

## OVERVIEW OF 2014

**Global growth at previous year's level** Despite a good start to the year, the global economic growth rate of 3.3 per cent in 2014 again merely matched that of 2013. Germany's growth rate of 1.5 per cent was the best among the larger countries in the eurozone once more, while the US economy grew strongly at a rate of 2.4 per cent. By contrast, growth in China, another particularly important market for DEUTZ, slowed to 7.4 per cent. Trends in DEUTZ's customer industries varied from region to region and sector to sector.

**Year-on-year rise in revenue** In 2014, we particularly benefited from customers buying more engines than they needed in anticipation of the change to the emissions standard for engines under 130kW in the EU that came into effect on 1 October 2014. As a result, our revenue was up by 5.3 per cent to €1,530.2 million. Unit sales rose at an even faster rate than revenue, increasing by 6.7 per cent to 196,403 engines sold. However, operating profit (EBIT before one-off items), which had declined to €31.7 million, was significantly affected by exceptional items.

**DEUTZ celebrates its 150th anniversary** In 2014, DEUTZ AG celebrated 150 years of existence as a company. N.A. Otto & Compagnie, which would go on to become DEUTZ AG, was founded by Nicolaus August Otto and Eugen Langen in 1864. As the world's first engine factory, it ushered in an era of motorisation that endures to this day. As well as other events, we celebrated this special anniversary with our friends and partners at an official celebration in Koelnmesse exhibition centre in Cologne on 9 May 2014.

**Decision to optimise sites in Germany** Our objective is long-term efficiency enhancement. With this in mind, we took the decision in 2014 to carry out a comprehensive optimisation of our network of sites. Firstly, this includes the consolidation of our facilities in Cologne where we will move out of our Cologne-Deutz site within two years and build a new shaft centre for the production of camshafts and crankshafts at our largest site in Cologne-Porz. This will provide long-term security for at least 140 permanent positions. Secondly, we will close our exchange engine plant in Übersee on Lake Chiemsee and integrate it into the plant in Ulm. We have also initiated further measures as part of our 'operational excellence' efficiency and quality programme.

**New products also attract new customers** Last year, we completed the introduction of engines that comply with the latest EU Stage IV/US EPA Tier 4<sup>1)</sup> emissions standard. The engines feature an extremely compact design, exhaust gas aftertreatment systems tailored to customers' individual needs and low lifecycle costs, showing that in terms of technology, we remain at the leading edge of the market. It was additionally encouraging that our new products not only impressed our existing customers, but also attracted new customers for us across all regions and sectors.

## FUNDAMENTAL FEATURES OF THE GROUP

### BUSINESS SEGMENTS AND PRODUCT RANGE

For over 150 years, DEUTZ has been supplying reliable drive systems for mobile and standalone static applications – as an independent manufacturer of compact diesel engines in the 25kW to 520kW power range for both on and off-road use. We develop, design, produce and sell diesel engines that are cooled by water, oil or air. The operating activities of the DEUTZ Group are divided between the DEUTZ Compact Engines segment and the DEUTZ Customised Solutions segment: the DEUTZ Compact Engines segment comprises liquid-cooled engines with capacities of up to eight litres, while the DEUTZ Customised Solutions segment specialises in air-cooled engines and large liquid-cooled engines with capacities of more than eight litres. Operating under the name DEUTZ Xchange, the DEUTZ Customised Solutions segment also supplies reconditioned parts and engines as the main element of our service business.

We also offer our customers advice and support on operating the machinery. Our services are closely aligned with each of our customers' individual needs. We actively assist customers with the repair, maintenance and servicing of their vehicles and machines fitted with DEUTZ engines. The global DEUTZ service network, which comprises subsidiaries, service centres and authorised agents, guarantees a reliable and rapid supply of spare parts.

### LEGAL STRUCTURE AND PRODUCTION SITES

DEUTZ maintains a comprehensive international presence in a globalised market: with thirteen sales companies, seven sales offices and over 800 sales and service partners in more than 130 countries, we can offer our customers service and support virtually anywhere with very short response times. DEUTZ AG is the executive and operating parent company in the DEUTZ Group; it is headquartered in Cologne, Germany, and has various domestic and foreign subsidiaries. The subsidiaries include a production facility in Spain and several companies that perform sales and service functions.

In addition to DEUTZ AG, six German companies (31 December 2013: six) and 14 foreign companies (31 December 2013: 14) were included in the consolidated financial statements as at 31 December 2014. A complete list of DEUTZ AG shareholdings as at 31 December 2014 is given in the annex to the notes to the consolidated financial statements on page 117.

<sup>1)</sup> The Tier 4 Interim/Tier 4 final emissions standard is mentioned at various points in the annual report. This refers both to the EPA Tier 4 Interim and EPA Tier 4 standards for diesel engines in the United States and to the 97/68 Stage III B and Stage IV exhaust emissions standards in the European Union, but for the sake of simplicity the latter is not always explicitly mentioned.

DEUTZ AG	
<b>DEUTZ Compact Engines</b>	<b>DEUTZ Customised Solutions</b>
<ul style="list-style-type: none"> <li>Liquid-cooled engines of up to 8 litres cubic capacity</li> </ul>	<ul style="list-style-type: none"> <li>Air-cooled engines</li> <li>Liquid-cooled engines of more than 8 litres cubic capacity</li> </ul>

## MARKET AND COMPETITIVE ENVIRONMENT

DEUTZ manufactures diesel engines for professional applications used in countries with stringent emissions standards, in particular Stages III and IV. These technically sophisticated applications include construction equipment, agricultural machinery, lifting and material-handling equipment, pumps, gensets, medium and heavy-duty trucks and buses. The market for DEUTZ engines is therefore separate from the market segments for diesel engines used in passenger cars and small commercial vehicles up to a permissible gross weight of around 3.5 tonnes. Engines that rely on outdated technology and that are intended for use in applications in countries or application segments with only very low requirements in terms of product quality, emissions and fuel consumption also do not feature in our target market.

The market for technically sophisticated diesel engines divides into what are known as the captive and non-captive areas. The captive area comprises equipment manufacturers who produce their own engines, some of whom are also active as engine suppliers in the market. The non-captive area is made up of equipment manufacturers who for the most part do not produce their own engines and who, therefore, buy in engines from other suppliers. It is in this non-captive market that DEUTZ sells its high-quality engines with outputs between 25kW and 520kW around the globe.

In recent years, we have attained an outstanding position as one of the biggest suppliers in the non-captive market. We face competition from other engine suppliers in western Europe, North America and Asia, but none of these competitors can offer an identical product range to DEUTZ in terms of the power outputs and application segments that they cover.

## Main competitors

Application segments	Applications	Main competitors (in alphabetical order)
<b>Mobile Machinery</b>	Construction equipment Ground support equipment Material handling equipment Mining equipment	Cummins, USA Kubota, Japan Perkins, UK Yanmar, Japan
<b>Agricultural Machinery</b>	Tractors Harvesters	Deere, USA Kubota, Japan Perkins, UK Yanmar, Japan
<b>Stationary Equipment</b>	Gensets Compressors Pumps	Deere, USA Kubota, Japan Perkins, UK Yanmar, Japan
<b>Automotive</b>	Special vehicles Rolling stock Trucks Buses	Cummins, USA Fiat Powertrain, Italy MAN, Germany Mercedes, Germany

## INTERNAL CONTROL SYSTEM

### RESPONSIBLE CORPORATE MANAGEMENT BASED ON TRANSPARENT PERFORMANCE INDICATORS

The DEUTZ Group defines its budget targets and medium-term corporate targets using selected key performance indicators (KPIs). In order to increase profitability and achieve sustained growth, we manage the Group using the following financial performance indicators:

		2014	2013
Revenue growth	(%)	5.3	12.5
EBIT margin before one-off items	(%)	2.1	3.3
Working capital ratio <sup>1)</sup> (average)	(%)	13.3	12.0
ROCE before one-off items <sup>2)</sup>	(%)	3.9	6.0
R&D ratio	(%)	3.5	3.6
Free cash flow <sup>3)</sup>	€ million	52.0	13.8

<sup>1)</sup> Working capital ratio (average): ratio of working capital (inventories plus trade receivables minus trade payables), as an average of the four quarters, to revenue for the preceding twelve months.

<sup>2)</sup> Return on capital employed (ROCE): ratio of EBIT to average capital employed. Capital employed: total assets less cash and cash equivalents, trade payables and other current and non-current liabilities, based on average values from two balance sheet dates.

<sup>3)</sup> Free cash flow: cash flow from operating and investing activities minus net interest expense.

Our internal control system focuses, on the one hand, on revenue growth and the EBIT margin before one-off items, while on the other hand, we manage tied-up capital via the average working capital ratio. In conjunction with working capital and EBIT optimisation, this in turn determines the return on capital employed. In managing its liquidity, DEUTZ focuses on free cash flow as a key performance indicator. Also, as a technology-oriented company, we consider the R&D ratio, which represents the ratio of research and development expenditure (less reimbursements) to revenue, to be a key management variable as part of our internal