2,264)</u>
Permanent differences	<u>(2,509)</u>	<u>1,662</u>
Income tax expense	<u>16,571</u>	<u>14,763</u>

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In general, each Group company has open to inspection by the taxation authorities the years which have not prescribed in accordance with tax legislation applicable to each company.

The years open to inspection by the taxation authorities vary for the different companies of the consolidated tax group, but mainly cover the last three or four years.

Permanent differences arise from the application of the tax rate to non-taxable income, which mainly consists of the following:

- In accordance with applicable tax regulations, the Company has applied a 60% reduction to income deriving from the temporary transfer of intangible assets developed by the Company to Group companies for an amount of Euros 9,339 thousand.
- The Company has applied a reduction of 10% of the amount of the increase in its equity for tax purposes compared to the average for the two prior periods for an amount of Euros 9,000 thousand. In this regard, it has apportioned an amount equal to non-distributable reserves for a minimum period of five years, except for the portion of the increase that is incorporated into capital.

In accordance with current legislation in Spain, taxes cannot be considered definitive until they have been inspected and agreed by the taxation authorities or before the inspection period of four years has elapsed. At 31 December 2016 all main applicable taxes since 31 December 2011 are open to inspection by the taxation authorities. Due to the treatment permitted by fiscal legislation of certain transactions, additional tax liabilities could arise in the event of inspection. In any event, the directors do not consider that any such liabilities that could arise would have a significant effect on the 2016 consolidated annual accounts taken as a whole.

10. Inventories

Details of inventories are as follows:

	Thousands of Euros	
	2016	2015
Raw materials	20,811	14,512
Auxiliary and production materials	63,387	72,522
Finished goods and work in progress	<u>108,753</u>	<u>120,335</u>
	192,951	207,369
Impairment	<u>(11,978)</u>	<u>(6,359)</u>
	<u>180,973</u>	<u>201,010</u>

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At 31 December 2016 and 2015 there are no inventories with a recovery period of more than 12 months from the consolidated balance sheet date.

Group companies have contracted insurance policies to cover the risk of damage to their inventories. The coverage of these policies is considered sufficient.

The effect of the change in impairment has been recognised under changes in inventories of finished goods and work in progress.

11. Trade and Other Receivables

Details of trade and other receivables are as follows:

	Thousands of Euros	
	2016	2015
Trade receivables	190,794	202,391
Personnel	-	6
Other loans	10,828	9,638
Less impairment due to uncollectibility	<u>(7,166)</u>	<u>(6,757)</u>
Total	<u>194,456</u>	<u>205,278</u>

The carrying amount of trade and other receivables does not differ significantly from their fair value.

Based on recoverability levels, the Company considers all balances older than 30 days to be past due. At 31 December 2016 there are matured loans amounting to Euros 6.1 million, which is equivalent to 0.79% of sales.

As explained in the note on risks in the directors' report, the level of actual recoverability of matured loans in the past is significant, thus bringing actual uncollectibility to below the aforementioned percentage.

There is no concentration of credit risk as regards trade receivables as the Group has a large number of customers worldwide.

At 31 December 2016 and 2015 the Company has no trade and other receivables discounted at financial institutions.

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12. Other Current Assets and Liabilities

Details of other current assets are as follows:

	Thousands of Euros	
	<u>2016</u>	<u>2015</u>
Public entities		
Value added tax	8,650	6,624
Other items	<u>184</u>	<u>112</u>
	<u><u>8,834</u></u>	<u><u>6,736</u></u>

Details of other current liabilities are as follows:

	Thousands of Euros	
	<u>2016</u>	<u>2015</u>
Public entities		
Value added tax	14,914	17,446
Withholdings and payments on account	2,695	9,960
Social Security	2,858	1,730
Other	<u>844</u>	<u>412</u>
	<u><u>21,311</u></u>	<u><u>29,548</u></u>

13. Equity

Details of equity and movement during the year are shown in the statement of changes in equity.

Details of other reserves and retained earnings and movement during the year are shown in the Appendix.

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VIDRALA, S.A. AND SUBSIDIARIES

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(a) Capital

Movement of issued and outstanding shares in 2016 and 2015 is as follows:

	Number of shares outstanding	Thousands of Euros		
		Ordinary shares	Own shares	Total
At 31 December 2014	24,783,120	25,290	(236)	25,054
Acquisition of own shares	(151,386)	-	(6,498)	(6,498)
Sale of own shares	162,607	-	6,734	6,734
At 31 December 2015	24,794,341	25,290	-	25,290
Acquisition of own shares	(80,727)	-	(3,757)	(3,757)
Sale of own shares	20,828	-	933	933
At 31 December 2016	24,734,442	25,290	(2,824)	22,466

At 31 December 2016 and 2015 the share capital of Vidrala, S.A. is represented by 24,794,341 ordinary shares represented by book entries of Euros 1.02 par value each, fully paid and listed on the Madrid and Bilbao stock exchanges. No company directly or indirectly holds more than 10% of share capital.

These shares are freely transferable.

At the Vidrala, S.A. annual general meeting held on 31 May 2016, the shareholders authorised and granted the board of directors the necessary powers to carry out a derivative acquisition of own shares, either directly or indirectly through Group companies, and to reduce share capital, if appropriate, in order to redeem own shares.

In 2016 and 2015, 80,727 and 151,386 Parent shares were acquired on the organised market for Euros 3,757 thousand and Euros 6,498 thousand, respectively. Similarly, 20,828 and 162,607 Parent shares were sold for Euros 1,214 thousand and Euros 7,231 thousand, respectively.

The Group manages its capital with the aim of safeguarding its capacity to continue operating as a going concern, so as to continue providing shareholder remuneration and benefiting other stakeholders, while maintaining an optimum capital structure to reduce the cost of capital.

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To maintain and adjust the capital structure, the Group can adjust the amount of dividends payable to shareholders, repurchase or sell own shares, reducing capital if necessary by redeeming own shares, reimburse capital, issue shares or dispose of assets to reduce debt.

The Vidrala Group controls its capital structure using a number of different indicators. One of these is the ratio of equity as a percentage of total equity and liabilities on the consolidated balance sheet, which it endeavours to keep no lower than 20%.

In 2016, despite the increase in debt due to the extraordinary financing assumed for the acquisition of Encirc Limited in the prior year (see note 15), the Group's capitalisation has strengthened, as shown by the following ratios for 2016 and 2015:

	Thousands of Euros	
	2016	2015
Total equity	474,934	476,536
Total equity and liabilities	1,096,243	1,200,033
Total equity/total equity and liabilities	<u>43.32%</u>	<u>39.71%</u>

The Vidrala Group controls its levels of net financial debt based on net debt as a percentage of equity.

This calculation was performed as follows:

	Thousands of Euros	
	2016	2015
Net financial debt	322,266	404,162
Equity	474,934	476,536
Debt ratio	<u>0.68</u>	<u>0.85</u>

Net financial debt is understood as current and non-current loans and borrowings less cash and cash equivalents.

(Continued)

VIDRALA, S.A. AND SUBSIDIARIES

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In conclusion, year-end solvency indicators for the Group have strengthened, showing a debt-to-equity ratio of 0.68 (0.85 at the 2015 close) and debt equivalent to 1.89 times accumulated EBITDA (2.51 at the 2015 close). The interest coverage ratio, measured as EBITDA for the year divided by the consolidated net finance cost, is 17.8.

(b) Other reserves

- **Revaluation reserve Provincial Law 4/1997**

This revaluation reserve comprises the revaluation carried out by the Parent as permitted by Alava Provincial Law 4/1997 of 7 February 1997, whereby Vidrala revalued its property, plant and equipment in 1996 by a net amount of Euros 3.8 million.

- **Revaluation reserve Decree Law 66/2016**

Euros 2,311 thousand was recognised in revaluation reserves in 2016 comprising the revaluation carried out in the subsidiary Gallo Vidro, S.A., as permitted by Decree Law 66/2016 of 3 November 2016 on the revaluation of commercial assets enacted by the Portuguese government.

- **Capitalisation reserve**

The capitalisation reserve has been appropriated in accordance with articles 25 and 62 of the Spanish Income Tax Law, which require that an amount equal to the reduction in the tax group's taxable income for the year be appropriated to the reserve. The amount by which the tax group is entitled to reduce taxable income is equal to 10% of the increase in its equity, as defined in the aforementioned article. In no case may this reduction exceed 10% of the tax group's taxable income for the tax period prior to the reduction, before the integration referred to in article 11.12 of the Law and before offsetting tax loss carryforwards. However, if the reduction cannot be applied because the tax group does not generate sufficient taxable income, the outstanding amounts may be applied in the tax periods ending in the two years immediately after the end of the tax period in which the tax group became entitled to the reduction, together with any reduction applicable in that period, subject to the limit indicated. The reserve is restricted and the increase in the tax group's equity must be maintained for a five-year period from the end of the tax period in which the group became entitled to the reduction, unless accounting losses are incurred.

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At 31 December 2016 the Group has included a non-distributable capitalisation reserve of Euros 150,671,076.11 within voluntary reserves.

- **Legal reserve**

The legal reserve has been appropriated in compliance with article 274 of the Revised Spanish Companies Act, which requires that companies transfer 10% of profits for the year to a legal reserve until this reserve reaches an amount equal to 20% of share capital.

The legal reserve is not distributable to shareholders and if it is used to offset losses, in the event that no other reserves are available, the reserve must be replenished with future profits.

(c) **Other comprehensive income**

Movement in cash flow hedges and the tax effect, is as follows:

	Thousands of Euros		
	Cash flow hedges	Tax effect	Net
Balances at 31 December 2014	<u>(713)</u>	<u>200</u>	<u>(513)</u>
Income and expenses generated during the year	(11,204)	3,137	(8,067)
Reclassification to profit or loss	<u>1,451</u>	<u>(406)</u>	<u>1,045</u>
Balances at 31 December 2015	<u>(10,466)</u>	<u>2,931</u>	<u>(7,535)</u>
Income and expenses generated during the year	10,324	(2,891)	7,433
Reclassification to profit or loss	<u>1,889</u>	<u>(529)</u>	<u>1,360</u>
Balances at 31 December 2016	<u>1,747</u>	<u>(489)</u>	<u>1,258</u>

Translation differences

Translation differences fully comprise the effect of converting the financial statements of the subsidiary Encirc, the functional currency of which is the Pound Sterling, giving a negative impact for the year of Euros 57,397 thousand deriving from the appreciation of the euro against the pound.

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Defined benefit plans

These fully comprise the cost of defined benefit plans for pensions and other post-employment medical benefits for the subsidiary Encirc, the impact of which on other comprehensive income is Euros 1,308 thousand (see note 19).

(d) Dividends and restrictions on distribution of dividends

Total dividends distributed by Vidrala, S.A. to shareholders in 2016 amounted to Euros 17,853 thousand (Euros 16,225 thousand in 2015), which is equivalent to 72.00 euro cents per share outstanding (65.46 euro cents in 2015). The dividends reflect the distribution of 2015 profit.

The distribution of Company profits and reserves for the year ended 31 December 2015, approved by the shareholders at their annual general meeting held on 31 May 2016, was as follows:

<u>Basis of allocation</u>	<u>Euros</u>
Profit for the year	36,980,147,56
 <u>Distribution</u>	
Other reserves	19,127,279,85
Dividend	4,767,455,89
Interim dividend	<u>13,085,411,82</u>
	<u>36,980,147,56</u>

On 20 December 2016 the directors agreed to distribute an interim dividend on 2016 profit of 58.00 euro cents per share to shareholders, totalling Euros 14,360 thousand, which was paid on 14 February 2017.

The amount distributed did not exceed the profits reported by the Parent since the end of the previous reporting period, after deducting the estimated income tax payable on these profits, as required by article 277 of the Revised Spanish Companies Act.

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VIDRALA, S.A. AND SUBSIDIARIES

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The provisional accounting statement prepared in accordance with statutory requirements demonstrating that sufficient cash was available for distribution of the aforementioned dividend is as follows:

	<u>Thousands of Euros</u>
Forecast distributable profit for 2016	
Projected profit after income tax to 31.12.2016	
Interim dividend distributed	17,853
Forecast cash flow for the one-year period from 20 December 2016	
Cash and cash equivalents at agreement date	-
Credit facilities available at agreement date	54,165
Projected operating receipts and payments (net)	42,757
Projected cash and cash equivalent balances one year from agreement date	<u>96,922</u>
Credit facilities available (one year later)	<u>18,211</u>

The proposed distribution of 2016 profit and other Parent reserves to be submitted to the shareholders for approval at their annual general meeting is as follows:

<u>Basis of application</u>	<u>Euros</u>
Profit for the year	54,957,207,04
<u>Distribution</u>	
Other reserves	35,130,078,34
Dividend	5,466,311,68
Interim dividend	<u>14,360,817,02</u>
	<u>54,957,207,04</u>

The proposed distribution of dividends is equivalent to a total unit dividend, including the interim dividend paid, of Euros 0.8016 per share outstanding at the reporting date.

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14. Deferred Income

Details of this caption are as follows:

	Thousands of Euros	
	2016	2015
Capital grants (note 6(a))	20,333	22,385
Tax credits for investments	<u>11,202</u>	<u>11,278</u>
	<u>31,535</u>	<u>33,663</u>

In 2016 the Group incorporated additional capital grants amounting to Euros 3,534 thousand (Euros 3,750 thousand in 2015), of which Euros 3,590 thousand was taken to income during the year (Euros 3,278 thousand in 2015) (see note 22).

Tax credits capitalised in 2004 and 2005 were recorded as deferred income and taken to the income statement in line with the depreciation of the financed assets, in the case of property, plant and equipment, or the recovery of the investments in the case of business combinations. Euros 2,264 thousand was taken to profit or loss as a reduction in income tax in 2016 and 2015 (see note 9).

15. Debt with Financial Institutions

Details of current and non-current loans and borrowings are as follows:

	Thousands of Euros			
	2016		2015	
	Non-current	Current	Non-current	Current
Loans and borrowings	299,689	10,801	409,129	3,099
Other financial liabilities	10,599	1,275	6,703	405
Accrued interest	-	<u>326</u>	-	<u>546</u>
	<u>310,288</u>	<u>12,402</u>	<u>415,832</u>	<u>4,050</u>

Some of these contracts contain financial covenant clauses. At 31 December 2016 and 2015 the Group complies with these requirements.

Other financial liabilities include interest-free loans from public entities.

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The terms and conditions of these loans and borrowings are as follows:

<u>Type</u>	<u>Extended</u>	<u>Maturity</u>	<u>Limit extended/ nominal amount</u>	<u>Thousands of Euros</u>	
				<u>Current</u>	<u>Non-current</u>
Loan	2015	2021	440,000	-	284,615
Loan	2014	2018	15,000	-	15,000
Credit facility	2010	2018	5,000	-	74
Credit facility	2010	2018	7,500	-	-
Credit facility	2010	2018	25,000	-	-
Other short-term credit facilities	2016	2017	88,250	<u>10,801</u>	<u>-</u>
				<u>10,801</u>	<u>299,689</u>

Non-current loans and borrowings mature as follows:

	<u>Thousands of Euros</u>	
	<u>2016</u>	<u>2015</u>
Between 1 and 2 years	23,386	37,820
Between 2 and 5 years	166,902	216,101
More than 5 years	<u>120,000</u>	<u>161,911</u>
	<u>310,288</u>	<u>415,832</u>

On 12 January 2015 Vidrala, S.A. entered into a secure financing agreement for an amount of Euros 465 million, divided into three tranches - a bridge loan, a non-current loan and a revolving credit facility - in order to transitionally fund the acquisition of Encirc Ltd., which was paid on 14 January 2015 through its subsidiary Inverbeira Sociedad Promoción de Empresas, S.A.

With a view to structuring its non-current defined financing model, on 13 March 2015 Vidrala cancelled the aforementioned agreement, refinancing it entirely through a single new non-current syndicated financing agreement with a group of nine financial institutions for an amount of Euros 465 million. The new financing agreement comprised a non-current loan of Euros 440 million, with maturity on 21 March 2021, and a revolving credit facility of up to Euros 25 million. Several Group companies acted as guarantors of the loan: Inverbeira Sociedad de Promoción de Empresas, S.A.; Aiala Vidrio, S.A.U.; Crisnova Vidrio, S.A.; Castellar Vidrio, S.A. and Vidrala Italia S.R.L.

On 10 December 2015 Vidrala agreed with all of the financial institutions to renew the loan, changing the applicable interest rate.

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On 14 November 2016 Vidrala agreed with the financial institutions to further renew the loan, changing the applicable interest rate, the repayment period and maturity date, which was extended to 13 September 2022. As the conditions of the new loan are not substantially different from the previous one (the percentage difference between the current value of the cash flows of the new financial liability compared to the amended one is 2.5%), it is considered an amendment of the previous loan rather than an exchange of liabilities (see note 3(g)).

As a result, the balance of the non-current syndicated loan at year end is Euros 290 million, as early repayments totalling Euros 175 million have been made since the loan was extended. The applicable interest rate on the loan is a variable rate equivalent to Euribor plus a spread of 1.25%, reviewed on an annual basis by tranche based on the evolution of the net debt/consolidated EBITDA ratio. In 2017 the loan will be in a grace period and as such the Company has no obligation to repay the principal. The first repayment of the principal falls due on 13 September 2019 for an amount of Euros 10 million.

The agreement has clauses containing commitments linked to certain stipulations (covenants), typical of agreements of this nature, failure to comply with which could give rise to the early maturity of the financing.

At the date of authorisation for issue of these annual accounts, these commitments have been complied with, as reflected by the results of the following indicators at 31 December 2016:

Net financial debt / consolidated EBITDA: 1.9

Consolidated EBITDA / consolidated net finance cost: 17.8

The credit facilities included under loans and borrowings have a combined limit, including the aforementioned loan, of Euros 431 million and Euros 557 million at 31 December 2016 and 2015, respectively. Consequently, Euros 118 million and Euros 146 million were available for drawdown at those dates. Furthermore, a limit of Euros 20 million was available in discounting lines in 2016 and 2015, with no amounts having been used at the year-end closes.

Financial liabilities under this heading comprise debts and payables at amortised cost.

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The carrying amount and fair values of current and non-current liabilities do not differ significantly.

Group financial liabilities are measured in Euros.

16. Trade and Other Payables

Details of trade and other payables are as follows:

	Thousands of Euros	
	2016	2015
Trade payables	147,361	138,049
Salaries payable	10,938	9,374
Dividends to shareholders	14,362	13,086
Suppliers of fixed assets	-	385
Other payables	<u>1,845</u>	<u>6,827</u>
	<u>174,506</u>	<u>167,721</u>

The carrying amount of trade and other payables does not differ significantly from their fair value.

17. Average Supplier Payment Period. "Reporting Requirement", Third Additional Provision of Law 15/2010 of 5 July 2010

Information on the average Spanish supplier payment period by the Spanish companies in 2016 is as follows:

	Days	
	2016	2015
Average supplier payment period	8,34	6,55
Transactions paid ratio	12,83	8,96
Transactions payable ratio	13,54	8,43
	Amount (thousands of Euros)	
Total payments made	172,498	208,518
Total payments outstanding	35,404	33,431

18. Risk Management Policy**Business risks**

Risk management at Vidrala involves procedures drawn up by management, overseen by the directors and implemented in the daily running of the organisation.

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Operational risk

The Vidrala Group's manufacturing and sales activity, carried out through eight industrial centres, is continuous, intensive and subject to inherent risks linked to routine operations. In 2016, work continued on the identification, evaluation and monitoring of business risks defined as operational. The aim is to identify potential risks, through continuous review, gain a perspective on their impact and probability of occurrence and, principally, to link each area of operations and each business process to adequate control and monitoring systems in order to minimise their potential adverse effects.

Potential operating risks include the following:

i. Environmental risks

The Vidrala Group declares itself firmly committed to protecting the environment. With this objective in mind, Vidrala implements specific action plans in relation to emissions in the atmosphere, dumping, waste, the consumption of raw materials, energy, water and noise.

Glass manufacturing is an inherently energy-intensive process as melting furnaces are in operation 24 hours a day, 365 days a year. Given the industrial nature of the process, one of management's objectives is to reduce the associated environmental impact. In order to achieve this, specific investments are made to upgrade factory facilities and adapt them to the most efficient technological systems for reducing environmental impacts. Additionally, operating priorities are focused on intensifying the growing use of recycled products as the main raw material for manufacturing glass, the effect of which is twofold as it not only avoids the consumption of natural raw materials, but also contributes to reducing fossil fuel consumption and the resulting pollution.

One of the Group's strategic guidelines is the implementation of environmental management systems. In line with this commitment, all the Group's production facilities have ISO 14001:2004 certification, demonstrating that Vidrala operates under a global, externally verified and recognised environmental management system. Furthermore, in keeping with its undertaking to continuous improvement, the implementation and certification of new environmental standards has begun, such as ISO 14064:2012, related to the voluntary declaration of CO₂ emissions, or the ISO 50001:2011 energy management system standard, both of which, CO₂ emissions and energy, are of clear environmental significance in our industrial process.

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In addition, Vidrala has a specific commitment to invest in minimising the potential polluting effect of its facilities. Of particular relevance during 2016 in this regard was the conclusion of a major project to install special atmospheric emissions purification systems, called electrostatic precipitators or electrofilters, in all production centres. These installations, which have cost the Group more than Euros 20 million over the last eight years, are aimed exclusively at reducing emissions of particulate pollutants, and are recognised under European legislation as the best currently available technology in this regard. Electrofilters work by attracting and retaining articles generated during the melting process through electrical fields, and reduce typical melting furnace emissions by more than 90%.

As proof of our environmental commitment, Vidrala's advancement towards environmental efficiency is documented in detail in its annual sustainability report published on the Company's website.

ii. Occupational health and safety

Vidrala's daily activity is carried out by some 3,200 employees, the majority of whom work in an industrial or manufacturing environment.

Consequently, the Vidrala Group remains committed to establishing the soundest occupational health and safety measures. This commitment is endorsed by the gradual implementation of occupational health and safety management systems based on OSHAS 18001:2007, which are certified by independent entities accrediting the existence of an internationally recognised management framework.

With a specific view to preventing labour-related accidents, Vidrala implements specific and systematic ongoing staff training and awareness plans. The sustainability report, attached to this report, details the progress of occupational health and safety management indicators. These plans are developed and distributed among all agents involved in the organisation, allowing health and safety trends to be objectively measured and documented, and enabling the actual effectiveness of the processes and controls implemented to be observed, and whether additional corrective measures are needed.

iii. Supply chain risk

Production-intensive, continuous-service industries such as Vidrala's can be vulnerable to risks of distortion in the supply chain.

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As regards supply risk affecting key products, materials, installations or technologies for the production process, management initiatives include the continual and specialised search for supply sources and strengthening ties with suppliers, diversifying and forging long-term relationships, establishing ongoing audit and standardisation processes and developing supply alternatives in all relevant areas.

Steps taken to address customer service and product quality risks include the development of a specific departmental area separate from the rest of the organisational areas dedicated exclusively to quality. There is a specific investment project nearing completion that aims to guarantee product quality targets and optimise product quality control through the implementation of state of the art technology across all the Group's facilities.

Concerning inventory risk, the Group systematically carries out a specific and periodic controls to ensure the quality of finished products in the warehouse, and optimise ageing and rotation so that both the volume and value of stocks are balanced to sales forecasts. These controls have resulted in the implementation of automated stock monitoring processes and the subsequent application of specific adaptation, physical and valuation measures, which in 2016 are giving rise to inventory impairment adjustments in the income statement.

Financial risk

Global uncertainty in the financial markets and the growing scale of Vidrala's operations expose activities to potentially destabilising elements of an external nature. These financial risks require the implementation of specific control mechanisms.

Managing Vidrala's financial risks focuses on the identification, analysis and monitoring of market fluctuations in items that could affect the business's profits. This involves defining systematic measurement, control and monitoring processes to minimise any potential adverse effects and structurally reduce the volatility of results. To hedge certain risks, Vidrala employs, or is in a position to employ, derivative financial instruments the volume and characteristics of which are described in the annual report.

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The most relevant financial risks are as follows:

i. Currency risk

Vidrala operates at international level and is therefore exposed to currency risk on transactions in currencies other than the euro.

Currency risk affecting the Group's present structure mainly stems from the exposure inherent in the global expansion of the Group after the incorporation of Encirc Ltd. in 2015, with activities in the UK and Ireland. Approximately 80% of operating results generated by this division over the past year were in pounds sterling, and the remainder directly in euros.

In order to quantify the sensitivity to the currency at consolidated Group level, as a result of the above, approximately 30% of EBITDA is generated in pounds sterling. Consequently, reporting this in euros is subject to translation risks that may arise from fluctuations in sterling against the euro. There is also a risk when converting sterling cash generated in the UK to euros, in that the depreciation of sterling could reduce the equivalent value in euros, thus reducing the amount of cash generated by the business.

To quantify the sensitivity to this risk, based on 2016 data, had sterling depreciated by an average of 5% during year, and the remaining variables remained constant, and assuming there were no instruments to hedge this risk, the Group's consolidated profit would have varied by approximately 2.8% and annual cash flow would have fallen by approximately 1.7%.

To control currency risk, Vidrala uses derivative instruments, principally forward sale contracts or currency put options. To manage the risks described, at the 2016 reporting date Vidrala had sterling put options expiring in 2017, for an accumulated equivalent of Euros 23 million. This is equivalent to approximately 65% of the cash generated in this currency during 2016.

ii. Interest rate risk

Interest rate risk affects the cost of borrowings used to finance the Group's operations. Borrowings contracted at variable interest rates expose Vidrala to the risk of interest rate fluctuations, which in turn affects forecast cash flows.

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The Group's financing policy is to focus its borrowings on variable rate instruments. Vidrala manages interest rate risks in cash flows through interest rate swaps or caps. These derivative hedging instruments convert variable interest rates on borrowings to fixed interest rates (swaps) or limit the cost of variable rate borrowings (caps). Generally the Vidrala Group obtains long-term variable rate borrowings and swaps them for fixed interest rates. This gives better rates than had the financing been obtained directly with fixed interest rates. Through interest rate swaps the Vidrala Group undertakes to periodically exchange the difference between fixed and variable interest with other financial entities. The difference is calculated based on the contracted notional amount. Under interest rate caps Vidrala has the right, and the counterparty the obligation, to settle the difference between the variable interest rate and the stipulated rate if this is positive. The effectiveness of these instruments as regards fixing the interest rate of contracted financing is assessed and documented using accepted methodologies under applicable accounting legislation.

On account of this risk control policy, at the 2016 reporting date Vidrala has interest rate swaps for an accumulated equivalent of Euros 405 million, which start and expire progressively until 2022, of which Euros 305 million are in force at the reporting date. As a result, the total debt interest cost to be assumed by the Group during 2017 is hedged against fluctuations in market interest rates.

iii. Credit risk

The Vidrala Group has specific policies to mitigate the credit risk of receivables. The procedure begins with developing systemised sales authorisation processes for customers with adequate credit records and solvency in order to minimise the risk of default. This control process involves ongoing solvency analysis, setting specific, assumable risk limits for each customer, analysing variables such as specific credit metrics, the segment or geographical area in which they operate and preparing individual classifications of ratings typical of evolved credit control systems. In summary, the procedure is done through the creation and maintenance of an internal customer credit rating system.

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Furthermore, control of collection risk is intensified with a second level of control involving credit insurance policies with external insurance entities. The aim of these credit insurance policies is to cover the economic impact of eventual situations involving significant amounts where the internal system is ineffective in predicting a risk of default.

In order to demonstrate the collection risk system implemented, Vidrala has subjected the quality of its processes to official external certification. Obtaining this certification, and the resolve to periodically renew it, will guarantee the validity, effectiveness and efficiency of the system in place, and will require formal audits, dynamic monitoring and ongoing improvements.

As a result of the control procedures described, the actual impact of bad trade debts during 2016 was limited to 0.01 % of turnover

Other credit risks: financing, derivative and cash transactions are only carried out with financial institutions with high credit ratings.

iv. Liquidity risk

Vidrala's liquidity risk basically stems from the maturing of current and non-current debt obligations, transactions with derivative instruments and payment commitments with other trade creditors. Vidrala's policy is to continually monitor and ensure that sufficient resources are available to meet these obligations, maintain internal control processes through follow-ups of budgets and deviations, and implement any necessary contingency plans.

In order to accomplish these objectives, Vidrala prudently manages its liquidity risk by adapting maturities to the maturity of assets to be financed, diversifying the sources of financing used and maintaining the availability of immediate financing.

At 31 December 2016 the Vidrala Group had Euros 118.4 million in immediately available, external undrawn credit, representing 37% of total debt.

(Continued)

VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

v. Debt and solvency

At 31 December 2016, the Vidrala Group had consolidated net financial debt of Euros 322.3 million, having reduced indebtedness by Euros 82 million, or 20.3%, during the year. The financial solvency indicators at the reporting date reflect a debt equivalent to 1.9 times accumulated EBITDA for the last twelve months, representing a financial deleveraging compared to the ratio of 2.5 at the prior year end.

The core of the financing structure is a long-term syndicated loan signed on 13 March 2015 with a consortium of nine financial institutions, for an original amount of Euros 465 million. After a second novation of the loan terms was signed in November 2016, the applicable interest rate on the loan in 2017 will be a variable rate pegged to Euribor plus a spread of 1%, reviewed on an annual basis by tranche based on the evolution of the net debt/consolidated EBITDA ratio. The due date of the loan has been extended to 13 September 2022, and is gradually repayable from 13 March 2019. Consequently, in 2017 the loan will be in a grace period, with no obligation to repay the principal.

This loan has certain covenants attached, which are typical in these types of contract. At the reporting date, these commitments have been fully complied with, as reflected by the results of the following indicators:

Net financial debt / consolidated EBITDA 1.9x

Consolidated EBITDA / consolidated net finance cost 17.8x

vi. Price risk in energy purchases

Energy consumption, principally natural gas and electricity, represents a significant source of operating costs inherent in Vidrala's glass production and manufacturing activity.

(Continued)

VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

Fluctuations in the variables that determine their prices, represented in the natural volatility of the global energy commodities markets, has a bearing on the profitability of the business. In order to manage the potential impact of this risk, the Group employs specific control processes to mitigate potential unexpected effects on operating margins that would arise in the event of inflationary tendencies in the market. These measures involve implementing adapted price-setting formulas, continuous monitoring of market variables through dedicated management and control departments and risk control through price hedging strategies, including the contracting of tariffs at fixed prices and the use of derivative hedging instruments.

As a result of this risk control policy, at the 2016 reporting date Vidrala has hedging derivatives on energy commodities for a nominal equivalent of Euros 51.2 million.

vii. Other risks. Result of the Brexit referendum

Vidrala has strategic business interests in the UK and Ireland through its Encirc Limited division, acquired at the beginning of 2015. Encirc is a manufacturer of glass containers aimed at the domestic food and drinks market in Ireland and the UK, where it operates two plants. It offers a complete range of services, from the manufacture of glass containers to state of the art packaging processes and logistics services. Of the profits obtained by this division over the past year, approximately 80% of operating results are generated in sterling, and the remainder directly in euros. As a whole, Encirc is eminently domestic, producing glass containers in the UK for sale throughout the British Isles, including the Republic of Ireland, and the volume of exports outside these regions is immaterial.

On 23 June 2016, the UK voted in a referendum on whether to remain in the European Union, resulting in the now famous Brexit. As a result, a political process has begun to negotiate the terms and conditions of the referendum whose implications are still uncertain.

VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

One instant effect was the devaluation of sterling, which at the reporting date had depreciated by approximately 11.8% against the euro compared to pre-referendum levels. For the purposes of quantifying the sensitivity of the business to fluctuations in sterling, as in the section on the quantification of currency risks, if sterling had depreciated by an average of 5% during the year, with the rest of the variables remaining constant, and not considering hedging instruments, the Group's annual consolidated profit would have varied by approximately 2.8% and annual cash flow would have fallen by approximately 1.7%.

In any event, the structural foundations of demand for glass packaging in the UK remain stable, backed by the region's level of socio-demographic development, the progressive lean towards greater consumption of quality products and the natural limited variability of demand for food and drink products. Encirc optimises these market foundations thanks to a commercial position endorsed by relationships fostered with world class customers, market share stability, competitiveness backed by modern industrial facilities and the added value they give to packaging services, whose unique competitive advantages for owners interested in exporting bulk materials to the growing demand in the UK have been boosted.

19. Provisions

Movement in provisions in 2016 and 2015 is as follows:

	Thousands of Euros			
	Emission allowances	Personnel	Other provisions	Total
At 31 December 2015	<u>2,481</u>	<u>952</u>	<u>338</u>	<u>3,771</u>
Charge against profit or loss	3,956	1,569	1,011	6,536
Actuarial gains and losses due to changes in financial assumptions	-	1,308	-	1,308
Payments	(1,130)	-	-	(1,130)
Other	-	<u>1,270</u>	-	<u>1,270</u>
At 31 December 2016	<u>5,307</u>	<u>5,099</u>	<u>1,349</u>	<u>11,755</u>

	Thousands of Euros			
	Emission allowances	Personnel	Other provisions	Total
At 31 December 2014	<u>3,158</u>	<u>1,776</u>	<u>453</u>	<u>5,387</u>
Charge against profit or loss	3,278	-	-	3,278
Payments	<u>(3,955)</u>	<u>(824)</u>	<u>(115)</u>	<u>(4,894)</u>
At 31 December 2015	<u>2,481</u>	<u>952</u>	<u>338</u>	<u>3,771</u>

(Continued)

VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

The provision for emission allowances includes the estimated surrender of emission allowances in 2016 and 2015 measured at the grant date, as described in note 3.

The personnel provision reflects defined benefit plans and other obligations with employees. The Group makes contributions to a defined benefit plan in the UK, which consists of ensuring a pension for retired employees and post-retirement medical coverage. The plan is managed separately from the Company, and defined benefit plans are valued by an independent expert, Xafinity Consulting Limited, pursuant to IAS 19.

20. Contingencies

The Group has contingent liabilities for bank and other guarantees related to routine business operations amounting to Euros 3,794 thousand (Euros 16,611 thousand in 2015). These guarantees mainly comprise those extended to public entities for commitments assumed. The Group's directors do not expect any significant liabilities to arise from these guarantees.

21. Environmental Information

In 2010 positive results were obtained in the ISO 14001/2004 certification in recognition of the organisation's ongoing efforts to improve the environment.

The total cost of initiatives taken by the Vidrala Group in 2016 to comply with the Kyoto Protocol and emissions analyses amounted to Euros 82 thousand (Euros 107 thousand in 2015).

Environmental expenses mainly related to waste management incurred during 2016 totalled Euros 816 thousand (Euros 875 thousand in 2015).

Environment-related plant investments came to Euros 4,513 thousand (Euros 13,937 thousand in 2015).

22. Revenue and Other Income

Details of revenue are shown in note 4, Segment Reporting.

(Continued)

VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

Details of other income are as follows:

	Thousands of Euros	
	2016	2015
Operating grants	146	224
Capital grants taken to income (note 14)	3,590	3,278
Grants for emission allowances	2,611	3,659
Other income	<u>2,109</u>	<u>2,731</u>
	<u>8,456</u>	<u>9,892</u>

23. Other Expenses

Details of other expenses are as follows:

	Thousands of Euros	
	2016	2015
External services	35,918	37,981
Electricity	39,371	46,801
Sales expenses	73,456	79,889
Surrender of emission allowances (note 19)	3,956	3,278
Taxes	5,716	5,493
Impairment and uncollectibility of trade and other payables (note 11)	409	522
Other operating expenses	<u>7,688</u>	<u>8,047</u>
	<u>166,514</u>	<u>182,011</u>

24. Employee Benefits Expense

Details of the employee benefits expense in 2016 and 2015 are as follows:

	Thousands of Euros	
	2016	2015
Salaries, wages and similar	141,081	142,502
Contributions to defined contribution plans	243	246
Other employee benefits	<u>24,807</u>	<u>23,367</u>
	<u>166,131</u>	<u>166,115</u>

(Continued)

VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

The average headcount of the Group in 2016 and 2015, distributed by category, is as follows.

	Average headcount	
	2016	2015
Senior management and proxies	41	40
Junior management	296	362
Administrative staff	347	280
Operators	<u>2,365</u>	<u>2,370</u>
	<u>3,049</u>	<u>3,052</u>

At 31 December 2016 and 2015 the distribution by gender of Group personnel and directors is as follows:

	Number			
	2016		2015	
	Female	Male	Female	Male
Board members	3	8	3	8
Management	3	40	2	37
Junior management	56	323	56	338
Administrative staff	118	263	117	254
Operators	<u>202</u>	<u>2,097</u>	<u>204</u>	<u>2,059</u>
	<u>382</u>	<u>2,731</u>	<u>382</u>	<u>2,696</u>

(Continued)

VIDRALA, S.A. AND SUBSIDIARIES
Notes to the Consolidated Annual Accounts

25. Finance Income and Finance Costs

Details of finance income and finance costs are as follows:

<u>Finance income</u>	Thousands of Euros	
	<u>2016</u>	<u>2015</u>
Exchange gains	805	-
Other finance income	<u>174</u>	<u>1,650</u>
Total finance income	<u>979</u>	<u>1,650</u>

<u>Finance costs</u>	Thousands of Euros	
	<u>2016</u>	<u>2015</u>
Interest on loans and borrowings	6,042	8,578
Hedging derivatives	1,889	1,451
Exchange losses	-	637
Other finance costs	<u>1,845</u>	<u>1,648</u>
Total finance costs	<u>9,776</u>	<u>12,314</u>

26. Earnings per Share

(a) Basic

Basic earnings per share is calculated by dividing the profit or loss for the year attributable to equity holders of the Parent by the weighted average number of ordinary shares outstanding during the year, adjusted for own shares held (see note 13).

Details of the calculation of basic earnings per share are as follows:

	<u>2016</u>	<u>2015</u>
Profit for the year attributable to equity holders of the Parent (thousands of Euros)	67,671	60,860
Weighted average number of ordinary shares outstanding (thousands)	<u>24,728</u>	<u>24,787</u>
Basic earnings per share (Euros per share)	<u>2.73</u>	<u>2.46</u>

(Continued)

VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

The weighted average number of ordinary shares outstanding is determined as follows:

	<u>2016</u>	<u>2015</u>
Ordinary shares outstanding at 1 January	24,794,341	24,776,281
Effect of own shares	<u>(41,282)</u>	<u>11,221</u>
Weighted average number of ordinary shares outstanding at 31 December	<u>24,753,059</u>	<u>24,787,502</u>

(b) Diluted

Diluted earnings per share is determined by adjusting the profit or loss for the year attributable to equity holders of the Parent and the weighted average number of ordinary shares outstanding for the effects of all dilutive potential ordinary shares. The Company has no dilutive potential ordinary shares.

27. Related Party Balances and Transactions**(a) Commercial transactions**

During 2016 and 2015 the Group has not carried out any transactions with related parties vis-à-vis the sale or purchase of goods or the rendering of services.

(b) Related party balances

The Group has no related party balances.

(c) Conflicts of interest concerning the directors

The directors of Vidrala, S.A. and their related parties have had no conflicts of interest requiring disclosure in accordance with article 229 of the Revised Spanish Companies Act.

(Continued)

VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

(d) Remuneration of key management personnel and directors

Details are as follows:

	<u>Thousands of Euros</u>	
	<u>2016</u>	<u>2015</u>
Salaries and other current remuneration paid to employees, management and directors	<u>3,973</u>	<u>6,784</u>

During 2016 the Group has reviewed its organisational structure and redefined senior management positions. At 31 December 2016, the directors and senior management numbered 23 in total (50 in 2015).

(e) Remuneration of the directors of Vidrala

The Company has not extended any amounts to the members of the board of directors of the Parent in respect of guarantees, advances, loans or any pension-related rights. Total remuneration accrued by the board during the year, including salaries, allowances and other items, amounted to Euros 1,227 thousand (Euros 1,111 thousand in 2015).

28. Audit Fees

The firm auditing the annual accounts of the Group has accrued net fees for professional services during the years ended 31 December 2016 and 2015 as follows:

	<u>Thousands of Euros</u>	
	<u>2016</u>	<u>2015</u>
KPMG Auditores, S.L.		
Audit services	182	180
Other services	<u>25</u>	<u>26</u>
	<u>207</u>	<u>206</u>
Total KPMG	<u>207</u>	<u>206</u>

(Continued)

VIDRALA, S.A. AND SUBSIDIARIES

Notes to the Consolidated Annual Accounts

These amounts include all fees for services rendered during 2016 and 2015, irrespective of the date of invoice.

During 2016, other auditors have invoiced the Group audit fees of Euros 159 thousand (Euros 148 thousand in 2015).

VIDRALA, S.A. AND SUBSIDIARIES

Details of Other Reserves and Retained Earnings and Movement
for the years ended
31 December 2015 and 2014

(Expressed in thousands of Euros)

(Free translation from the original in Spanish. In the event of discrepancy,
the Spanish-language version prevails)

	Revaluation reserves	Legal reserve	Voluntary reserves	Reserves in fully consolidated companies	Profit for the year	Total
At 31 December 2014	-	5,234	216,623	118,350	51,607	391,814
Share capital increase	-	-	-	-	-	-
Share capital decrease	-	-	-	-	-	-
Distribution of 2014 profit						
Reserves	-	-	39,809	(4,427)	(35,382)	-
Dividends	-	-	-	-	(16,225)	(16,225)
Own shares sold	-	-	497	-	-	497
Other movements	-	-	68	-	-	68
Profit for 2015	-	-	-	-	60,860	60,860
At 31 December 2015	-	5,234	256,997	113,923	60,860	437,014
Distribution of 2015 profit						
Reserves	-	-	19,127	23,880	(43,007)	-
Dividends	-	-	-	-	(17,853)	(17,853)
Own shares sold	-	-	281	-	-	281
Revaluation of property, plant and equipment	2,311	-	-	-	-	2,311
Profit for 2016	-	-	-	-	67,671	67,671
At 31 December 2016	2,311	5,234	276,405	137,803	67,671	489,424

This appendix forms an integral part of note 13 to the consolidated annual accounts, in conjunction with which it should be read.

VIDRALA, S.A.
2016 Directors' Report

Relevant Indicators

	Year <u>2016</u>	Year <u>2015</u>	Variation <u>%</u>	Variation at constant <u>exchange rate %</u>
Sales (millions of Euros)	773.1	802.6	-3.7%	+1.6%
EBITDA (millions of Euros)	170.7	161.3	+5.8%	+11.2%
Earnings per share (Euros/share)	2.73	2.46	+11.0%	
Net debt (millions of Euros)	322.3	404.3	-20.3%	

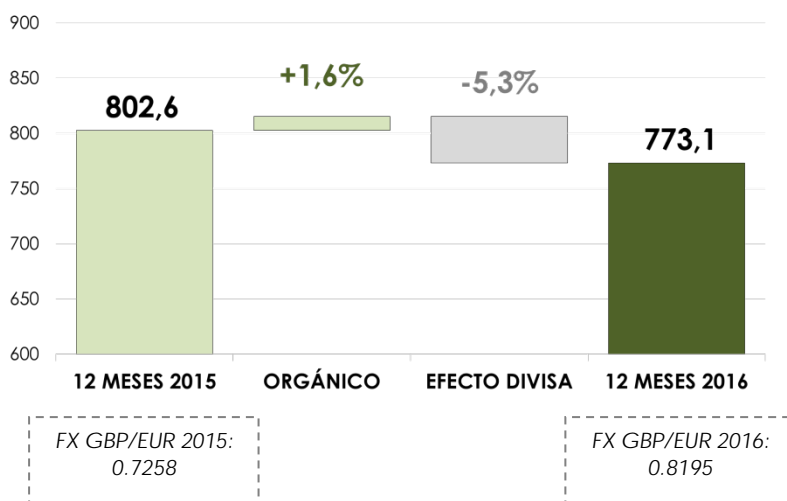
- ✓ Sales in 2016 amounted to Euros 773.1 million, an organic increase of 1.6% on the prior year, but down -3.7% in reported terms if the exchange rate effect is included.
- ✓ Gross operating profit, EBITDA, totalled Euros 170.7 million, equivalent to a sales margin of 22.1%.
- ✓ Earnings per share for the year were 11.0% higher than the prior year.
- ✓ Debt during the year fell by 20.3% to Euros 322.3 million, equivalent to 1.9 times EBITDA.

Sales

Vidrala sales in 2016 amounted to Euros 773.1 million, a drop of 3.7% on the prior year. At a constant exchange rate, sales witnessed organic growth of 1.6%.

SALES YEAR-ON-YEAR

In millions of Euros



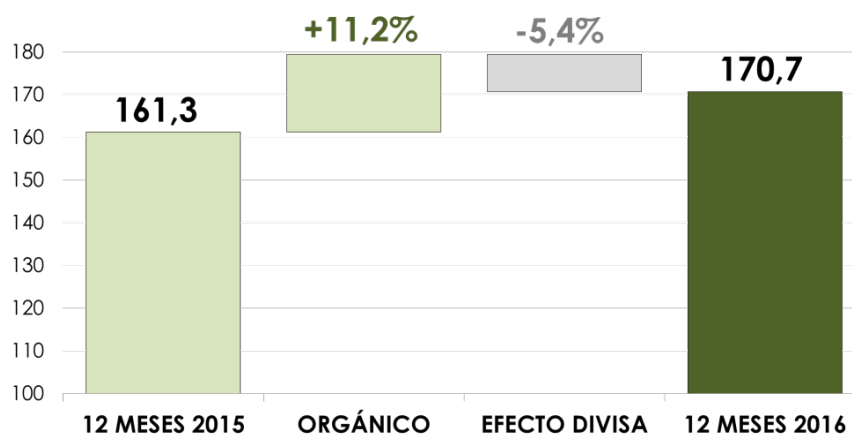
Operating activity

Gross operating profit, EBITDA, for the year amounted to Euros 170.7 million. This represents a reported increase of 5.9% on the prior year in organic terms, and 11.2% at a constant exchange rate.

EBITDA represents a sales margin of 22.1%.

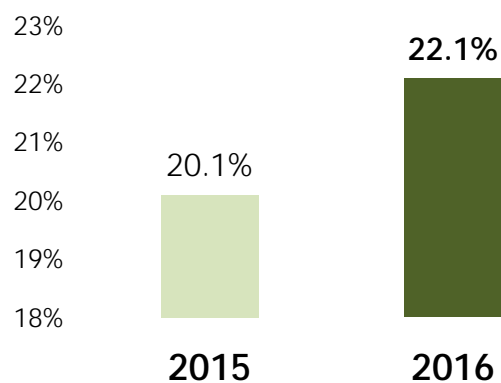
EBITDA YEAR-ON-YEAR

In millions of Euros



OPERATING MARGINS EBITDA ANNUAL TREND

As a percentage of sales



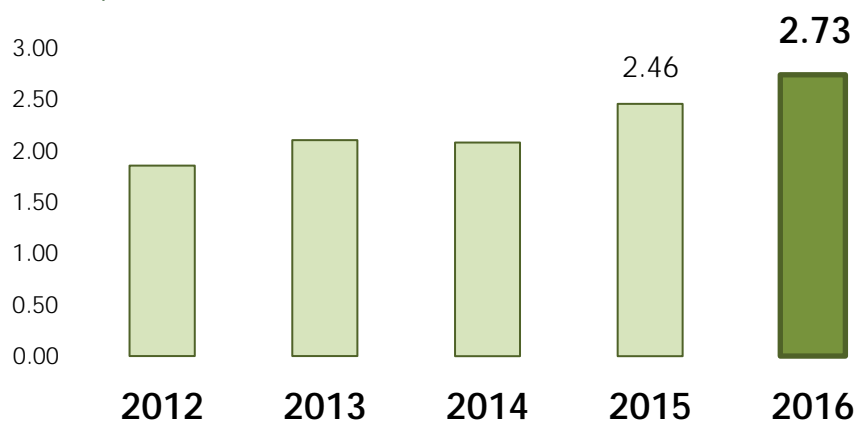
Profit and balance sheet

Net profit for 2016 amounted to Euros 67.7 million, after recognising an annual finance cost equivalent to 1.1% of sales and income tax of 19.7%.

Earnings per share in 2016 amounted to Euros 2.73/share, a rise of 11.0% on the prior year.

EARNINGS PER SHARE SINCE 2012

In Euros per share

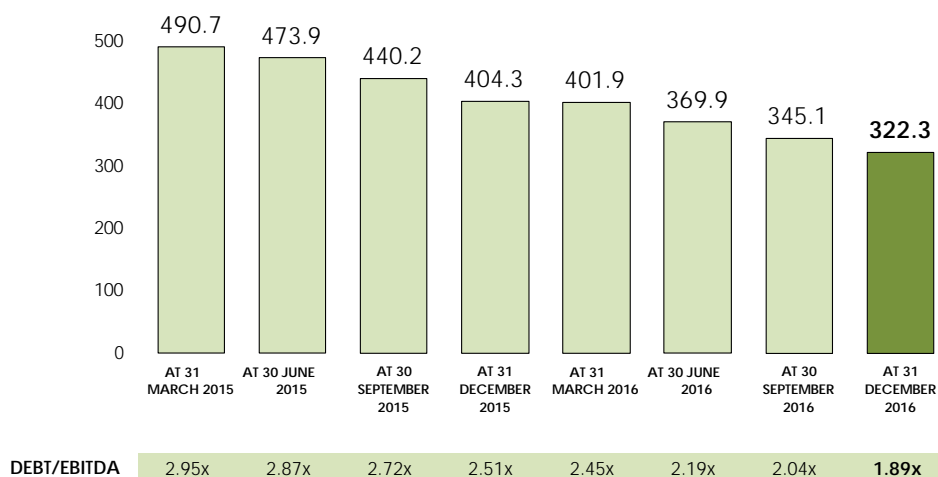


At balance sheet level, debt at 31 December 2016 stood at Euros 322.3 million, having been reduced by 20.3% during the year. This represents a leverage ratio equivalent to 1.9 times EBITDA for the period.

The decline in debt during 2016 is due to the generation of accumulated free cash flow of Euros 102.6 million.

DEBT QUARTERLY TREND

In millions of Euros since 2015



RELEVANT MANAGEMENT INDICATORS

Millions of Euros (except operating margin in %)	2016	2015
SALES	773.1	802.6
GROSS OPERATING PROFIT (EBITDA)	170.7	161.3
OPERATING MARGIN EBITDA (percentage)	22.1%	20.1%
NET OPERATING PROFIT (EBIT)	93.0	86.3
PROFIT BEFORE TAX	84.2	75.6
NET PROFIT	67.7	60.9
FREE CASH FLOW	102.6	88.2
NET DEBT	322.3	404.3
DEBT / EBITDA (multiple)	1.9	2.5

Conclusions and outlook

Profit for 2016 is a reflection of how the business has developed in line with long-term strategic guidelines. Over the past year, Vidrala has evolved and consolidated itself as a diversified, multinational company; a leading supplier in the packaging industry with a firm commitment to fostering trade relations with our customers, our *raison d'être*.

As regards outlook, demand for glass packaging in the main European markets remains stable, with a general tendency towards growth. This is a reflection of the economic environment, with changing consumption patterns of food and drink products and the sustained preference of packagers and consumers for glass, a tried and tested packaging material.

Against this backdrop, sales stability for 2017 will depend, in part, on the extent to which economic growth expectations in the different areas of activity are met. At operating level, Vidrala will take steps aimed at guaranteeing customer service levels, progressing in industrial efficiency, developing cost structure competitiveness and, as a result, improving operating margins.

In any event, long-term priorities will remain firmly focused on optimising the three key elements of customer service, cost competitiveness and sustained cash flow generation as the cornerstones for creating value.

Shareholder remuneration policy

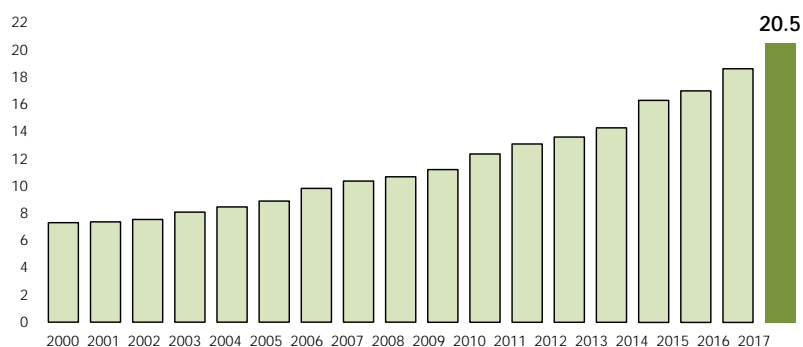
Vidrala's shareholder remuneration policy is based on maintaining dividends in the long term as the principal means of distributing profits and securing the loyalty of its shareholders. Cash payments are generally supplemented by premiums for attending general shareholders' meetings.

In line with this policy, in 2016 the Group distributed dividends of 72 euro cents per share. This represents an increase of 10% on the prior year. Additionally, 3 euro cents per share was offered as a premium to attend the general meeting of shareholders, thus bringing the total effective dividend to 75 euro cents per share.

As regards payments for 2017, Vidrala has proposed a profit distribution representing an annual dividend increase of 11.3%. The first interim dividend of 58.06 euro cents per share was paid on 14 February 2017, a 10% increase on the prior year. An increase of 15% on the prior year has been proposed for the second interim dividend, bringing the dividend to 22.10 euro cents per share, payable on 14 July 2017. Additionally, 3 cents per share will be offered as a premium for attending the general meeting of shareholders. The effective accumulated dividend for 2017 will thus total 83.16 euro cents per share.

CASH REMUNERATION DIVIDENDS AND PREMIUMS TO THE SHAREHOLDER

Millions of Euros. Since 2000

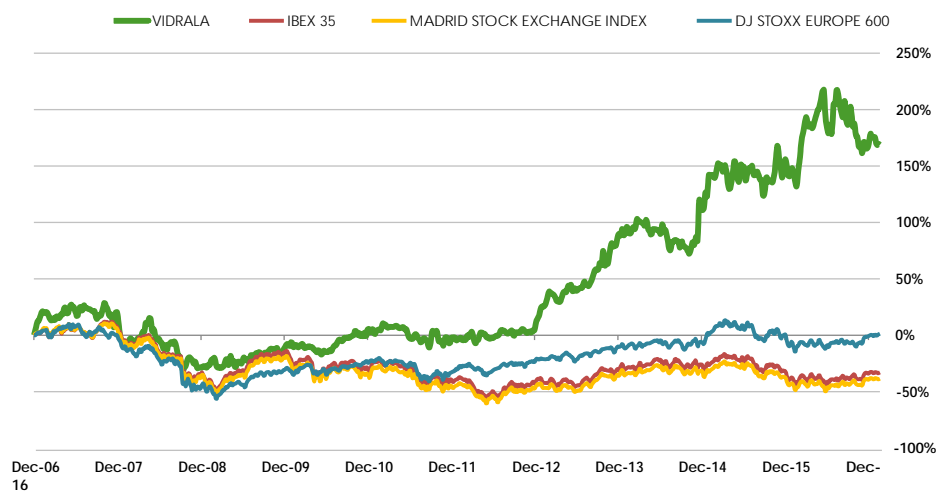


Shares

Vidrala's share price at the end of 2016 was Euros 49.00, an annual increase of 5.3%, excluding dividends. This is equivalent to a market capitalisation of Euros 1,125 million.

5.3 million shares were traded on the stock exchange in 2016, which is 23% up on the prior year and equivalent to an accumulated total of Euros 243 million.

Share price. Compared in percentage terms. Since 2007



Business risks

Risk management at Vidrala involves procedures drawn up by management, overseen by the directors and implemented in the daily running of the organisation.

Operational risk

The Vidrala Group's manufacturing and sales activity, carried out through eight industrial centres, is continuous, intensive and subject to inherent risks linked to routine operations. In 2016, work continued on the identification, evaluation and monitoring of business risks defined as operational. The aim is to identify potential risks, through continuous review, gain a perspective on their impact and probability of occurrence and, principally, to link each area of operations and each business process to adequate control and monitoring systems in order to minimise their potential adverse effects.

Potential operating risks include the following:

i. Environmental risks

The Vidrala Group declares itself firmly committed to protecting the environment. With this objective in mind, Vidrala implements specific action plans in relation to emissions in the atmosphere, dumping, waste, the consumption of raw materials, energy, water and noise.

Glass manufacturing is an inherently energy-intensive process as melting furnaces are in operation 24 hours a day, 365 days a year. Given the industrial nature of the process, one of management's objectives is to reduce the associated environmental impact. In order to achieve this, specific investments are made to upgrade factory facilities and adapt them to the most efficient technological systems for reducing environmental impacts. The efforts geared towards energy efficiency have a global effect on the business, reducing consumption, cutting costs and minimising the impact on the environment. Additionally, operating priorities are focused on intensifying the growing use of recycled products as the main raw material for manufacturing glass, the effect of which is twofold as it not only avoids the consumption of natural raw materials, but also contributes to reducing fossil fuel consumption and the resulting pollution.

One of the Group's strategic guidelines is the implementation of environmental management systems. In line with this commitment, all the Group's production facilities have ISO 14001:2004 certification, demonstrating that Vidrala operates under a global, externally verified and recognised environmental management system. Furthermore, in keeping with its undertaking to continuous improvement, the implementation and certification of new environmental standards has begun, such as ISO 14064:2012, related to the voluntary declaration of CO₂ emissions, or the ISO 50001:2011 energy management system standard, both of which, CO₂ emissions and energy, are of clear environmental significance in our industrial process.

In addition, Vidrala has a specific commitment to invest in minimising the potential polluting effect of its facilities. Of particular relevance during 2016 in this regard was the conclusion of a major project to install special atmospheric emissions purification systems, called electrostatic precipitators or electrofilters, in all production centres. These installations, which have cost the Group more than Euros 20 million over the last eight years, are aimed exclusively at reducing emissions of particulate pollutants, and are recognised under European legislation as the best currently available technology in this regard. Electrofilters work by attracting and retaining articles generated during the melting process through electrical fields, and reduce typical melting furnace emissions by more than 90%.

As proof of our environmental commitment, Vidrala's advancement towards environmental efficiency is documented in detail in its annual sustainability report published on the Company's website.

ii. Occupational health and safety

Vidrala's daily activity is carried out by some 3,200 employees, the majority of whom work in an industrial or manufacturing environment.

Consequently, the Vidrala Group remains committed to establishing the soundest occupational health and safety measures. This commitment is endorsed by the gradual implementation of occupational health and safety management systems based on OSHAS 18001:2007, which are certified by independent entities accrediting the existence of an internationally recognised management framework.

With a specific view to preventing labour-related accidents, and more importantly, to improving health in the workplace, Vidrala implements specific and systematic ongoing staff training and awareness plans. The sustainability report, attached to this report, details the progress of occupational health and safety management indicators. These plans are developed and distributed among all agents involved in the organisation, allowing health and safety trends to be objectively measured and documented, and enabling the actual effectiveness of the processes and controls implemented to be observed, and whether additional corrective measures are needed.

iii. Supply chain risk

Production-intensive, continuous-service industries such as Vidrala's can be vulnerable to risks of distortion in the supply chain.

As regards supply risk affecting key products, materials, installations or technologies for the production process, management initiatives include the continual and specialised search for supply sources and strengthening ties with suppliers, diversifying and forging long-term relationships, establishing ongoing audit and standardisation processes and developing supply alternatives in all relevant areas.

Steps taken to address customer service and product quality risks include the development of a specific departmental area separate from the rest of the organisational areas dedicated exclusively to quality. There is a specific investment project nearing completion that aims to guarantee product quality targets and optimise product quality control through the implementation of state of the art technology across all the Group's facilities.

Concerning inventory risk, the Group systematically carries out a specific and periodic controls to ensure the quality of finished products in the warehouse, and optimise ageing and rotation so that both the volume and value of stocks are balanced to sales forecasts. These controls have resulted in the implementation of automated stock monitoring processes and the subsequent application of specific adaptation, physical and valuation measures, which in 2016 are giving rise to inventory impairment adjustments in the income statement.

Financial risk

Global uncertainty in the financial markets and the growing scale of Vidrala's operations expose activities to potentially destabilising elements of an external nature. These financial risks require the implementation of specific control mechanisms.

Managing Vidrala's financial risks focuses on the identification, analysis and monitoring of market fluctuations in items that could affect the business's profits. This involves defining systematic measurement, control and monitoring processes to minimise any potential adverse effects and structurally reduce the volatility of results. To hedge certain risks, Vidrala employs, or is in a position to employ, derivative financial instruments the volume and characteristics of which are described in the annual report.

The most relevant financial risks are as follows:

i. Currency risk

Vidrala operates at international level and is therefore exposed to currency risk on transactions in currencies other than the euro.

Currency risk affecting the Group's present structure mainly stems from the exposure inherent in the global expansion of the Group after the incorporation of Encirc Ltd. in 2015, with activities in the UK and Ireland. Approximately 80% of operating results generated by this division over the past year were in pounds sterling, and the remainder directly in euros.

In order to quantify the sensitivity to the currency at consolidated Group level, as a result of the above, approximately 30% of EBITDA is generated in pounds sterling. Consequently, reporting this in euros is subject to translation risks that may arise from fluctuations in sterling against the euro.

There is also a risk when converting sterling cash generated in the UK to euros, in that the depreciation of sterling could reduce the equivalent value in euros, thus reducing the amount of cash generated by the business.

To quantify the sensitivity to this risk, based on 2016 data, had sterling depreciated by an average of 5% during year, and the remaining variables remained constant, and assuming there were no instruments to hedge this risk, the Group's consolidated profit would have varied by approximately 2.8% and annual cash flow would have fallen by approximately 1.7%.

To control currency risk, Vidrala uses derivative instruments, principally forward sale contracts or currency put options. To manage the risks described, at the 2016 reporting date Vidrala had sterling put options expiring in 2017, for an accumulated equivalent of Euros 23 million. This is equivalent to approximately 65% of the cash generated in this currency during 2016.

ii. Interest rate risk

Interest rate risk affects the cost of borrowings used to finance the Group's operations. Borrowings contracted at variable interest rates expose Vidrala to the risk of interest rate fluctuations, which in turn affects forecast cash flows.

The Group's financing policy is to focus its borrowings on variable rate instruments. Vidrala manages interest rate risks in cash flows through interest rate swaps or caps. These instruments convert variable-rate borrowings to fixed-rate in the case of swaps, or limit the cost of variable interest rates in the case of caps. Generally the Vidrala Group obtains long-term variable rate borrowings and swaps them for fixed interest rates. This gives better rates than had the financing been obtained directly with fixed interest rates. Through interest rate swaps the Vidrala Group undertakes to periodically exchange the difference between fixed and variable interest with other financial entities. The difference is calculated based on the contracted notional amount. Under interest rate caps

Vidrala has the right, and the counterparty the obligation, to settle the difference between the variable interest rate and the stipulated rate if this is positive. The effectiveness of these instruments as regards fixing the interest rate of contracted financing is assessed and documented using accepted methodologies under applicable accounting legislation.

On account of this risk control policy, at the 2016 reporting date Vidrala has interest rate swaps for an accumulated equivalent of Euros 405 million, which start and expire progressively until 2022, of which Euros 305 million are in force at the reporting date. As a result, the total debt interest cost to be assumed by the Group during 2017 is hedged against fluctuations in market interest rates.

iii. Credit risk

The Vidrala Group has specific policies to mitigate the credit risk of receivables. The procedure begins with developing systemised sales authorisation processes for customers with adequate credit records and solvency in order to minimise the risk of default. This control process involves ongoing solvency analysis, setting specific, assumable risk limits for each customer, analysing variables such as specific credit metrics, the segment or geographical area in which they operate and preparing individual classifications of ratings typical of evolved credit control systems. In summary, the procedure is done through the creation and maintenance of an internal customer credit rating system.

Furthermore, control of collection risk is intensified with a second level of control involving credit insurance policies with external insurance entities. The aim of these credit insurance policies is to cover the economic impact of eventual situations involving significant amounts where the internal system is ineffective in predicting a risk of default.

In order to demonstrate the collection risk system implemented, Vidrala has subjected the quality of its processes to official external certification. Obtaining this certification, and the resolve to periodically renew it, will guarantee the validity, effectiveness and efficiency of the system in place, and will require formal audits, dynamic monitoring and ongoing improvements.

As a result of the control procedures described, the actual impact of bad trade debts during 2016 was limited to 0.01 % of turnover

Other credit risks: financing, derivative and cash transactions are only carried out with financial institutions with high credit ratings.

iv. Liquidity risk

Vidrala's liquidity risk basically stems from the maturing of debt obligations, transactions with derivative instruments and payment commitments with other trade creditors. Vidrala's policy is to continually monitor and ensure that sufficient resources are available to meet these obligations, maintain internal control processes through follow-ups of budgets and deviations, and implement any necessary contingency plans.

In order to accomplish these objectives, Vidrala prudently manages its liquidity risk by adapting maturities to the maturity of assets to be financed, diversifying the sources of financing used and maintaining the availability of immediate financing.

At 31 December 2016 the Vidrala Group had Euros 118.4 million in immediately available, external undrawn credit, representing 37% of total debt.

v. Debt and solvency

At 31 December 2016, the Vidrala Group had consolidated net financial debt of Euros 322.3 million, having reduced indebtedness by Euros 82 million, or 20.3%, during the year. The financial solvency indicators at the reporting date reflect a debt equivalent to 1.9 times accumulated EBITDA for the last twelve months, representing a financial deleveraging compared to the ratio of 2.5 at the prior year end.

The core of the financing structure is a long-term syndicated loan signed on 13 March 2015 with a consortium of nine financial institutions, for an original amount of Euros 465 million. After a second novation of the loan terms was signed in November 2016, the applicable interest rate on the loan in 2017 will be a variable rate pegged to Euribor plus a spread of 1%, reviewed on an annual basis by tranche based on the evolution of the net debt/consolidated EBITDA ratio. The due date of the loan has been extended to 13 September 2022, and is gradually repayable from 13 March 2019. Consequently, in 2017 the loan will be in a grace period, with no obligation to repay the principal.

This loan has certain covenants attached, which are typical in these types of contract. At the reporting date, these commitments have been fully complied with, as reflected by the results of the following indicators:

Net financial debt / consolidated EBITDA: 1.9x

Consolidated EBITDA / Consolidated net finance cost: 17.8x

vi. Price risk in energy purchases

Energy consumption, principally natural gas and electricity, represents a significant source of operating costs inherent in Vidrala's glass production and manufacturing activity.

Fluctuations in the variables that determine their prices, represented in the natural volatility of the global energy commodities markets, has a bearing on the profitability of the business. In order to manage the impact of this risk, the Group employs specific control processes to mitigate potential unexpected effects on operating margins that would arise in the event of inflationary tendencies in the market. These measures involve implementing adapted price-setting formulas, continuous monitoring of market variables through dedicated management and control departments and risk monitoring through price hedging strategies, including the contracting of tariffs at fixed prices and the use of derivative hedging instruments.

As a result of this risk control policy, at the 2016 reporting date Vidrala has hedging derivatives on energy commodities for a nominal equivalent of Euros 51.2 million.

- vii. Other risks:
Result of the Brexit referendum

Vidrala has strategic business interests in the UK and Ireland through its Encirc Limited division, acquired at the beginning of 2015. Encirc is a manufacturer of glass containers aimed at the domestic food and drinks market in Ireland and the UK, where it operates two plants. It offers a complete range of services, from the manufacture of glass containers to state of the art packaging processes and logistics services. Of the profits obtained by this division over the past year, approximately 80% of operating results are generated in sterling, and the remainder directly in euros. As a whole, Encirc is eminently domestic, producing glass containers in the UK for sale throughout the British Isles, including the Republic of Ireland, and the volume of exports outside these regions is immaterial.

On 23 June 2016, the UK voted in a referendum on whether to remain in the European Union, resulting in the now famous Brexit. As a result, a political process has begun to negotiate the terms and conditions of the referendum whose implications are still uncertain.

One instant effect was the devaluation of sterling, which at the reporting date had depreciated by approximately 11% against the euro compared to pre-referendum levels. For the purposes of quantifying the sensitivity of the business to fluctuations in sterling, as in the section on the quantification of currency risks, if sterling had depreciated by an average of 5% during the year, with the rest of the variables remaining constant, and not considering hedging instruments, the Group's annual consolidated profit would have varied by approximately 2.8% and annual cash flow would have fallen by approximately 1.7%.

In any event, the structural foundations of the demand for glass packaging in the UK remain stable, backed by the region's level of socio-demographic development, the progressive lean towards increasing consumption of quality products and the natural limited variability of demand for food and drink products. Encirc optimises these market foundations thanks to a commercial position endorsed by relationships fostered with world class customers, market share stability, competitiveness backed by modern industrial facilities and the added value they give to packaging services, whose unique competitive advantages for owners interested in exporting bulk materials to the growing demand in the UK have been boosted.