

STRATEGY

In 2014, we continued to forge ahead with our strategy of expanding our customer and product base with the objective of globalising and internationalising our business. It is particularly encouraging that our product offensive is having a lasting effect and we have succeeded in gaining many new customers in all regions. As well as continuing to focus on the Asian market, we also aim to consolidate our network of sites to enhance our efficiency and enable the DEUTZ Group to continue achieving profitable growth.

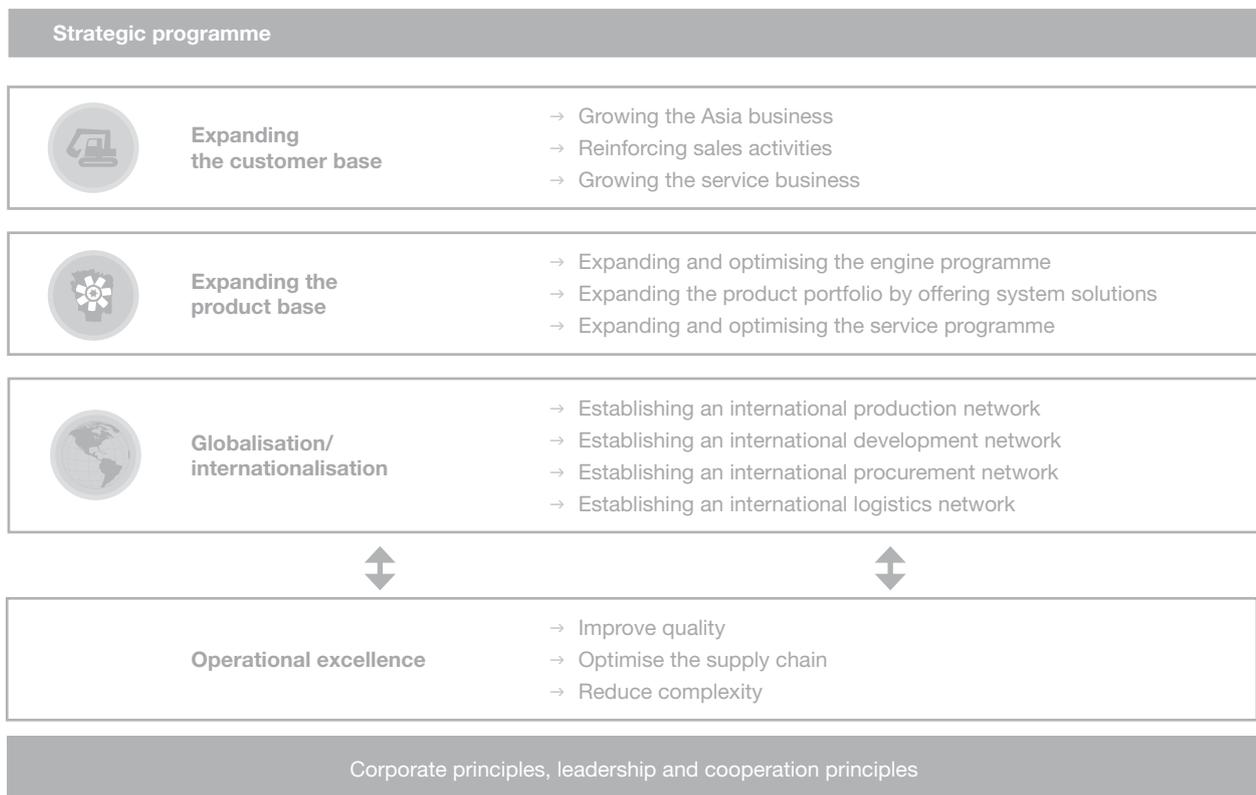
Our growth strategy is based on three pillars:

→ The first is the **expansion of our customer base** while achieving profitable growth. Our aim is to increase business in all regions with new and existing customers. The fact that we managed to achieve this once more in 2014 shows that the product offensive we launched a few years ago is taking effect. We have been marketing our new generation of engines very successfully worldwide. This includes highlighting the numerous advantages of these engines, such as very compact installed dimensions, intelligent exhaust aftertreatment designs and lower lifecycle costs than their predecessors. In Asia, we were particularly pleased to have acquired promising new customers in the form of Japan's Hitachi Construction Machinery Co., Ltd.,

one of the world's biggest producers of construction equipment, and Tong Yang Moolsan (TYM), a South Korean tractor manufacturer. In China, where market conditions remained as challenging as in 2013, our joint venture DEUTZ (Dalian) Engine Co., Ltd. continued to grow and gain market share. This year, we are expecting our joint venture in the automotive sector to benefit from the nationwide introduction of the China IV emissions standard (equivalent to Euro 4) on 1 January 2015. In the reporting year, we opened a new sales office in Shanghai. Sales staff as well as application engineers and service engineers will work there in order to further expand customer support. This office is in addition to our sales and service company in Beijing.

Strategic programme up to 2020

We supply the most successful engine systems in the world



In terms of application segments, our main focus remains on Mobile Machinery and Agricultural Machinery, but we are also active in the market for Stationary Equipment and niche applications. Our automotive business is increasingly shifting to Asia, where we occupy a very strong position in the market by virtue of our DEUTZ Dalian joint venture.

In the service business, we also aim to continue growing sustainably and expanding our market share in terms of the total number of engines in existence. As well as the active management of dealers and ongoing product training for our dealer network because of the growing complexity of our products, we may also invest in our own service support centres in selected locations and increase our use of the internet as a sales channel.

The sales and marketing function stepped up and improved its market analysis in the year under review. This has provided us with excellent information about potential in the market which will enable us to improve the direction and focus of other sales activities.

→ The second pillar is the **expansion of our product base** using products at the leading edge of technology. Due to the introduction of the EU Stage IV/US Tier 4 exhaust emissions standards, we have fundamentally overhauled our range of engines and actively followed the downsizing trend. We have streamlined our engine platforms without cutting back on the 25 to 520 kW power output range they cover. This platform strategy and the possibilities offered by electronic management will considerably reduce the variety of components. In 2014, we completed the introduction of engines that meet the current most stringent emissions standard. In 2015, we will be using our 'Stage V ready' campaign to actively advertise the fact that our TCD engines in the 2.9 to 7.8 litre cubic capacity range already meet the more stringent EU limits announced for 2019¹⁾. In the future, we will be adding gas engines to our product range.

System solutions complete our product portfolio. In order to meet the latest emissions legislation, engines now have to include exhaust aftertreatment systems. Developing, testing and certifying these engine systems is our responsibility. We will continue to work on developing solutions to improve energy efficiency throughout the system. In addition, we intend to expand our application expertise – an area in which our competitors already acknowledge us as leaders – both at our R&D centre in Cologne and in the regions. Going forward, we will also be actively marketing customised engineering services. The range of services offered will include the optimum system integration of the hardware components and software functions required for each machine, such as a customer-specific range of data sets that goes beyond what is supplied as standard.

A profitable service business makes us less exposed to fluctuations in the economic cycle. We plan to exploit the opportunities presented by the greater complexity of engines that meet new emissions standards and to expand our service business accordingly. For example, we intend to offer additional repair options and to create a wider range of spare parts and add-on components.

→ The third pillar is the **globalisation and internationalisation** of the DEUTZ Group, because the main market focuses are shifting and the trend is increasingly towards basing assembly nearer to the customer. Against this background, we want to create structures in the three major economic areas of Europe, America and Asia, which in addition to their sales, marketing and service activities, will also encompass local assembly, purchasing, logistics and application development activities. These activities will need to be closely interlinked and centrally coordinated.

In April 2014, we decided to carry out a comprehensive optimisation of our network of sites in Germany in order to increase efficiency. We will be consolidating our facilities in Cologne by moving out of our Cologne-Deutz site within two years and building a new shaft centre for the production of camshafts and crankshafts at our largest site in Cologne-Porz. Our exchange engine plant in Übersee on Lake Chiemsee will be closed and integrated into the plant in Ulm in two stages in 2015 and 2017.

¹⁾ EU Commission's proposal for EU Stage V published on 25 September 2014.

We continue to have every faith in the long-term potential of the Chinese market. Nevertheless, China has been a very challenging market for some time, particularly as growth forecasts have been revised down and there is considerable capacity in the engine production sector. After the balance sheet date, we therefore decided to consolidate our Chinese operations and sites and to utilise the capacity available there. Our intention is to focus our production operations in China on our established and successful DEUTZ Dalian joint venture, which has plenty of capacity.

In February 2015, together with our partner AB Volvo, we took a joint decision to wind up our DEUTZ Engine (China) Co., Ltd. joint venture in Linyi, China. We had already reported in November 2014 that the joint venture was undergoing a strategic reassessment by both parties, and the joint venture has not made any substantial investments to date. Going forward, we aim to continue satisfying local demand from our partners and other target customers using local Chinese production operations.

OPERATIONAL EXCELLENCE

In the year under review, we added the **'operational excellence'** efficiency and quality programme to the three pillars of our growth strategy. It supplements the various continuous improvement processes in the DEUTZ Group and forms the basis for achieving profitable growth.

The optimisation of our sites in Germany will significantly enhance our efficiency and create long-lasting added value. Given the challenging market situation, the streamlining of our sites in China is primarily market-driven, but it is also an efficiency programme.

Operational excellence also focuses on continuously improving quality, managing the supply chain and reducing complexity.

GLOBAL MEGATRENDS DRIVE ENGINE GROWTH

Demographic change, increasing urbanisation and ongoing globalisation are the megatrends that shape our business. They are causing global demand to rise continually, which also impacts on demand for agricultural machinery, infrastructure investment and transport. These global megatrends are therefore underpinning growth in the global engine market.

There are only limited natural resources to meet this demand, however. Hence the imposition of increasing numbers of environmental and climate change regulations in practically every industrialised country and emerging market. Consequently, emissions legislation has been the major technology driver in the diesel engine market in recent years. We are, of course, delighted to take up the emissions legislation challenge. As a leading technology company, we regard this legislation as an opportunity. Emissions legislation in the emerging economies is generally at least one step behind.

To this extent, the structural growth drivers at DEUTZ are the engine systems that meet the new emissions standard, which are of considerably higher value and more complex than their respective predecessors. Our investment in the new product portfolio is also delivering results. As a result, we see significant growth potential for the DEUTZ Group over the coming years, despite continuing to face a highly cyclical market environment, and the fact that our European customers will be drawing to a significant extent during 2015 on engines which they purchased ahead of the introduction of the tighter emissions standard in October 2014.