2015 COMBINED MANAGEMENT REPORT FOR DEUTZ AG AND THE DEUTZ GROUP

OVERVIEW OF 2015

Revenue lower than in previous year Having made a solid start in the first six months of 2015, our business suffered in the second half of the year due to a slowdown in global economic growth and a strong reluctance to invest on the part of our customers. Moreover, the advance production of engines in the prior year continued to have an impact. As a result, our revenue was down by 18.5 per cent to €1,247.4 million. Unit sales fell by 29.8 per cent to 137,781 engines. However, operating profit (EBIT) remained in positive territory at €4.9 million, underlining the effectiveness of the measures we have taken to improve efficiency.

Consolidation in China In view of lower growth forecasts in China, we decided in 2015 to consolidate our Chinese manufacturing operations. In future, our established DEUTZ Dalian joint venture, which has adequate capacity, will satisfy local demand. As part of this consolidation, we wound up our DEUTZ Engine (China) Co., Ltd. joint venture, sold the WEIFANG WEICHAI-DEUTZ DIESEL ENGINE CO., LTD. joint venture to our previous co-shareholder and initiated the closure of the DEUTZ Engine (Shandong) Co., Ltd. joint venture.

Optimisation of German site network on schedule The decision that we took in 2014 to optimise our network of sites in Germany is being implemented as planned. Firstly, this includes the consolidation of our facilities in Cologne, where we are moving out of our Cologne-Deutz site and, from 2016, will begin producing camshafts and crankshafts in a new shaft centre at our largest site in Cologne-Porz. Secondly, our exchange engine plant in Übersee on Lake Chiemsee will have been integrated into the plant in Ulm by 2017 and will then be closed; assembly and order management have already been moved. We expect these measures to bring about a further long-term increase in our efficiency.

Positive market response to new products Our TCD engines equipped with a diesel particulate filter in the 2.9 to 7.8 litre cubic capacity range already meet EU Stage V, the next European emissions standard, which is expected to come into effect in 2019. This offers many advantages to our customers. The feedback on our products has been very positive. We have also announced that we intend to add gas engines to our product range in future. In addition, we have intensified our existing partnership with the KION Group, entering into an extended long-term cooperation arrangement.

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 13 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 2014: six) and twelve foreign companies (31 December 2014: 14) were included in the consolidated financial statements as at 31 December 2015. A complete list of DEUTZ AG shareholdings as at 31 December 2015 is given in the annex to the notes to the consolidated financial statements on page 123.

DEUTZ AG

DEUTZ Compact Engines	DEUTZ Customised Solutions
• Liquid-cooled engines of up to 8 litres cubic capacity	• Air-cooled engines • Liquid-cooled engines of more than 8 litres cubic capacity

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. Diesel 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 can be divided into the captive segment and the non-captive segment. The captive segment comprises equipment manufacturers who produce their own engines; some of these manufacturers are also active as engine suppliers in the market. The non-captive segment 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-value 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)
Mobile Machinery	Construction equipment Ground support equipment Material handling equipment Mining equipment	Cummins, USA Kubota, Japan Perkins, UK Yanmar, Japan
Agricultural Machinery	Tractors Harvesters	Deere, USA Kubota, Japan Perkins, UK Yanmar, Japan
Stationary Equipment	Gensets Compressors Pumps	Deere, USA Kubota, Japan Perkins, UK Yanmar, Japan
Automotive	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:

		2015	2014
Revenue growth	(%)	–18.5	5.3
EBIT margin before one-off items	(%)	0.4	2.1
Working capital ratio [1] (average)	(%)	17.6	13.3
ROCE before one-off items [2]	(%)	0.6	3.9
R&D ratio	(%)	3.3	3.5
Free cash flow [3]	(€ million)	35.0	52.0

[1] Working capital ratio (average): ratio of working capital (inventories plus trade receivables less trade payables), as an average of the four quarters, to revenue for the preceding twelve months.
[2] 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.
[3] Free cash flow: cash flow from operating and investing activities less 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 performance indicator system. On the basis of these KPIs, the Group's financial flexibility is subject to constant analysis in the form of a comparison between budget and actual so that we can take swift, appropriate action in the event of significant variances. One-off items are defined as material income and expenses that are exceptional and unlikely to recur.

In order to enable us to be proactive and respond promptly, DEUTZ has set up an early warning system based on the performance indicators. A monthly/quarterly reporting process enables the Board of Management to track changes in the performance indicators. This approach ensures that we can respond immediately to the latest business developments. At the same time, we operate a sound system of causal analysis to ensure that we minimise risks and make the most of opportunities. Three times a year we produce an annual forecast for all key performance indicators. In this way, we ensure optimum transparency in our business performance, benefiting both the Group and all stakeholders.

In addition to the financial performance indicators which form part of the management system described above, we also employ a range of other parameters to measure our economic performance. These include, but are not limited to, new orders received, revenue and unit sales on the income side, the working capital as at the reporting date with regard to tied-up capital, and earnings before interest, taxes, depreciation and amortisation (EBITDA). Moreover, the Group net income and the DEUTZ AG statutory income in accordance with the German Commercial Code are significant factors for us as regards dividend payments.

CONTINUOUS OPTIMISATION OF THE CONTROL SYSTEM

Regardless of fluctuations in the economic cycle, one of the DEUTZ Group's overriding aims is the continuous optimisation of its management systems. This essentially involves the annual planning of all specified performance indicators. This planning is based on both internal estimates of future business and benchmark figures from competitors. Each organisational unit prepares detailed plans for its area of responsibility, which are then coordinated with the management strategy. Both the specific unit sales and revenue targets and the customer and product-related targets (EBIT margins) are aligned with the operating units each year, taking groupwide objectives into consideration. This means that they are available at the relevant hierarchical level for use by the operational management.

We specify working capital targets for the individual companies in the DEUTZ Group in order to optimise the capital tied up in the business. These overall figures are then broken down and specific targets for inventories, trade receivables and trade payables are allocated to the relevant individual employees.

We are pursuing long-term growth objectives. In order to secure the financial basis for this, we have made the management of capital expenditure a central element in the management of tied-up capital: clearly specified budget figures set out the framework for the level of capital expenditure and development expenditure; actual requirements are derived from the medium-term planning of unit sales and the resulting requirements in terms of capacity and technologies. Annual budget meetings are held to coordinate individual projects, development expenditure and planned capital expenditure with the groupwide financial planning process and to record the outcomes. An additional detailed review is carried out before projects are actually approved. To this end, we use standard investment appraisal methods (internal rate of return, amortisation period, net present value, the impact on the income statement and cost comparisons). A project with an appropriate budget is only approved if there is a clear positive outcome from this investment appraisal.

BUSINESS PERFORMANCE IN THE DEUTZ GROUP

ECONOMIC ENVIRONMENT

Global economic growth remained weak in 2015 As in previous years, the economy did not live up to expectations in 2015. Forecasts were successively lowered as the year progressed. The reporting year was shaped by various factors, including geopolitical crises, weak growth in emerging markets, lower prices for commodities, oil, gas and agricultural goods, quantitative easing (particularly by the European Central Bank [ECB]), the first interest rate hike carried out by the US Federal Reserve at the end of the year, strong exchange rate movements and waves of migration to Europe. These factors resulted in palpable uncertainty and a reluctance to invest, although European exports received a small boost from the weak euro exchange rate.

The International Monetary Fund (IMF)[1] is expecting worldwide growth of 3.1 per cent for 2015 as a whole, which is below the 2014 level of 3.4 per cent. The eurozone economy expanded by 1.5 per cent in 2015, which is considerably stronger than the 2014 rate of 0.9 per cent. The German economy's growth was on a par with 2014 at 1.5 per cent. Spain's economic performance was very encouraging – despite the country only having emerged from recession in the previous year – with growth of

[1] IMF World Economic Outlook, January 2016.

3.2 per cent. Italy also moved out of recession, expanding by 0.8 per cent. There was also positive news from France, where the economy grew by 1.1 per cent.

As in 2014, the US economy was one of the major drivers of global economic growth. It expanded by 2.5 per cent (2014: 2.4 per cent) thanks, in particular, to favourable conditions in the labour market.

At 6.9 per cent, the pace of growth in the Chinese economy continued to slow. This trend is set to continue in the years ahead. Conditions remained difficult in the truck and construction equipment sector, which is a core market for DEUTZ. The Russian economy slipped into recession due to the crisis and sanctions; the growth engine was still not running smoothly in South America either.

Weakness in DEUTZ's customer industries Demand in our main customer markets fell in 2015. According to DEUTZ's own estimates, demand for construction equipment – excluding the effect of the advance production of engines – was down by around 10 per cent in Europe and was unchanged year on year in North America. In China, however, demand fell by around 44 per cent[1]. According to the VDMA[2], the agricultural machinery sector in Europe contracted by 8 per cent in the year under review. The market for medium and heavy-duty trucks contracted by 29 per cent in China[3].

IMPACT OF ECONOMIC CONDITIONS ON BUSINESS PERFORMANCE

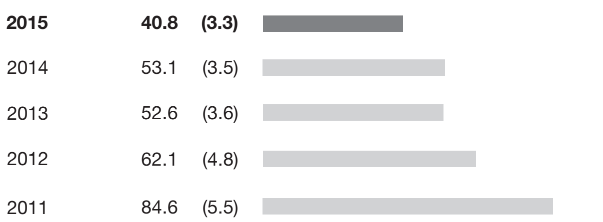
DEUTZ suffering from customers' reluctance to invest Whereas the global economy grew by 3.1 per cent in 2015, DEUTZ's revenue fell by 18.5 per cent and its unit sales by 29.8 per cent. The even greater decrease in unit sales was due to the growing proportion of unit sales accounted for by higher-value engines. Overall, most of our key customer sectors experienced significant negative growth. DEUTZ's performance was therefore similar to that of its customer sectors.

The economy in the eurozone expanded by 1.5 per cent in the year under review. DEUTZ's key customer sectors in this region did poorly, however: volumes in the agricultural machinery sector were down by roughly 8 per cent, for example, and demand for construction equipment declined by around 10 per cent. Furthermore, European customers drew on their inventories of the engines that they had purchased on a large scale in 2014 in anticipation of the new emissions standard. DEUTZ's revenue in our biggest market, EMEA (Europe, Middle East and Africa), went down by 27.6 per cent in 2015; the decrease in unit sales was 38.6 per cent. US economic output grew by a relatively strong 2.5 per cent in 2015, and demand for construction equipment in North America was at the same level as in 2014. Our unit sales in the Americas region fell by 11.0 per cent, but we were able to increase our revenue by 7.3 per cent. Momentum in China, our key international market, continued to slow, with economic growth of 6.9 per cent year on year. In this environment, the markets for construction equipment and medium and heavy-duty trucks declined by approximately 44 per cent and 29 per cent respectively. By contrast, DEUTZ's revenue rose by 18.8 per cent and its unit sales by 14.4 per cent in the Asia-Pacific region. However, the revenue generated by our DEUTZ (Dalian) Engine Co., Ltd. joint venture, which is not included in consolidated revenue, dropped by 5.6 per cent year on year; its unit sales were down by a substantial 29.5 per cent.

RESEARCH AND DEVELOPMENT

Research and development expenditure (after deducting grants)[1]

€ million (R&D ratio in %)



[1] Spending on research and development after deducting grants received from major customers and development partners.

R&D spending scaled back as planned Expenditure on research and development in 2015 amounted to €49.5 million (2014: €68.7 million). After deducting grants received from major customers and development partners, expenditure was €40.8 million (2014: €53.1 million). The R&D ratio (after deducting grants), i.e. the ratio of net development expenditure to consolidated revenue, fell marginally as planned to 3.3 per cent (2014: 3.5 per cent). This decrease in R&D expenditure was largely due to all engines for the latest emissions standards, EU Stage IV/US Tier 4, having being launched in the market in 2014. In the year under review, 31.9 per cent of development expenditure after deducting grants was capitalised (2014: 49.5 per cent).

Spending by the DEUTZ Compact Engines segment after deducting grants came to €38.2 million (2014: €48.1 million) and that of the DEUTZ Customised Solutions segment came to €2.6 million (2014: €5.0 million).

Stage V ready During previous years, we had completely overhauled our engine portfolio for the EU Stage IV/US Tier 4 emissions standards. This has resulted in very compact engines, featuring low lifecycle costs and exhaust aftertreatment designs tailored to customer needs. Our engines in the 2.9 to 7.8 litre cubic capacity range that are equipped with diesel particulate filters already meet the next European emissions standard, EU Stage V, which is expected in 2019[4]. There are currently no plans for a further emissions standard in the USA.

[1] China Construction Machinery Association, January 2016; own estimates.
[2] Konjunkturbulletin of the German Engineering Federation (VDMA), November 2015.
[3] China Automotive Information Net, January 2016.
[4] The EU Commission's Stage V proposals as published on 25 September 2014.

We do not anticipate being faced again with such a complex challenge as that presented by the EU Stage IV/US Tier 4 emissions standards in future; rather, we expect to be able to market these engines well into the next decade. Going forward, developments will be influenced to a lesser extent by emissions legislation and, instead, will be driven by business decisions to a greater degree. We will continue to strive for technologically leading designs and to further improve the performance of our engines without increasing their size in future.

Expansion of the product portfolio We intend to enhance our product range with further developments. One of these is the TCD2.2, a three-cylinder engine that we are developing on the basis of the existing four-cylinder engine with a 2.9 litre capacity. In addition, we will offer smaller engines not only in a diesel variant but also in a liquefied petroleum gas (LPG) variant. The latter is a particularly interesting option for forklift trucks and other material handling applications.

Preliminary development work at a high level Exhaustive research and development will continue to provide the bedrock for DEUTZ's position at the forefront of innovation within the sector. Following the successful completion of work on the latest emissions standard, we can now turn our attention to other matters. The focus will be on electronics and software development as well as the enhancement of our exhaust aftertreatment technology in order to further reduce the space required for its installation.

New technical designs We are constantly developing new, innovative approaches and have recently expanded our activity in the field of alternative fuels. For example, we have developed the prototype for an engine powered by compressed natural gas (CNG), based on the TCD 3.6, and fitted it in a tractor. We carried out this project, which was supported by the German Foundation for the Environment, in cooperation with the University of Rostock and the SAME DEUTZ-FAHR Group. The tractor was showcased at Agritechnica in Hannover in November 2015.

Intellectual property rights safeguard our know-how We protect our know-how from unauthorised outside use by means of patents, patent applications and utility models. In 2015, we submitted 19 new patent applications, seven of which were in Germany. We now hold a total of 153 patents registered in Germany and 262 registered elsewhere.

PROCUREMENT

In 2015, purchasing continued to focus on improving the competitiveness of the engine portfolio by reducing material costs. We took decisive action as part of our defined material group strategies, primarily in relation to the model series in the segment for engines with capacities of up to four litres. Requirements for security of supply and supplier performance were further tightened, too.

Fall in commodity prices The price of cast-iron scrap continued to fall sharply in the year under review. The decrease in aluminium and copper prices was less pronounced. Platinum prices were significantly lower compared with previous years. The price of palladium followed a similar trajectory in 2015, although this element is far less important to DEUTZ than platinum. All average annual values lay below the range we had forecast. Overall, commodity prices have only a limited influence on the procurement prices for parts from suppliers because there is a very high element of value added.

Since the introduction of Tier 4, the proportion of product categories accounted for by EAT components has been rising. Nonetheless, foundry products (particularly cylinder heads and engine blocks), fuel injection equipment (predominantly pumps and valves) and measurement & control devices (for example mechanical and electronic regulators and sensors) make up the bulk of the overall volume of materials purchased.

Last year, we particularly focused on the procurement strategies for fuel injection, ECU, EAT and AGR. The more technology-intensive components have developed rapidly in recent years. Price structures have therefore changed over the past five years, and what were once new market players are becoming established suppliers. A structured process for selecting suppliers, conducting negotiations and awarding contracts has enabled us to avoid competitive disadvantages and ensure we have chosen the right strategic partners.

We have stepped up our level of procurement from emerging markets because prices in the manufacturing sector are coming under slight pressure as a result of the Chinese economic slowdown. We took advantage of this situation and were thus able to further reduce costs.

Supplier performance stabilised at a high level with further improvements Close collaboration between logistics and purchasing enabled us to improve average supplier performance over the year, with this metric rising by three percentage points compared with the previous year to over 97 per cent. This meant we largely avoided extra costs caused by short-term under-supply or delays.

Enduring improvement in supplier quality Our parts per million (ppm) rate as a performance indicator for defective parts was below 1,000 ppm for the fourth year in succession and thus remained at a historical low. This success is due to the rigorous and ongoing monthly evaluation of suppliers as well as the implementation of measures to improve supplier quality.

PRODUCTION AND LOGISTICS

In production and logistics, we quickly made changes to the number of employees and the provision of materials in response to the changing demand situation in 2015. Numerous measures were implemented as planned, following the decision made in 2014 to optimise the network of sites. Other areas of focus were workplace safety and ergonomics, product and process quality, and efficiency.

The Cologne plants, Germany Last year, we began various activities aimed at improving workplace safety and ergonomics at Cologne-Porz, our largest assembly site for production engines. We optimised the provision of materials and redesigned the picking zones. To optimise productivity, we replaced our driverless transport vehicles in the test bay. We expanded the employee information system that we had implemented in 2014. In addition, we stepped up both responsive and preventive measures aimed at improving quality.

Component manufacture Relocation of the components produced in the Cologne-Deutz plant has begun – one of the measures to optimise the network of sites. The main activity is the construction of a new 13,500m^2 shaft centre at our Cologne-Porz site, where crankshaft and camshaft manufacture will be located from mid-2016. As part of the detailed planning process, we optimised the layout of machines and the organisation of work using kaizen techniques and also improved their ergonomics.

The Herschbach component plant saw its largest individual capital expenditure project in recent years come on stream in 2015. It involves an ultra-modern processing centre with a pallet storage system in which all kinds of complex engine add-on components can be manufactured very cost-effectively in any batch size.

The plants in Ulm and Übersee on Lake Chiemsee, Germany As part of the site optimisation strategy, the Ulm plant is being expanded to become the plant for small production runs, focusing on DEUTZ Customised Solutions products, project business, exchange engines and models which are becoming obsolete. Assembly and order management were relocated to Ulm from Übersee on Lake Chiemsee in 2015. Despite the move, there was an increase in revenue from the reconditioned exchange engine business. Throughput times, which are critical in the Xchange process, were shortened and synergies were leveraged. All other functions will move from Übersee to Ulm in 2017.

The Zafra plant, Spain In future, our plant in Zafra (Spain) is to produce the crankcases for engines of up to four litres in addition to the other major engine components already manufactured there, namely cylinder heads, conrods and gearwheels. In addition to the crankcase for the 2011 engine series, which is now being produced in Zafra rather than inhouse in Cologne, the 2.9 crankcase will also be manufactured in Spain in future.

The plants in Georgia, USA In 2015, production of ready-to-install system solutions tailored to customer-specific or segment-specific needs was transferred from Norcross, Georgia to Pendergrass, Georgia. As a result, all activities in the value creation process for the US market are now consolidated at one site. This enables us to leverage synergies between the existing exchange engine production operations in Pendergrass and the relocated assembly line. Processes throughout the logistics chain and in production were optimised at the same time.

Logistics Last year, we brought additional suppliers within the scope of our demand and capacity management system which, at the end of 2015, covered some 95 per cent of the total purchasing volume. We extended the relevant procedures and processes in order to improve the stability of supply from critical suppliers. In connection with the closure of the Cologne-Deutz site, we transferred the empties centre back to the inhouse operation in the Cologne area. This secured an additional 35 permanent positions. We worked with a logistics service provider to set up and implement distribution centre structures for deliveries of engines to North America. This is saving both time and costs.

QUALITY

Quality is anchored in our corporate principles The DEUTZ name has always stood for high quality standards in engines. We intend to continue to live up to this reputation.

For this reason, we decided to introduce a zero-error strategy in 2015. Our main aim in pursuing this quality assurance programme is to ensure we always meet our customers' expectations. The idea is to detect errors before they actually occur. And where errors do occur, we have to learn from them quickly in order not to make the same mistakes again. One of the challenges in this context is that we offer a large number of variants and our products are now highly complex.

Last year, we also restructured the product development process in order to greatly improve the methods used and to ensure the quality department is involved from an early stage. Optimised processes for drawing up specifications should help to ensure that customers' wishes are reflected even more accurately in product development.

In 2015, our external certification body carried out a monitoring audit in order to review our adherence to the ISO 9001 (quality management), 14001 (environmental management) and 50001 (energy management) standards. All criteria were again met.

This enabled the certificates to be renewed. The more wide-ranging requirements resulting from the revised ISO 9001:2015 and 14001:2015 standards are currently being integrated into the existing DEUTZ management system.

INTERNATIONAL JOINT VENTURES

China has been a very challenging market for some time. Growth forecasts have been revised down, and there is considerable capacity in the engine production sector. At the start of 2015, we decided to consolidate our Chinese production operations in our established DEUTZ (Dalian) Engine Co., Ltd. joint venture in Dalian, China, which has adequate capacity.

We have been operating the DEUTZ Dalian joint venture with the First Automotive Works Group, one of China's leading vehicle manufacturers, since 2007. Here, we produce three to eight litre diesel engines, mainly for automotive applications for the Chinese market. The unit sales figure for 2015 was just short of 75,000 engines, a year on year decrease of 29.5 per cent. DEUTZ Dalian's business performance was severely affected by market conditions in China, especially in the truck and construction machinery segments. An improved product mix brought in revenue equivalent to roughly €340 million, down by 5.6 per cent year on year. Measured in the local currency, the fall in revenue was 19.6 per cent compared with 2014. The company, accounted for under the equity method, had a negative impact of €7.0 million on the DEUTZ Group's operating profit, having contributed €3.5 million to operating profit in 2014. We expect the market situation to remain challenging but predict a smaller negative impact on operating profit. Nevertheless, capacity utilisation will continue to have a strong influence on earnings.

We made significant progress in consolidating our other Chinese production activities in the year under review. The DEUTZ Engine (China) Co., Ltd. joint venture in Linyi, China, was wound up at the end of 2015. We had originally founded the company, which never made any substantial investments, with AB Volvo.

At the end of 2015, we sold our WEIFANG WEICHAI-DEUTZ DIESEL ENGINE CO., LTD. joint venture in Weifang, China, to our previous co-shareholder, Weichai Power. The company only produces the 226B engine series under licence and we no longer considered it to be strategically important.

We have also begun the process of closing the DEUTZ Engine (Shandong) Co., Ltd. joint venture in Linyi, China, in which we have a 70 per cent shareholding. It is expected to be fully wound up during 2016. Implementation work in connection with this company was suspended and terminated at an early stage.

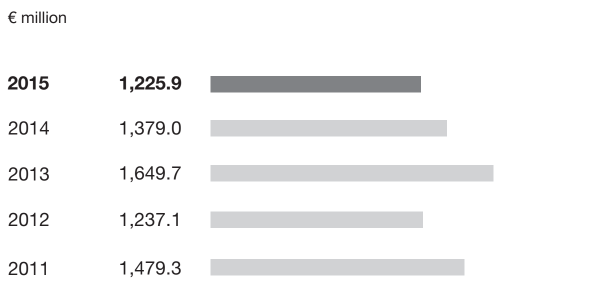
Overall, the winding-up and sale of the aforementioned companies – i.e. DEUTZ Engine China, WEIFANG WEICHAI-DEUTZ DIESEL ENGINE CO., LTD. and DEUTZ Engine (Shandong) Co., Ltd. – resulted in a small contribution to earnings in the reporting year.

DEUTZ AGCO MOTORES S.A. (DAMSA), our Argentinian joint venture with the AGCO Group, produces engines for the local market, with a particular focus on agricultural machinery, buses and industrial applications. In 2015, the company sold around 1,150 engines in very challenging market conditions. It generated revenue of around €19 million, which was about a fifth more than in 2014 owing to price increases. The company made a loss of €0.1 million.

We hold a stake of 30 per cent in D.D. Power Holdings (Pty) Ltd., our South African joint venture. This sales and service company is active in the local market, focusing on sectors such as the local mining business. In the year under review, the company achieved revenue of around €20 million and a profit of approximately €2.5 million, with both figures increasing year on year.

NEW ORDERS

DEUTZ Group: New orders

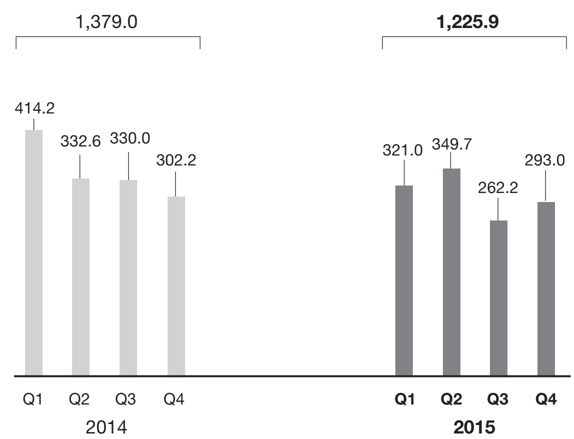


Decline in new orders compared with 2014 In 2015, the DEUTZ Group received orders worth €1,225.9 million, which was 11.1 per cent below the figure of €1,379.0 million achieved in the previous year. With the exception of the service business, where new orders rose by 7.2 per cent, all other application segments reported a decrease in new orders compared with 2014. New orders were down by 20.0 per cent in the Mobile Machinery application segment, by 8.9 per cent in the Stationary Equipment application segment and by 4.1 per cent in the Agricultural Machinery application segment. There was also a small decrease in the Automotive application segment of 1.3 per cent.

The level of new orders varied considerably over the course of the year. The second quarter was the only one with a year-on-year increase and, at €349.7 million, was also the strongest quarter. Year-on-year decreases were registered in all other quarters. As a consequence of the advance production of engines, European customers drew on their inventories of the engines that they had purchased on a large scale in 2014 in anticipation of the changing emissions standard, although this trend had been expected. From the third quarter onwards, end customers were very reluctant to invest, which had a huge negative impact on new orders in the second half of the year. At €262.2 million, the lowest level of new orders was registered in the third quarter. In the fourth quarter, orders amounted to €293.0 million, up by 11.7 per cent on the very weak previous quarter and down by 3.0 per cent on the fourth quarter of 2014.

DEUTZ Group: New orders by quarter

€ million

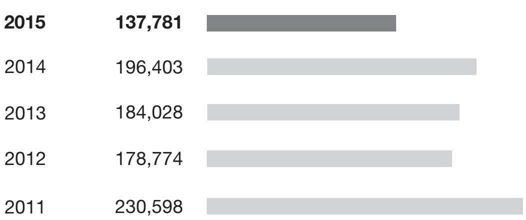


Orders on hand totalled €201.0 million as at 31 December 2015, a decline of 8.5 per cent compared with €219.7 million at the end of 2014.

UNIT SALES

DEUTZ Group: Unit sales

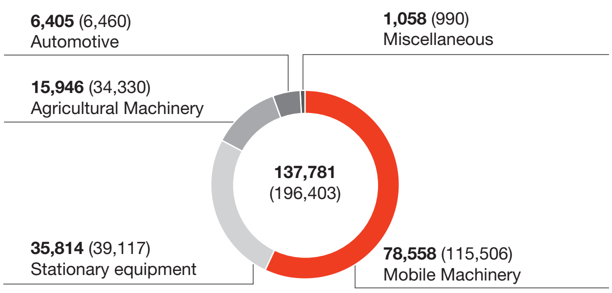
units



Year-on-year fall in unit sales DEUTZ sold 137,781 engines in the year under review, 29.8 per cent fewer than the 196,403 engines sold in 2014. The decreases in the Agricultural Machinery and Mobile Machinery application segments were particularly substantial at 53.6 per cent and 32.0 per cent respectively.

DEUTZ Group: Unit sales by application segment

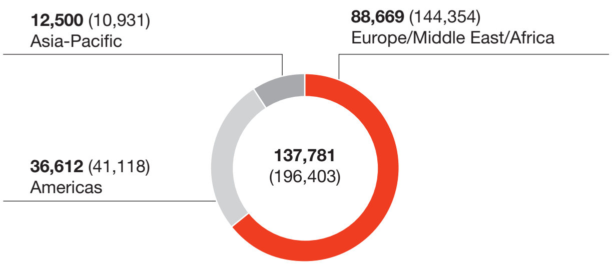
units (2014 figures)



The breakdown by region reveals a very disparate pattern. Unit sales in our biggest market – EMEA (Europe, Middle East and Africa) – dropped by 38.6 per cent to 88,669 engines. They were down by 11.0 per cent to 36,612 engines in the Americas. By contrast, unit sales in the Asia-Pacific region rose by 14.4 per cent to 12,500 engines.

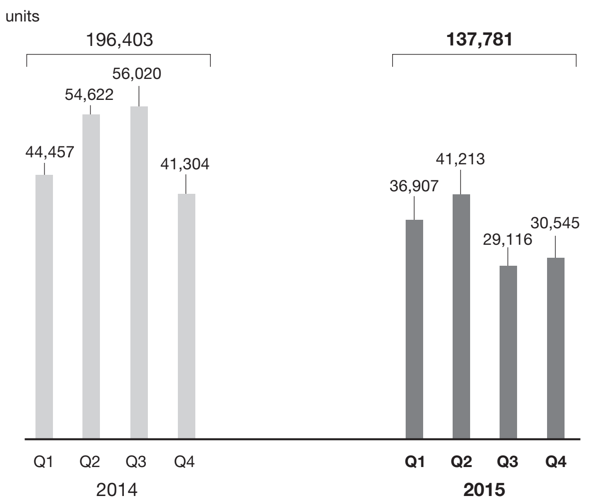
DEUTZ Group: Units sales by region

units (2014 figures)

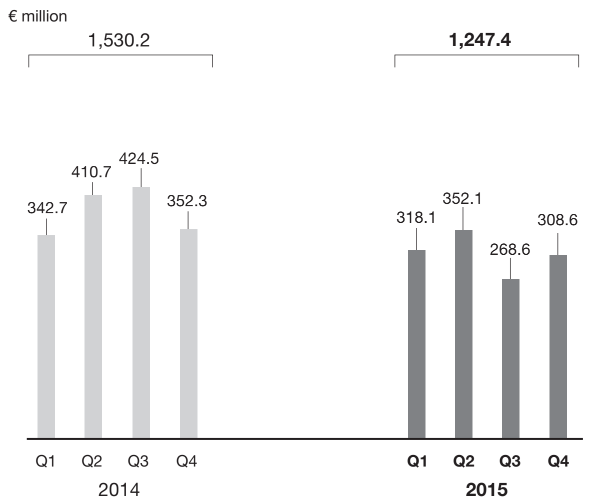


Significant year-on-year decreases were registered in all four quarters of the year. The highest unit sales figure was achieved in the second quarter with 41,213 engines. In the fourth quarter, 30,545 engines were sold, representing a slight increase of 4.9 per cent on the very weak previous quarter and a decline of 26.0 per cent compared with the fourth quarter of 2014.

DEUTZ Group: Consolidated unit sales by quarter



DEUTZ Group: Revenue by quarter



RESULTS OF OPERATIONS

DEUTZ Group: Revenue

€ million

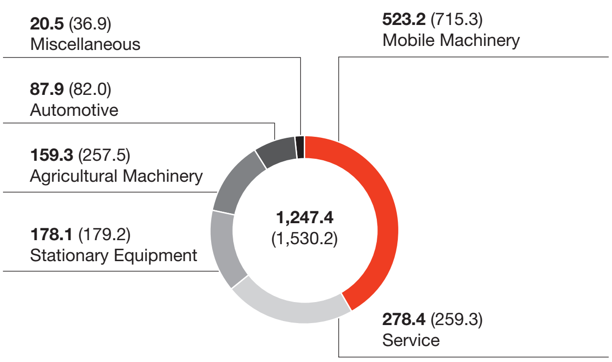
2015	**1,247.4**
2014	1,530.2
2013	1,453.2
2012	1,291.9
2011	1,529.0

Revenue decline low relative to fall in unit sales In 2015, DEUTZ generated revenue of €1,247.4 million, 18.5 per cent less than in the previous year when revenue amounted to €1,530.2 million. This meant that we did not achieve the forecast published in the 2014 annual report, in which we predicted a decline in revenue of around 10 per cent. In September 2015, we revised our forecast to an approximately 20 per cent decrease in revenue, and we surpassed the revised revenue target. The decline in revenue is due partly to the changes to emissions standards for engines under 130kW that came into force in the European Union on 1 October 2014 and the resulting effects from the advance production of engines. Furthermore, the end customers for our engines showed a pronounced reluctance to invest in the second half of 2015, which is why we updated our forecast. The fall in revenue was, in percentage terms, not as substantial as the drop in unit sales.

Revenue levels were very uneven over the course of the year. After €318.1 million in the first quarter, revenue increased to €352.1 million in the second quarter before falling again to €268.6 million in the third. In the fourth quarter, we generated revenue of €308.6 million, which was 14.9 per cent more than in the previous quarter but 12.4 per cent less than in the fourth quarter of 2014. The second quarter was thus the strongest of the year, but all four quarters registered year-on-year falls.

DEUTZ Group: Revenue by application segment

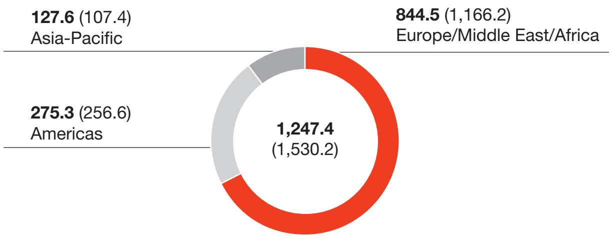
€ million (2014 figures)



Our largest application segment, Mobile Machinery, fell short of the significantly increased revenue figure reported in 2014. Its revenue was down by 26.9 per cent to €523.2 million in the reporting year. Revenue also decreased significantly in the Agricultural Machinery application segment, falling by 38.1 per cent to €159.3 million. However, revenue in the Stationary Equipment application segment was on a par with 2014 at €178.1 million, while the Automotive application segment's revenue was up by 7.2 per cent to €87.9 million and that of the service business rose by 7.4 per cent to €278.4 million.

DEUTZ Group: Revenue by region

€ million (2014 figures)



Broken down by region, revenue in EMEA (Europe, Middle East and Africa) dropped by 27.6 per cent to €844.5 million. By contrast, revenue in the Americas region increased by 7.3 per cent to €275.3 million although, taken in isolation, the second half of 2015 was considerably worse than both the first half of 2015 and the second half of 2014. Moreover, revenue in the Asia-Pacific region climbed by an impressive 18.8 per cent to €127.6 million.

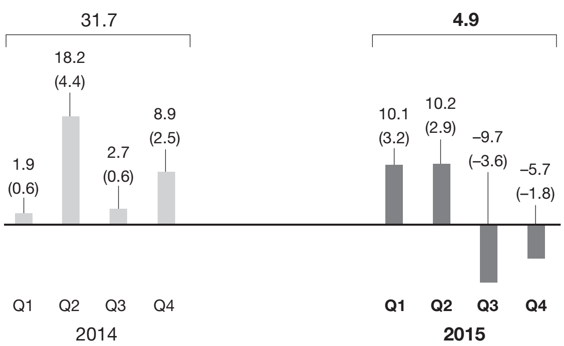
DEUTZ Group: Operating profit/EBIT margin before one-off items

€ million (EBIT margin in %)

2015	**4.9**	**(0.4)**
2014	31.7	(2.1)
2013	47.5	(3.3)
2012	37.1	(2.9)
2011	91.2	(6.0)

DEUTZ Group: Operating profit (before one-off items)/EBIT margin by quarter

€ million (EBIT margin in %)



Earnings performance Operating profit before depreciation and amortisation (EBITDA before one-off items) amounted to €112.2 million in 2015, a year-on-year decrease of €25.2 million (2014: €137.4 million). This trend was mainly attributable to the decline in the volume of business in the DEUTZ Compact Engines segment and a smaller contribution to earnings from our Chinese joint venture DEUTZ (Dalian) Engine Co., Ltd. caused by China's current economic slowdown. Earnings were boosted, however, by lower production costs and warranty costs, currency effects and increased revenue in the high-margin DEUTZ Customised Solutions segment. Despite low capacity utilisation, the EBITDA margin (before one-off-items) held steady at 9.0 per cent.

EBITDA before one-off items amounted to €26.6 million in the fourth quarter of 2015, a decrease of €16.3 million year on year (Q4 2014: €42.9 million) but an increase of €11.4 million compared with the previous quarter (Q3 2015: €15.2 million). This was due, in particular, to the change in the volume of business.

Operating profit after depreciation and amortisation (EBIT before one-off items) came to €4.9 million in 2015, a year on year reduction of €26.8 million (2014: €31.7 million). Before one-off items, the EBIT margin for the reporting year was 0.4 per cent (2014: 2.1 per cent). We were thus unable to match the forecast for 2015 of around 3 per cent that we had published at the start of the year. This was mainly due to the very sharp fall in the volume of business during the second half of the year. However, we did fully meet the revised forecast, issued in September 2015, for operating profit at around break-even level. Depreciation and amortisation included impairment losses totalling €9.7 million on intangible assets and on property, plant and equipment. In 2014, there had been impairment losses before one-off items of €9.5 million. The impairment losses were recognised in the year under review because of the market situation and mainly related to capitalised development expenditure. In the fourth quarter of 2015, the operating loss before one-off items amounted to €5.7 million (Q3 2015: loss of €9.7 million; Q4 2014: profit of €8.9 million), giving an EBIT margin of minus 1.8 per cent (Q3 2015: minus 3.6 per cent; Q4 2014: 2.5 per cent).

After one-off items, operating profit (EBIT) deteriorated by €7.9 million (2014: €12.8 million). In the previous year, EBIT had been reduced by one-off items of €18.9 million relating mainly to expenses connected with the measures to optimise the network of sites. There were no one-off items in the year under review.

There was a deterioration in return on capital employed (ROCE)[1], our internal KPI, from 3.9 per cent in 2014 to 0.6 per cent in 2015. This was due to the unexpectedly strong contraction in the volume of orders and to the impairment losses recognised on intangible assets and on property, plant and equipment. At the start of the year, we expected ROCE to rise slightly compared with 2014. However, we were unable to achieve this forecast due to the reasons outlined above.

[1] Return on capital employed (ROCE before one-off items): ratio of EBIT before one-off items 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.

Cost of sales In 2015, the cost of sales amounted to €1,054.8 million (2014: €1,327.6 million). This year-on-year decrease of 20.5 per cent was mainly attributable to lower costs for materials, staff and contract workers resulting from the decline in the volume of unit sales. There was also a substantial decrease in warranty costs. Accordingly, the ratio of cost of sales to revenue fell from 86.8 per cent in 2014 to 84.6 per cent in 2015. The gross margin therefore improved markedly – despite the smaller volume of business.

Overview of the DEUTZ Group's results of operations

€ million

	2015	2014
Revenue	1,247.4	1,530.2
Cost of sales	–1,054.8	–1,327.6
Research and development costs	–76.3	–74.3
Selling and administrative expenses	–104.8	–100.0
Other operating income	29.3	22.9
Other operating expenses	–30.6	–41.4
Profit/loss on equity-accounted investments	–6.3	1.9
Other financial income	1.0	1.1
Operating profit (EBIT)	4.9	12.8
One-off items	–	–18.9
EBIT (before one-off items)	4.9	31.7
Interest expenses, net	–4.0	–6.1
Income taxes	2.6	12.8
Net income	3.5	19.5

Research and development costs In the year under review, research and development costs totalled €76.3 million (2014: €74.3 million). Although R&D expenditure, which is a metric relevant to liquidity, was reduced as planned, R&D costs increased slightly (by €2.0 million) because of the far lower capitalisation rate. Research and development costs largely comprised staff costs, cost of materials and amortisation on completed development projects, from which investment grants received and capitalised development expenditure were deducted.

Selling and administrative expenses There was a small rise in selling expenses, which advanced to €68.3 million in 2015 (2014: €65.7 million), and in administrative expenses, which went up to €36.5 million (2014: €34.3 million). Administrative expenses included transition costs in connection with the switch of IT service provider at the end of the year under review. Without this one-off cost item, there would have been a moderate decline in administrative expenses. As a proportion of revenue, selling and administrative expenses rose to 5.5 per cent (2014: 4.3 per cent) and 2.9 per cent (2014: 2.2 per cent) respectively, due to the greatly reduced volume of business.

Other operating income The reporting year saw an increase of €6.4 million in other operating income to €29.3 million (2014: €22.9 million). This rise was primarily attributable to effects arising on the translation of foreign currency positions. However, foreign currency gains were offset by a similar level of foreign currency losses, which are reported in other operating expenses. Furthermore, a gain on disposal of €2.9 million was recognised following the disposal of the shares in WEIFANG WEICHAI-DEUTZ DIESEL ENGINE CO., LTD., Weifang, China, in 2015. Other operating income also included a gain of €1.0 million arising from the deconsolidation of DEUTZ Engine (China) Co. Ltd., Linyi, China.

Other operating expenses Other operating expenses totalled €30.6 million in the reporting year, a year-on-year decrease of €10.8 million (2014: €41.4 million). The prior-year figure had included restructuring costs of €17.1 million. Excluding this one-off effect in the prior-year figure, other operating expenses increased by €6.3 million in 2015 as a result of higher losses arising on the translation of foreign currency positions.

Profit/loss on equity-accounted investments In 2015, there was a loss on equity-accounted investments of €6.3 million, a deterioration of €8.2 million compared with the profit on equity-accounted investments reported for 2014 of €1.9 million. This change is primarily attributable to the contribution to earnings from our Chinese joint venture DEUTZ (Dalian) Engine Co., Ltd. on the back of China's pronounced economic slowdown. Further information can be found in the 'International joint ventures' section on page 36.

Net interest expense Net interest expense amounted to €4.0 million (2014: €6.1 million). This significant year-on-year improvement of €2.1 million was attributable to lower utilisation of credit lines.

Income taxes In 2015, there was overall tax income of €2.6 million (2014: €12.8 million). This amount included the current tax expense of €5.7 million, which was €3.4 million lower than in the previous year (2014: €9.1 million). The main factors in this decrease were the drop in earnings at DEUTZ Corporation, Atlanta, USA, and the reversal of provisions for income taxes relating to the tax audit conducted at DEUTZ AG for the years 2009 to 2011. The current tax expense was offset by deferred tax income of €8.3 million. This mainly resulted from the reversal of deferred tax liabilities arising in connection with the capitalisation of development expenditure under IFRS. The year-on-year decrease was €13.6 million (2014: €21.9 million). The deferred tax income reported in 2014 was largely influenced by effects from the tax audit carried out at DEUTZ AG for the years 2009 to 2011.

Earnings per share As a result of weaker operating profit and lower deferred tax income, net income dropped to €3.5 million in 2015, a year-on-year decrease of €16.0 million (2014: €19.5 million). This resulted in earnings per share of €0.04 (2014: €0.18).

BUSINESS PERFORMANCE IN THE SEGMENTS

DEUTZ Group: Segments

€ million

	2015	2014
New orders		
DEUTZ Compact Engines	958.4	1,115.0
DEUTZ Customised Solutions	267.5	264.0
Total	**1,225.9**	**1,379.0**
Unit sales (units)		
DEUTZ Compact Engines	125,214	183,125
DEUTZ Customised Solutions	12,567	13,278
Total	**137,781**	**196,403**
Revenue		
DEUTZ Compact Engines	967.2	1,279.9
DEUTZ Customised Solutions	280.2	250.3
Total	**1,247.4**	**1,530.2**
EBIT before one-off items		
DEUTZ Compact Engines	–31.9	15.2
DEUTZ Customised Solutions	31.3	18.8
Other	5.5	–2.3
Total	**4.9**	**31.7**

BUSINESS PERFORMANCE IN THE DEUTZ COMPACT ENGINES (DCE) SEGMENT

New orders down on prior year In 2015, the DEUTZ Compact Engines (DCE) segment received new orders worth €958.4 million, 14.0 per cent down on 2014 when orders worth €1,115.0 million were received. As was the case at Group level, only the service business grew, increasing by 3.5 per cent to €160.7 million. In the Mobile Machinery application segment, new orders were down by 21.9 per cent to €463.2 million. The Automotive, Agricultural Machinery and Stationary Equipment application segments also reported decreases of 10.8 per cent, 4.8 per cent and 3.6 per cent respectively. Orders on hand amounted to €137.2 million at the end of the year, down by 3.0 per cent compared with the end of 2014.

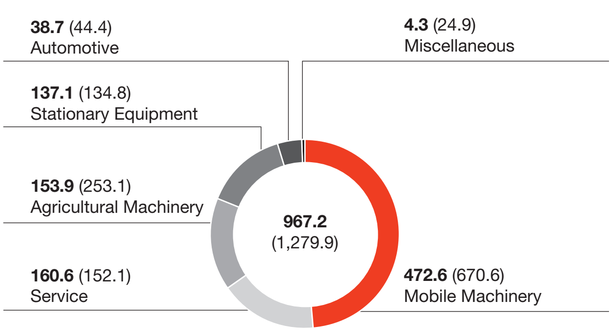
Fewer engines sold Unit sales in the DCE segment fell by almost a third to 125,214 engines. The number sold in the prior year was 183,125 engines. In EMEA, our largest market, 81,428 engines were sold, which was 40.7 per cent fewer than in 2014. Unit sales went down by 8.3 per cent in the Americas region but rose by 15.2 per cent in the Asia-Pacific region. There were decreases across all application segments, with particularly pronounced drops for Agricultural Machinery and Mobile Machinery of 53.9 per cent and 32.8 per cent respectively.

Revenue also down year on year At €967.2 million, revenue in the DCE segment declined by 24.4 per cent (2014: €1,279.9 million). The fall in revenue was therefore not as substantial as the drop in unit sales – as was also the case at Group level. The EMEA region's revenue decreased by 32.8 per cent to €683.7 million. By contrast, the Americas region rose by 7.6 per cent to €228.1 million and the Asia-Pacific region by 10.6 per cent to €55.4 million. Revenue decreased by 29.5 per cent in the Mobile Machinery application segment, by 39.2 per cent in the Agricultural Machinery application segment and by 12.8 per cent in the Automotive application segment. However, revenue in the service business was up by 5.6 per cent year on year and in the Stationary Equipment application segment it increased by 1.7 per cent.

Q4 better than Q3 in 2015 In the DCE segment, new orders reached €234.4 million in the fourth quarter of 2015, which was on a par with the prior-year figure of €232.5 million and represented a significant increase of 20.8 per cent on the third quarter of 2015. Unit sales fell by 24.5 per cent to 27,618 engines year on year but rose by 5.2 per cent compared with the previous quarter. Revenue in the final quarter of 2015 amounted to €237.1 million, which was 14.4 per cent less than the fourth quarter of 2014 but 17.5 per cent more than in the third quarter of 2015.

DEUTZ Compact Engines: Revenue by application segment

€ million (2014 figures)



Sharp fall in DCE's operating profit The DEUTZ Compact Engines segment reported an operating loss of €31.9 million in 2015 (2014: operating profit of €15.2 million). A greatly reduced volume of business and a smaller contribution to earnings from our Chinese joint venture DEUTZ (Dalian) Engine Co., Ltd., Dalian, China, caused this deterioration of €47.1 million compared with the prior year, despite lower production costs and warranty costs as well as positive currency effects. The operating profit for the segment was also adversely affected by impairment losses totalling €7.1 million on intangible assets and on property, plant and equipment.

BUSINESS PERFORMANCE IN THE DEUTZ CUSTOMISED SOLUTIONS (DCS) SEGMENT

Small rise in new orders compared with 2014 The DEUTZ Customised Solutions (DCS) segment took new orders worth €267.5 million in the reporting year, an increase of 1.3 per cent compared with the 2014 figure of €264.0 million. Unlike the DCE segment, this segment was not affected by the advance production of engines in 2014. With the exception of Stationary Equipment, where new orders fell by 24.7 per cent, and the Other segment, where new orders fell by 28.6 per cent, all application segments received more orders than in the previous year. As at the end of 2015, orders on hand stood at €63.8 million, down by 18.4 per cent on the figure reported a year earlier (31 December 2014: €78.2 million).

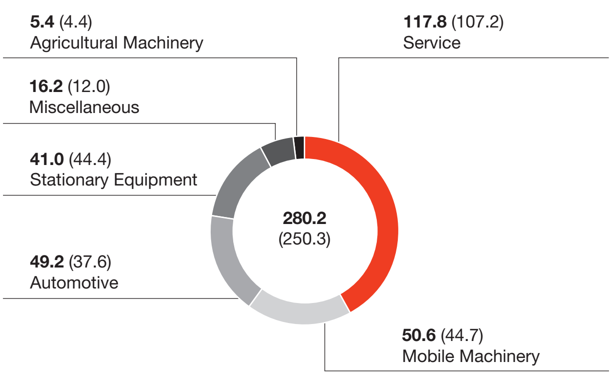
Slightly fewer engines sold Unit sales in the DCS segment declined by 5.4 per cent to 12,567 engines in 2015. Unit sales were down in the Americas region but rose in EMEA, our largest region, and in the Asia-Pacific region. There were significant year-on-year gains for the Automotive application segment, but all other application segments sold fewer engines.

Rise in revenue year on year In contrast to unit sales, revenue in the DCS segment climbed by 11.9 per cent to €280.2 million in the reporting year. All regions generated growth, with revenue rising by 8.4 per cent in the EMEA region, by 5.8 per cent in the Americas and by 26.0 per cent in the Asia-Pacific region. The only application segment where revenue decreased was Stationary Equipment (by 7.7 per cent). All other application segments saw an increase in revenue: 13.2 per cent for Mobile Machinery, 30.9 per cent for Automotive, 22.7 per cent for Agricultural Machinery and 9.9 per cent for the service business.

Slightly weaker fourth quarter In the fourth quarter of 2015, new orders in the DCS segment totalled €58.6 million, down by 15.9 per cent year on year and down by 14.1 per cent on the previous quarter. There were also fewer unit sales in the final three months of the year, with a year-on-year decrease of 37.8 per cent to 2,927 engines. However, unit sales had been exceptionally high in the fourth quarter of 2014, especially in this segment's smaller power output categories. However, unit sales rose by 1.9 per cent compared with the third quarter of 2015. The revenue attributable to the DCS segment in the final quarter fell by 4.9 per cent year on year to €71.5 million, but nonetheless was 7.0 per cent higher than in the third quarter of 2015.

DEUTZ Customised Solutions: Revenue by application segment

€ million (2014 figures)

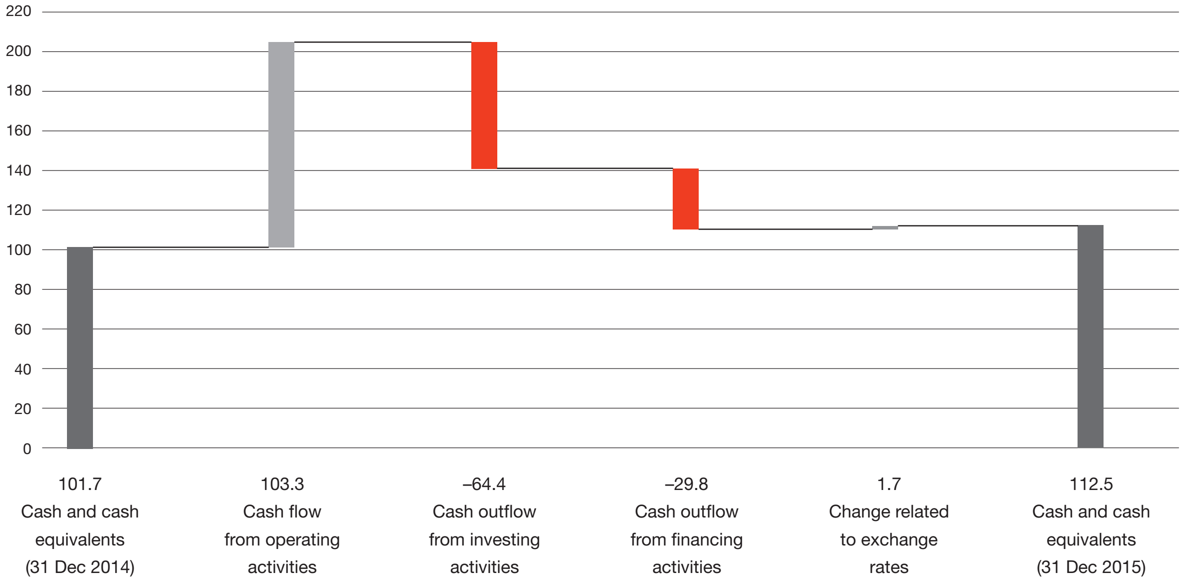


Vast improvement in DCS's operating profit The operating profit of the DEUTZ Customised Solutions segment for the reporting year was €31.3 million (2014: €18.8 million). This sharp increase compared with 2014 is due, in particular, to the larger volume of business and to positive currency effects. Furthermore, the prior-year figure had included impairment losses of €9.5 million recognised on intangible assets and on property, plant and equipment and of €1.8 million recognised on equity-accounted investments. In 2015, impairment losses totalling €2.6 million were recognised on intangible assets and on property, plant and equipment.

Other The operating profit reported by the Other segment came to €5.5 million (2014: operating loss of €2.3 million). This positive trend was due, above all, to the sale of the shares in WEIFANG WEICHAI-DEUTZ DIESEL ENGINE CO., LTD., Weifang, China, and the cancellation of a liability denominated in a foreign currency. This liability consisted of an outstanding

DEUTZ Group: Change in cash and cash equivalents

€ million



contribution to the issued capital of DEUTZ Engine (China) Co, Ltd. in Linyi, China. The decision to wind up the company cancelled this obligation in the third quarter of 2015, thereby eliminating the unrealised negative currency effect that had applied in 2014.

FINANCIAL POSITION

BASIC PRINCIPLES AND OBJECTIVES OF FINANCIAL MANAGEMENT

Overview of the DEUTZ Group's financial position

€ million

	2015	2014
Cash flow from operating activities	103.3	114.1
Cash flow from investing activities	–64.4	–55.9
Cash flow from financing activities	–29.8	–17.5
Change in cash and cash equivalents	9.1	40.7
Free cash flow from continuing operations	35.0	52.0
Cash and cash equivalents at 31 Dec	112.5	101.7
Current and non-current interest-bearing financial debt at 31 Dec	73.5	88.0
Net financial position at 31 Dec	39.0	13.7

Free cash flow: cash flow from operating and investing activities less net interest expense.
Net financial position: cash and cash equivalents less current and non-current interest-bearing financial debt.

Central responsibility for treasury Responsibility for financial management in the DEUTZ Group lies with DEUTZ AG as the parent company of the Group. Financial management primarily consists of obtaining the necessary funds, managing their use within the Group, pooling cash resources and hedging interest-rate risk, currency risk and commodities risk throughout the Group.

FUNDING

Syndicated credit line and loan from the European Investment Bank ensure sufficient liquidity In order to ensure sufficient liquidity, DEUTZ has at its disposal a syndicated, revolving working capital facility of €160 million provided by a consortium of banks. It is a floating-rate, unsecured line. In 2015, the term of the facility was extended to May 2020. DEUTZ can elect whether to utilise the cash line as a bilateral overdraft facility (up to €60 million) or to draw down amounts with interest periods of three to six months.

In addition, we have an amortising loan from the European Investment Bank with a remaining balance of €68.4 million at 31 December 2015. This loan, which is also unsecured, is repayable in instalments until July 2020. We have hedged the interest-rate risk arising from this loan.

As part of the contractual agreements for both loans, DEUTZ is obliged to comply with certain financial covenants. They do not limit our leeway for growth projects, however. The working capital facility and the loan from the European Investment Bank have enabled us to secure funding for our projects and for further growth over the medium to long term.

Receivables management optimised by means of factoring The sale of receivables is an important way of optimising receivables management. Because the credit quality of our customer receivables is excellent, factoring is also a cost-effective way of improving working capital, especially as considerable cash resources are required to cover the period from the preliminary financing of production to receipt of payment from the customer. The volume of sales of receivables on the balance sheet date was lower than at the end of 2014 as a result of the business situation, the volume as at 31 December 2015 being around €99 million (31 December 2014: €107 million).

FREE CASH FLOW

Cash flow from operating activities amounted to €103.3 million in 2015 (2014: €114.1 million), a year-on-year decrease of €10.8 million. The main reason for this change was the sharp contraction in the volume of business during the reporting year.

The net cash used for investing activities came to €64.4 million in 2015, a rise of €8.5 million year on year (2014: €55.9 million). This increase was attributable, in particular, to higher cash payments in connection with capital expenditure on property, plant and equipment.

Financing activities in 2015 resulted in a net cash outflow of €29.8 million (2014: €17.5 million). This increase of €12.3 million was largely due to substantially higher payments of principal in relation to existing financial liabilities than in the prior year. As in the previous year, cash flow from financing activities included a dividend payment to shareholders of €8.5 million.

Cash and cash equivalents as at 31 December 2015 had risen by €10.8 million to €112.5 million (31 December 2014: €101.7 million). The net financial position[1] as at 31 December 2015 was €39.0 million, a further improvement of €25.3 million compared with the same date a year earlier (31 December 2014: €13.7 million).

Free cash flow[2] was lower than in the prior year, decreasing by €17.0 million to €35.0 million (2014: €52.0 million). This was due in large part to the fall in cash flow from operating activities caused by the drop in demand as well as to increased capital expenditure. However, it was within the bandwidth that we had forecast at the start of 2015 of free cash flow in the low to mid-double-digit million euro range.

CAPITAL EXPENDITURE ON PROPERTY, PLANT AND EQUIPMENT AND ON INTANGIBLE ASSETS

After deducting investment grants, capital expenditure on property, plant and equipment and on intangible assets totalled €69.2 million in 2015, which was €2.6 million more than in the previous year (2014: €66.6 million). The bulk of this spending (€50.9 million) went on property, plant and equipment (2014: €37.0 million). Capital expenditure on intangible assets accounted for €18.3 million (2014: €29.6 million). The investing activities relating to property, plant and equipment focused on measures aimed at optimising our network of sites, such as the construction of the shaft centre in Cologne-Porz. There were also additions in connection with replacement investments in machinery and tools. Capital expenditure on intangible assets went mainly on the refinement of our existing engine series.

Before the capitalisation of development expenditure, capital investment amounted to €56.2 million (2014: €40.3 million). Capital expenditure (before capitalisation of development expenditure) was thus slightly higher than the forecast of approximately €50 million that we had made at the start of the year. This was due to several capital spending projects being realised more rapidly than expected.

The bulk of the total capital expenditure after deducting investment grants – €61.7 million – was invested in the DEUTZ Compact Engines segment (2014: €57.8 million). Capital expenditure in DEUTZ Customised Solutions was €7.5 million (2014: €8.8 million). As was the case in 2014, investing activities in both segments focused on property, plant and equipment and on development expenditure.

NET ASSETS

Overview of the DEUTZ Group's assets

€ million

	31 Dec 2015	31 Dec 2014	Change
Non-current assets	589.6	625.8	–36.2
Current assets	498.1	523.0	–24.9
Assets classified as held for sale	0.4	0.4	–
Total assets	**1,088.1**	**1,149.2**	**–61.1**
Equity	495.6	511.0	–15.4
Non-current liabilities	280.8	322.7	–41.9
Current liabilities	311.7	315.5	–3.8
Total equity and liabilities	**1,088.1**	**1,149.2**	**–61.1**
Working capital (€ million)	183.6	196.2	–12.6
Working capital ratio (31 Dec, %)	14.7	12.8	1.9
Working capital ratio (average, %)	17.6	13.3	4.3
Equity ratio (%)	45.5	44.5	1.0

Working capital: inventories plus trade receivables less trade payables.
Equity ratio: equity/total equity and liabilities.

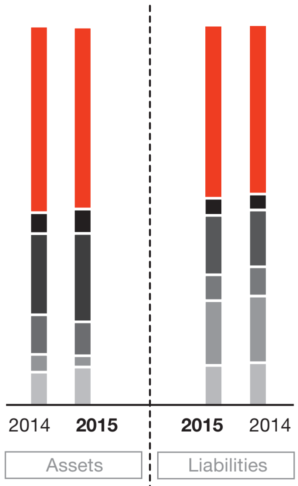
[1] Net financial position: cash and cash equivalents less current and non-current interest-bearing financial debt.
[2] Free cash flow: cash flow from operating and investing activities less net interest expense.

DEUTZ Group: Balance sheet structure

in % (2014 figures)

Assets

47.8	(49.0)	Non-current assets
6.4	(5.5)	Deferred taxes
23.2	(21.3)	Inventories
9.3	(10.6)	Trade receivables
3.0	(4.7)	Other receivables and assets
10.3	(8.8)	Cash and cash equivalents



Liabilities

45.5	(44.5)	Equity
4.5	(4.2)	Other liabilities
15.6	(14.9)	Trade payables
6.8	(7.7)	Financial liabilities
17.1	(17.6)	Pension provisions
10.5	(11.2)	Other provisions

Non-current assets Non-current assets of the DEUTZ Group totalled €589.6 million as at 31 December 2015 (31 December 2014: €625.8 million). The decline of €36.2 million was largely due to the reduction in intangible assets. At €17.8 million, additions were much lower than depreciation and amortisation amounting to €45.9 million as a consequence of the new engines having gone into volume production. The market situation also made it necessary to recognise impairment losses on intangible assets of €7.4 million.

Current assets Current assets were also lower than at the end of 2014, falling by €24.9 million to €498.1 million (31 December 2014: €523.0 million). This was mainly attributable to the volume-related decrease in trade receivables and other receivables and assets. The decrease in other receivables and assets primarily resulted from the derecognition of the outstanding contributions from non-controlling interests, which related to the AB Volvo Group's shareholding in DEUTZ Engine (China) Co., Ltd. in Linyi, China. The outstanding obligations were cancelled as a result of the company being wound up.

Working capital Working capital had dropped to €183.6 million as at 31 December 2015 (31 December 2014: €196.2 million). The main reason for this was the reduction in trade receivables caused by lower demand. Although there was a modest increase in inventories, they decreased slightly after adjustment for exchange rate effects. Trade payables were virtually unchanged. Despite the lower level of working capital, the working capital ratio[1)] increased to 14.7 per cent as at 31 December 2015 due to the sharp fall in the volume of business (31 December 2014: 12.8 per cent). The average working capital ratio[2)] also rose, reaching 17.6 per cent on the balance sheet date (31 December 2014: 13.3 per cent). Consequently, we were unable to achieve our forecast for an average working capital ratio of approximately 14 per cent, due mainly to the strong contraction in the volume of business.

Unrecognised intangible assets In addition to the assets recognised on the balance sheet, DEUTZ has further assets that are not recognised. The DEUTZ brand is synonymous with highly sophisticated technology, quality and reliability and the Company has been a firmly established player in the equipment manufacturing and operating industry for more than 150 years. DEUTZ also enjoys long-standing valuable relationships with customers; it has entered into long-term cooperation agreements, particularly with its key customers.

Equity As at 31 December 2015, equity had decreased to €495.6 million (31 December 2014: €511.0 million). This reduction of €15.4 million was predominantly caused by the change in non-controlling interests. Following the winding-up of DEUTZ Engine (China) Co., Ltd. in Linyi, China, €2.6 million of the capital that had already been injected by our joint venture partner, the AB Volvo Group, was repaid. The outstanding obligation of the AB Volvo Group to make a contribution to the joint venture's issued capital was also cancelled. By contrast, there was an increase in the Group equity attributable to the shareholders of DEUTZ AG due, above all, to the level of net income and to the positive effects from the higher discount rates used in the measurement of provisions for pensions and other post-retirement benefits. Despite the decrease in equity, the equity ratio rose slightly, from 44.5 per cent as at 31 December 2014 to 45.5 per cent as at 31 December 2015, and was thus within the range that we had forecast at the start of the reporting year of well above 40 per cent.

[1)] Working capital (inventories plus trade receivables less trade payables) as at the balance sheet date divided by revenue for the previous twelve months.

[2)] Average working capital (inventories plus trade receivables less trade payables) at the four quarterly reporting dates divided by revenue for the previous twelve months.

Non-current liabilities Non-current liabilities totalled €280.8 million as at 31 December 2015 (31 December 2014: €322.7 million). The decrease of €41.9 million was predominantly caused by the change in provisions for pensions and other post-retirement benefits. These provisions fell by €14.8 million compared with 31 December 2014, mainly due to higher discount rates. We also continued to lower our non-current financial debt, which amounted to €58.6 million as at 31 December 2015. This represented a year-on-year fall of €14.7 million (31 December 2014: €73.3 million). Other provisions also decreased, by €11.7 million, mainly due to a reduction in provisions for warranty costs.

Current liabilities Current liabilities also decreased slightly over the reporting year, from €315.5 million as at 31 December 2014 to €311.7 million as at 31 December 2015. The decline of €3.8 million was largely attributable to the lower level of other provisions.

Total assets amounted to €1,088.1 million as at 31 December 2015 (31 December 2014: €1,149.2 million).

OVERALL ASSESSMENT FOR 2015

For DEUTZ, 2015 was a year of two halves: while the first six months went well, business contracted significantly in the second six months due to increasingly difficult market conditions. This meant we were unable to meet our original targets for revenue and EBIT. Nonetheless, our new products continue to be very well received by the market. We will continue to strive for technologically leading designs with our engines and to further enhance our product range. However, this will be possible with considerably lower development expenditure. We do not regard the key figures for 2015 as satisfactory overall. Year on year, new orders were down by 11.1 per cent, revenue fell by 18.5 per cent to €1,247.4 million and unit sales dropped by almost 30 per cent to 137,781 engines. We had already planned for lower demand resulting from the advance production of engines in 2014, but this effect was compounded by a strong reluctance to invest on the part of our end customers in the second half of the year. On a positive note, however, we have succeeded in structuring the DEUTZ Group in such a way that it can still generate a profit even with a significantly lower volume of business. Operating profit (EBIT before one-off items) decreased from €31.7 million to €4.9 million. The EBIT margin was 0.4 per cent. Although net income fell to €3.5 million in 2015 (2014: €19.5 million), it was still in positive territory. Free cash flow amounted to €35.0 million in the reporting year. In operational terms, we continued as planned with the measures to optimise the network of sites in Germany and with the consolidation of our activities in China. We will continue to focus on increasing quality and efficiency in the DEUTZ Group. On that basis, we believe that we will benefit across the board in the event of a market recovery.

EVENTS AFTER THE REPORTING PERIOD

No events occurred after 31 December 2015 that had a material impact on the financial position or financial performance of the DEUTZ Group.

EMPLOYEES

Overview of the DEUTZ Group's workforce

Headcount

	31 Dec 2015	31 Dec 2014
DEUTZ Group	**3,730**	**3,916**
Thereof		
In Germany	2,910	3,093
Outside Germany	820	823
Thereof		
Non-salaried employees	2,221	2,338
Salaried employees	1,401	1,455
Trainees	108	123
Thereof		
DEUTZ Compact Engines	3,050	3,202
DEUTZ Customised Solutions	680	714

Number of employees adjusted to lower level of production At the end of 2015, the DEUTZ Group employed a total of 3,730 people, 186 fewer than at the end of 2014 (a fall of 4.7 per cent). As at 31 December 2015, we also had a further 151 people on temporary employment contracts, compared with 288 a year earlier. By offering fixed-term contracts and employing temporary workers, DEUTZ can respond flexibly to any fluctuations in demand. Around 6 per cent of all staff at DEUTZ had fixed-term or temporary contracts as at 31 December 2015.

78 per cent of our workforce is employed in Germany. Most of these employees are based in Cologne – 2,269 as at 31 December 2015. 410 employees are based at the Ulm facilities. Of the 820 employees outside Germany, 432 of them work at our DEUTZ SPAIN subsidiary.

DEUTZ Group: Breakdown of workforce by location

Headcount

	31 Dec 2015	31 Dec 2014
Cologne	2,269	2,422
Ulm	410	387
Other	231	284
In Germany	**2,910**	**3,093**
Outside Germany	820	823
Total	**3,730**	**3,916**

Looking at it by segment, DEUTZ Compact Engines employed 3,050 people as at 31 December 2015, 4.7 per cent fewer than it had employed a year earlier. The number of employees at DEUTZ Customised Solutions was 680, down by 4.8 per cent compared with the end of 2014.

Optimisation of sites going to plan On 20 June 2015, the first stage in the relocation of the plant in Übersee on Lake Chiemsee to Ulm was completed. The number of employees at the Übersee plant decreased by 68 in total. We were able to convince 15 employees to continue their work at the Ulm plant, on either a temporary or a permanent basis. Another 24 employees, after leaving DEUTZ, moved to the interim employment company that we had engaged.

Construction of the new shaft centre in Cologne-Porz is also proceeding according to schedule. The first employees have transferred to their new workplaces in Cologne-Porz as part of the relocation of the Cologne-Deutz site. The company medical service and the workplace health and safety department have already moved to Cologne-Porz.

Short-time working extended As the level of orders on hand remains weak, short-time working on the assembly line in Cologne was continued throughout 2015. Short-time working was also implemented in a number of development departments, depending on the work situation. From October 2015, short-time working was also introduced in the sales, service, administrative and support departments.

At our production facility in Zafra, Spain, agreement was reached with the works council for twelve days of short-time working in the fourth quarter of 2015 and 24 such days in 2016.

Excellent training at DEUTZ A solid level of training provides young people with the foundations for their future career. That is why we actively support vocational training by offering training in a variety of technical and engineering occupations to people embarking on their careers with our Company. The apprenticeships that we provide at our sites in Germany range from electronics and metalworking to warehouse logistics and mechatronics. Last year, 27 young women and men chose to train in our Company. The Cologne site employed 71 apprentices, while our plant in Ulm employed 20. We employed seven apprentices at the components plant in Herschbach (Westerwald) and ten at the Xchange plant in Übersee, Bavaria.

In addition to investing in these young people's futures, we also offer training for apprentices at other companies. Our training centre in Cologne is currently providing full-time or part-time vocational training in metalworking occupations to apprentices from twelve other local companies.

In 2015, our overall ratio of trainees to other employees was 3.7 per cent in Germany (2014: 4.0 per cent). All apprentices and trainees passing the final examination were given a permanent employment contract.

We are particularly pleased that a DEUTZ trainee was once again honoured by the Cologne Chamber of Industry and Commerce (IHK) for his top performance as a skilled metal worker apprentice. For the fifth year in succession, the DEUTZ training centre also received a Best Performer accolade from the Cologne IHK in recognition of its outstanding results in introductory vocational training. These accomplishments also meant that DEUTZ was pitted against the winners from all 16 IHKs in North Rhine-Westphalia. And here too, our metalworking apprentice and our instructors were among the winners of the coveted 'best of 2015' awards in Essen.

We aim to make young people with an interest in technology aware of our Company's attractive training programmes while they are still at school. That is why we took part in various training fairs and careers information events again last year. For example, our instructors and apprentices participate in initiatives such as the 'Erlebniswelt Maschinenbau' open day, enabling potential apprentices to speak to them in person.

With an intake of twelve trainees in its fourth year, the dual vocational training initiative at our Zafra plant in Spain continues to go from strength to strength. The aim is for the trainees to be taken on as foremen at the plant once they have completed the training. We also introduced a government-approved programme in which our production employees can improve their basic qualifications by obtaining certification as a machine operator. In future, this certification will be mandatory for those applying for a permanent employment contract at our Spanish subsidiary.

Recruitment activities remain successful Last year, we again participated in two of the most prestigious university fairs in North Rhine-Westphalia in order to make contact with students and graduates. By attending 'meet@thköln' in Cologne and 'bonding' in Aachen, we were again able to find students to help out in various areas of the Company. In 2015, there were 214 interns employed in our Company, of whom 26 students wrote their bachelor dissertations with us and eleven wrote their master's dissertations. A total of 62 students spent a practical semester at DEUTZ.

For many years, we have been striving to attract young women to engineering careers by taking part in events such as Girls' Day, when we demonstrate the diverse and exciting nature of a vocational apprenticeship in an engineering company. In 2015, two more young women started engineering apprenticeships with us, while a business administration trainee began her training in Ulm. Currently, around 7.4 per cent of apprentices at DEUTZ are female.

Rewards for creativity Our bonus-based ideas management system gathers creative suggestions for improvement from DEUTZ employees. Last year, they submitted 669 ideas – a wealth of creativity that pays off.

Investing in people In 2015, we pressed ahead with our talent programme, the purpose of which is to ensure the Company remains an attractive option for talented employees and to develop strong candidates internally through structured career planning. We also updated the succession planning at departmental manager level and used the talent programme to select potential successors. As a result, four employees from our talent pool were promoted to managerial positions.

We also significantly expanded the range of training courses available to employees. Having analysed the specific requirements in cooperation with managers from different areas of the Company, we significantly expanded the range of training courses available to employees. Sixty-nine courses were attended by 638 participants. The training ranges from seminars on DEUTZ-specific know-how and selected technical subjects to language courses and courses for improving methodological and interpersonal skills.

To upgrade the skills of our shop-floor staff, we continued to work with a training provider that specialises in production management and lean management and again made good use of the seminars on occupational health and safety offered by the professional association for the wood and metal industries.

We also stepped up our manager development activities in 2015. Firstly, we significantly increased the number of seminars for managers, which included management seminars for young managerial talent and project managers as well as management training courses designed specifically for different hierarchy levels. Secondly, we shone the spotlight on our principles of leadership and cooperation, and discussed with executive managers how they should implement the principles in their areas of responsibility.

Cross mentoring successfully completed Having begun in 2013, the intercompany programme to promote the advancement of women finished on a positive note last year, with the women who participated citing their increased visibility within their companies, the constructive discussions with mentors from other companies and the chance to broaden their horizons through various programme activities. The two mentors and mentees from DEUTZ AG concluded that they had gained invaluable new experience and that the cross-mentoring programme had helped with their personal development.

DEUTZ has long been committed to diversity management: we value the diversity of our individual employees around the world, in terms of gender, origin, age, religion and disability, and we try to harness this for the success of the Company. For example, we have a clear target to increase the number of management positions within the DEUTZ Group that are occupied by women. Further information can be found in the corporate governance report on page 133 et seq. of this annual report.

Ongoing health promotion initiatives The ‘Ergonomics in the workplace’ project, which was initiated in 2013, continued to run successfully in its third year. It has now become established at all of our plants in Cologne. The focus was on running the project on an ongoing basis so as to yield positive results for employees’ health year after year.

The health committee also decided to offer a further programme of colon cancer screening in summer 2015, a preventive measure that once again was very well received.

The psychosomatic consultations offered in Ulm proved useful. If the company doctor confirms that a short-term intervention is necessary, appointments with a psychologist or at the psychosomatic outpatient clinic at Ulm University Hospital can be organised at short notice so that employees can receive the help they require.

HRS Business Run 2015 The HRS Business Run again took place on 13 August 2015 at the Rhein Energie stadium in Cologne. There was another high turnout from DEUTZ of 252 employees. The event was a resounding success and all employees thoroughly enjoyed themselves.

CORPORATE SOCIAL RESPONSIBILITY

Corporate social responsibility has a long tradition at DEUTZ. As a corporate citizen with operations around the world, we are aware of our duties and obligations. We assume responsibility for our decisions and our actions, for our products and services, for our customers and lenders, for the environment and for the society in which we live. We have been involved in corporate citizenship projects for many years, not only in our home region in the area around Cologne but also throughout Germany and beyond.

Engine museum always popular with visitors The number of visitors to the DEUTZ engine museum rose again last year. It explains the origins and history of global motorisation and displays original machines from the early days of the engine. This all started more than 150 years ago with the founding of N.A. Otto & Cie., the predecessor of today's DEUTZ AG.

On 12 June 2015, DEUTZ again took part in the 'Nacht der Technik' engineering and technology evening along with other companies. Visitors were able to take a guided tour of our engine museum and the assembly hall at our Cologne-Porz site.

Getting young people and the unemployed into careers For almost 25 years, we have been working with IN VIA – an association under the auspices of the German Caritas organisation – and the German Federal Employment Agency to provide career preparation courses for young people with learning and social difficulties. In 2015/16, a total of 36 participants underwent basic metalwork training over a ten-month period at the DEUTZ training centre, which equipped them with a wealth of skills needed to take up a career.

Valuable and important contribution from people with disabilities DEUTZ has successfully worked with NOSTRA GmbH for more than 30 years. People with disabilities work as full and equal employees at DEUTZ AG's Cologne-Kalk site, where they carry out the final assembly and packing for the entire range of engine spare parts. Day in, day out, they prove that people with disabilities can make a valuable, economically viable contribution in the modern world of work. The tasks include packing small and large engine parts and assembling gasket sets and spare parts kits. Around 50 full-time employees now perform a variety of tasks, and highly complex certification standards, such as DIN EN ISO 9001, have been achieved.

DEUTZ has also successfully worked in partnership with GWK, a not-for-profit organisation based in Cologne, for more than 40 years. At the Bergisch Gladbach site, 62 people work on DEUTZ packing and assembly orders. Around 2,500 different articles are packed, weighed and labelled. Approximately 35 people use machines to produce additional articles such as belt pulleys and oil level gauges. In Cologne-Gremberg, a further 15 people handle printing orders. The many different work steps enable the integration of employees with a variety of abilities who benefit from the continuity of the repetitive tasks.

Employee engagement DEUTZ has always contributed to various charitable projects, especially in the run-up to Christmas. In November, we launched an internal donation campaign entitled 'DEUTZ helps' in aid of refugees. Together with the Cologne branch of the German Red Cross (DRK), we called on employees to donate urgently required items. Our employees responded brilliantly, enabling both a van and another vehicle to be filled to the roof with donated items and handed to the DRK.

As part of our 'DEUTZ fulfils your wish' initiative, we again transformed the Christmas tree in our reception area into a 'DEUTZ wishing tree' in December. Around 130 children from a local support centre for children, young people and disabled people wrote down their Christmas wishes on lovingly decorated 'wish notes' that were then hung on our wishing tree. Once again, our employees demonstrated their compassion and fulfilled all of the children and young people's wishes.

High-profile performances by the DEUTZ choir The DEUTZ choir has now been singing for almost 70 years. It was founded in March 1946 as a group of just eight enthusiastic singers, quickly growing into a powerful men's choir with more than 100 active members. Last year, the DEUTZ choir hosted a large opera gala at the Cologne Philharmonic Hall on 6 and 7 June. The choir was accompanied by the Bonner Operisten and Collegium Cantandi choirs along with the Württembergische Philharmonie Reutlingen orchestra. On 12 and 13 December, the choir gave further outstanding performances at its three Advent concerts in Cologne-Gürzenich, at which it was joined by the Domstadt Philharmoniker orchestra. At the concerts, a collection was made for the Kölner Klinikclowns charity.

The members of the Board of Management and managers at DEUTZ AG are fully aware of their responsibility to lead by example. For many years, they have been personally involved in various charitable associations, trade associations, committees, trusts and other forums.

ENVIRONMENT

Protection of the environment and the prevention of climate change are key corporate objectives for DEUTZ. We manufacture environmentally responsible products that meet the latest emissions standards and even future emissions standards and therefore make a vital contribution to protecting the environment. Our production processes are also resource-efficient. More than ten years ago, DEUTZ decided to implement an environmental management system as a way of contributing effectively to environmental protection. The system keeps track of aspects that are highly relevant to the environment, such as keeping the air clean, avoiding and correctly disposing of waste, protecting against soil and water pollution and sustainably reducing energy consumption.

ENERGY MANAGEMENT SYSTEM

We have successfully deployed our energy management system at our Cologne sites since 2013, and it first achieved certification in November of that year. In April 2015, as part of the annual quality and environmental audit, the certification body DNV GL once again accredited the energy management system without any reservations. As planned, the ISO 50001 certificate was then extended to all German sites. This means that we also satisfy the provisions of the German Energy Services Act (EDL-G), which requires all companies categorised as being larger than an SME to conduct energy audits.

The ongoing expansion of additional meter infrastructure enables energy to be monitored and, at the same time, provides a transparent overview of all energy flows. Additional potential was identified by implementing a variety of technical and organisational measures last year. The resulting annual savings amount to 775 MWh of electricity and 1,116 MWh of heat.

However, the potential for further savings is still far from exhausted: additional efficiency measures and the final phase in the expansion of the monitoring system are already being planned for 2016. New opportunities for savings will be opened up by the closure of the Cologne-Deutz site and the associated relocation of some manufacturing operations to the new production hall at the Cologne-Porz site, which is being built in accordance with the latest requirements under the German Energy Saving Regulation (EnEV).

DEUTZ Group: Energy consumption in our plants [1]

MWh

	2015	2014
Electricity[2]	77,388	87,944
Natural gas	34,243	34,768
District heating	23,857	22,596
Heating oil	3,788	3,456
Diesel fuel[3]	21,252	32,313

[1] Plants in the DEUTZ Group, excluding joint ventures.
[2] Recovered energy has been subtracted.
[3] At 9.85 kWh/litre (mean).

ENVIRONMENTAL MANAGEMENT SYSTEM

In April 2015, external environmental auditors from the certification body DNV GL found once again that DEUTZ AG's environmental management system conforms to the international ISO 14001 standard. For the first time since the environmental management system was implemented, a main target was defined and quantified in 2015: a year-on-year reduction of CO_2 emissions by at least 2.0 per cent per engine.

A comparison of total annual emissions shows that CO_2 emissions have gone down by around 13 per cent. This trend correlates closely with the production programme, which was smaller than in 2014.

CO_2 emissions per engine (Scopes 1–3) increased to 460kg in 2015 (2014: 365kg). The targeted reduction in CO_2 emissions of 2 per cent per unit of production was not achieved because we have an underlying energy requirement for the production of our engines (Scope 2 emissions) that applies regardless of the size of a production programme.

The closure of the site in Cologne-Deutz and the construction of the new shaft centre at the Porz plant are expected to lead to a significant improvement in our carbon footprint. DEUTZ is therefore continuing to pursue its target of a 2 per cent reduction in CO_2 per engine in the coming reporting year.

DEUTZ Group: Annual CO_2 emissions in our plants [1]

Tonnes

	2015	2014
CO_2 emissions (Scope 1)	13,251	16,289
CO_2 emissions (Scope 2)	51,070	57,021
CO_2 emissions (Scope 3)	531	1,528
Total CO_2 emissions	65,134	77,463

Scope 1: CO_2 emissions caused by combustion in our own facilities.
Scope 2: CO_2 emissions relating to purchased energy (e.g. electricity, district heating).
Scope 3: CO_2 emissions from flying and the use of hire cars.
[1] Plants in the DEUTZ Group, excluding joint ventures.

FURTHER IMPROVEMENT OF AIR PURITY

Over and above the effects of the production programme, emissions of dust, carbon dioxide, benzene and nitrogen oxide have decreased substantially as a result of particularly low-emission engines being tested and a shortening of the testing times in the test bay.

DEUTZ Group: Emissions per engine in our plants [1]

Emissions per engine

	2015	2014
CO_2 (kg)	460	365
Nitrogen oxide (kg)	0.128	0.140
Dust (g)	2.6	2.7
Benzene (mg)	44.8	48.6

[1] CO_2 emissions in plants in the DEUTZ Group. All other figures relate to German plants.

A variety of individual technical and organisational measures made it possible to shorten the testing times. To further reduce emissions and costs, we are planning to carry out cold testing[2] of some of our products in the production test bays in Cologne. The construction of a laboratory for exhaust after-treatment technology, which contains a model gas testing rig, enables the simulation of engine emissions for bench-scale testing. This saves on various test runs at the development stage.

In order to satisfy customers' requirement for even more eco-friendly engine technologies, DEUTZ AG has converted four of its test cells so that engines can be tested with LPG as part of research and development. The advantage in terms of air purity is obvious: LPG-powered engines do not emit any dust.

FOCUS ON WATER POLLUTION CONTROL

We ensure the safe operation of all equipment to which the German Federal Water Act (WHG) applies by having them inspected regularly by experts from a central monitoring agency. This not only ensures the necessary technical requirements for safe operation are in place but also reduces the likelihood of equipment downtimes.

The retirement and deinstallation of the electroplating plant in Cologne-Deutz significantly lowered environmental risk during the reporting year. The deinstallation of the electroplating equipment and the transfer of some of it to the new location of the external service provider were carried out in close cooperation with the local environmental authorities – a model example of collaborative partnership.

In the last stage of its expansion, the R&D testing centre's cellars were extensively refurbished. The work was undertaken in order bring the equipment-specific water pollution controls in line with the latest technology. This predominantly involved replacing waste water pipes and recoating the floors, which have to resist penetration by substances that could pollute the water. Just under €0.2 million was invested in these measures.

Use of resources improved again The recooling plant, which supplies the R&D testing centre with water for cooling, had previously been operated using an open recirculating cooling system. Besides the loss of water resulting from this process, the outdated machinery consumed a lot of electricity. We completed the installation of a closed recirculating cooling system and the replacement of the inefficient circulating equipment last year. Just under €0.3 million was invested in this construction work. The ongoing benefits of this measure – reduced water consumption at the Cologne-Porz site and lower consumption of electrical energy – will help to conserve the resources available to our Company in the long term.

[2] Functional testing of the engine without initiating the combustion process.

Target for a continuous decrease in waste The high standards of quality that we insist on for the products obtained from our suppliers require them to be adequately protected during transit. We therefore cannot do away with packaging completely. Nonetheless, we want to reduce it steadily and thereby lower the volume of waste that we expect to produce. We examine, on a case-by-case basis, whether returnable packaging systems (e.g. return of empty containers) can be used instead of non-reusable packaging and introduce them where possible. Last year, we invested €0.5 million in additional returnable packaging (2014: €1.1 million). Another example of successful waste reduction is the storage of the fuel additive AdBlue[1] in a 5m³ tank. €110 thousand was invested in the installation of this facility. In addition to a reduction in the cost of disposing of non-reusable packaging, there are savings from the reduced logistics, mainly derived from a decrease in the number of orders processed.

SAFETY MANAGEMENT

The Board of Management has defined a key target for workplace health and safety of zero accidents, an extremely challenging objective that is designed to set an example. The introduction of this target has resulted in a steady improvement in the frequency of accidents[2] and the number of notifiable accidents per thousand employees (TMQ)[3]. Accident frequency, which is the number of notifiable workplace accidents in relation to the number of hours worked, stood at 12.9 in 2015 (2014: 20.8), its lowest level since we began recording statistics on workplace health and safety. The number of notifiable accidents per thousand employees went down to 17.7 (2014: 26.1) and is now around 30 per cent below the current average for the companies insured by our industry-specific accident insurer BGHM (Berufsgenossenschaft Holz und Metall).

Internal health, safety and environment audits are conducted regularly, resulting in improved safety standards. The frequency of these audits depends mainly on the level of risk in the area being audited. Any variances from internal or statutory rules are followed up rigorously on the basis of action plans. The health, safety and environment departments must be involved in processes for approving hazardous materials and signing off machinery and equipment. Risk assessments are reviewed regularly and are adapted as the need arises. Personal protective gear is specified for each function and has been chosen based on an analysis of accidents.

Irrespective of the preventive measures taken with regard to health and safety, DEUTZ AG also has an emergency organisation consisting of full-time and ad-hoc staff. The linchpin of this organisation is the DEUTZ AG works fire brigade, which is officially recognised by the German authorities. Internal and external training is provided to ensure employees have the necessary skills and qualifications.

DEUTZ AG

The following remarks refer to the annual financial statements of DEUTZ AG. The annual financial statements of DEUTZ AG are prepared in accordance with the requirements of the German Commercial Code (HGB).

BASIC PRINCIPLES AND BUSINESS PERFORMANCE OF DEUTZ AG

DEUTZ AG is the parent company of the DEUTZ Group. At home and abroad, DEUTZ AG has various direct and indirect subsidiaries and equity investments. The subsidiaries include a production facility in Spain, a production company in China and several companies that perform sales and service functions. The Chinese production company DEUTZ Engine (China) Co., Ltd. in Linyi, China, was wound up at the end of 2015. DEUTZ AG has a direct or indirect stake in a total of 27 companies (2014: 29 companies). It is also by far the largest production company of the DEUTZ Group and provides the head-office functions for the Group.

Because the business performance and financial situation of DEUTZ AG are essentially the same as for the DEUTZ Group, we make reference here to the ‘Business performance in the DEUTZ Group’ section on page 32 et seq. of this combined management report.

Because of the significance of DEUTZ AG within the Group, and its heavy interdependencies with other Group companies, the Group is managed at the level of DEUTZ AG. In addition to the key performance indicators used for management at Group level, the net income of DEUTZ AG, as the relevant variable in the payment of dividends, is also an element of the management system of the Company. The internal management system for the DEUTZ Group is described on page 31 et seq. of this combined management report. The DEUTZ Group’s net income in accordance with IFRS is reconciled to DEUTZ AG’s net income in accordance with the German Commercial Code (HGB):

DEUTZ AG: Reconciliation

€ million	
DEUTZ Group net income (IFRS)	**3.5**
Consolidation of equity investments	10.7
DEUTZ AG income (IFRS)	**14.2**
Material differences due to different financial reporting standards	
Recognition of development expenditure	34.4
Measurement of provisions for pensions and other post-retirement benefits	–16.4
Other differences relating to the financial reporting standards	–5.4
DEUTZ AG net income (HGB)	**26.8**

[1] 32.5% aqueous urea solution (AdBlue® is a registered trade mark of the German Association of the Automotive Industry [VDA])
[2] Accident frequency: number of accidents per million hours worked (as defined by the employers’ liability insurance association).
[3] Known as TMQ (Tausend-Mann-Quote) in German.

RESULTS OF OPERATIONS

Overview of DEUTZ AG's results of operations

€ million

	2015	2014
Revenue	**1,118.6**	**1,437.8**
Cost of sales	–976.4	–1,280.6
Research and development costs	–43.6	–54.0
Selling and administrative expenses	–71.9	–68.8
Other operating income	40.8	31.1
Other operating expenses	–33.6	–15.9
Net investment income	5.6	–7.3
Write-downs of investments	–	–0.7
Operating profit (EBIT)	**39.5**	**41.6**
Interest expenses, net	–8.2	–11.6
Profit from ordinary activities	**31.3**	**30.0**
Extraordinary items	–2.3	–19.4
Income taxes	–1.7	15.0
Other taxes	–0.5	–1.2
Net income	**26.8**	**24.4**

Revenue In 2015, the revenue generated by DEUTZ AG came to €1,118.6 million, 22.2 per cent less than in the previous year (2014: €1,437.8 million). This decrease was largely driven by lower demand in our largest application segment, Mobile Machinery, and in the Agricultural Machinery application segment. In the Mobile Machinery application segment, revenue was down by 30.7 per cent to €470.0 million (2014: €677.8 million). Agricultural Machinery saw an even bigger drop of 38.8 per cent to €157.6 million (2014: €257.6 million). This decline in revenue is due partly to the changes to emissions standards for engines under 130kW that came into force in the European Union on 1 October 2014 and the resulting effects from the advance production of engines. Furthermore, the current reluctance to invest shown by end customers means that the inventories of a number of European customers are being used up more slowly.

Asia-Pacific was the only region to report a gain, with revenue there rising by a substantial 22.7 per cent to €113.1 million. By contrast, revenue in EMEA (Europe, Middle East and Africa) and the Americas went down by 28.6 per cent and 7.0 per cent to €810.5 million and €195.0 million respectively.

Earnings performance In 2015, DEUTZ AG generated an operating profit (EBIT) of €39.5 million (2014: €41.6 million). This year-on-year decline of €2.1 million was mainly attributable to the considerably lower business volume and interest-rate-related increases in expenses resulting from adjustments to provisions for pensions and other post-retirement benefits. Earnings were boosted, however, by lower production costs and warranty costs, greatly improved net investment income and lower research and development costs.

Earnings before interest, tax, depreciation and amortisation (EBITDA) at DEUTZ AG amounted to €93.5 million in 2015, compared with €89.7 million in 2014.

Cost of sales DEUTZ AG's cost of sales came to €976.4 million in 2015 (2014: €1,280.6 million). The year-on-year decline of €304.2 million was mainly attributable to the volume-related drop in costs for materials, staff and contract workers. There was also a substantial decrease in warranty costs. As a percentage of revenue, the cost of sales improved year on year from 89.1 per cent to 87.3 per cent.

Research and development costs Research and development costs fell by €10.4 million year on year to €43.6 million (2014: €54.0 million). Research and development costs largely comprised staff costs and cost of materials. Investment grants received and capitalised development expenditure were deducted. Unlike the development expenditure in the DEUTZ Group, which is recognised in accordance with IFRS requirements, the development expenditure in DEUTZ AG is recognised in accordance with HGB provisions and only expenditure relating to projects that started after initial application of the German Accounting Law Modernisation Act (BilMoG) at DEUTZ AG is capitalised.

Selling and administrative expenses Selling and administrative expenses in 2015 came to €71.9 million, an increase of €3.1 million compared with the previous year (2014: €68.8 million). The main factor in this rise was the recognition of one-off transition costs in connection with the switch of IT service provider at the end of the year under review. When measured as a proportion of revenue, selling and administrative expenses also went up year on year, from 4.8 per cent in 2014 to 6.4 per cent in 2015.

Other operating income The reporting year saw an increase of €9.7 million in other operating income to €40.8 million (2014: €31.1 million). This was predominantly due to the reduction in the provisions for warranty costs. Furthermore, a gain on disposal of €2.8 million was recognised following the disposal of the shares in WEIFANG WEICHAI-DEUTZ DIESEL ENGINE CO., LTD. in Weifang, China, in 2015.

Other operating expenses Other operating expenses were up year on year, advancing by €17.7 million to €33.6 million (2014: €15.9 million). This rise was mainly the result of higher expenses in connection with foreign-currency transactions and adjustments to provisions for pensions and other post-retirement benefits because of changes in measurement parameters. However, the foreign currency losses were offset by a similar level of foreign currency gains, which are reported in other operating income.

Net investment income Net investment income was up significantly on the previous year, climbing by €12.9 million to €5.6 million (2014: minus €7.3 million). This was due, in particular, to the fact that net investment income in the prior year was adversely affected by the reduction in the carrying amounts for the equity investments DEUTZ Engine (Shandong) Co., Ltd. and DEUTZ Engine (China) Co., Ltd. at the level of the holding companies DEUTZ Asien Verwaltungs GmbH and DEUTZ Engine China GmbH.

Net interest expense Net interest expense amounted to €8.2 million (2014: net expense of €11.6 million). This year-on-year improvement of €3.4 million was mainly attributable to lower utilisation of credit lines.

Extraordinary items In the reporting year, extraordinary items amounted to minus €2.3 million (2014: minus €19.4 million) and comprised the annual addition to the provisions for pensions and other post-retirement benefits of the difference arising under the initial application of BilMoG. This difference came about as a result of the remeasurement of the provisions for pensions and other post-retirement benefits on 1 January 2010. Extraordinary items in the previous year also included expenses in connection with the optimisation of our sites.

Income taxes Income taxes came to €1.7 million in the year under review. The current tax expense of €2.7 million was partly offset by deferred tax income of €1.0 million.

Net income Owing to the sharp drop in extraordinary expenses, the net income for the reporting year increased slightly, rising by €2.4 million year on year to €26.8 million (2014: €24.4 million). This movement was in line with the forecast that we had made at the start of 2015.

In view of the positive level of net income, the Board of Management and Supervisory Board propose using €8.5 million of the accumulated income for the financial year to pay a dividend of €0.07 per share.

FINANCIAL POSITION

Overview of DEUTZ AG's financial position

€ million

	2015	2014
Cash flow from operating activities	88.7	85.2
Cash flow from investing activities	–41.0	–23.0
Cash flow from financing activities	–23.9	–19.1
Change in cash and cash equivalents	23.8	43.1
Free cash flow	46.7	58.8
Cash and cash equivalents at 31 Dec	97.7	73.9

Free cash flow: cash flow from operating and investing activities less net interest expense.

Financial management in the DEUTZ Group is one of the core functions of the Group, and DEUTZ AG holds responsibility for this function. The basic principles and objectives of financial management at DEUTZ AG are therefore largely the same as those of the Group, as is the funding of DEUTZ AG. In this regard, please refer to the relevant sections on page 43 et seq. of this combined management report.

Liquidity Cash flow from operating activities amounted to €88.7 million last year (2014: €85.2 million). The small increase of €3.5 million compared with 2014 was mainly due to the lower level of working capital.

The cash flow from investing activities in 2015 was minus €41.0 million (2014: minus €23.0 million). This increased outflow of €18.0 million was attributable, in particular, to higher cash payments in connection with capital expenditure on property, plant and equipment.

Cash flow used for financing activities in 2015 totalled €23.9 million (2014: €19.1 million). This advance was largely due to substantially higher payments of principal in relation to existing financial liabilities than in the prior year. As in the previous year, cash flow used for financing activities included a dividend payment to shareholders of €8.5 million.

Free cash flow decreased year on year, falling by €12.1 million to €46.7 million (2014: €58.8 million) due, above all, to increased capital expenditure.

Capital expenditure After deducting investment grants, DEUTZ AG's capital expenditure in 2015 amounted to a total of €52.9 million (2014: €32.9 million). As in 2014, spending primarily related to property, plant and equipment, and the amount of €42.2 million (after deducting grants) spent on these assets was considerably higher than in the previous year (2014: €30.0 million). The investing activities relating to property, plant and equipment focused on measures aimed at optimising our network of sites, such as the construction of the shaft centre in Cologne-Porz. There were also additions in connection with replacement investments in machinery and tools.

NET ASSETS

Overview of DEUTZ AG's net assets

€ million

	31 Dec 2015	31 Dec 2014
Non-current assets	493.4	502.0
Current assets	408.0	404.5
Prepaid expenses	1.8	2.0
Deferred tax assets	86.3	85.3
Total assets	**989.5**	**993.8**
Equity	472.2	453.9
Provisions	269.4	284.0
Liabilities	247.5	255.3
Deferred income	0.4	0.6
Total equity and liabilities	**989.5**	**993.8**
Working capital (€ million)	67.7	80.6
Working capital ratio (31 Dec, %)	6.1	5.6
Equity ratio (%)	47.7	45.7

Working capital: inventories plus trade receivables less trade payables.
Equity ratio: equity / total equity and liabilities.

Non-current assets Non-current assets at 31 December 2015 amounted to €493.4 million (31 December 2014: €502.0 million). The year-on-year decrease of €8.6 million was mainly due to the lower figure for investments. Following the winding-up of DEUTZ Engine (China) Co., Ltd. in Linyi, China, an amount of approximately €5.0 million was withdrawn from the additional paid-in capital of the holding company, DEUTZ Engine China GmbH, and repaid to DEUTZ AG. There was a corresponding decrease in the carrying amount of the equity investment in DEUTZ Engine China GmbH.

Current assets As at 31 December 2015, current assets amounted to €408.0 million. This increase of €3.5 million compared with twelve months earlier (31 December 2014: €404.5 million) mostly resulted from the higher volume of cash and cash equivalents and inventories held on 31 December 2015. However, it was largely offset by a decline in trade receivables and other assets.

Working capital Working capital as at 31 December 2015 was €67.7 million (31 December 2014: €80.6 million), a year-on-year decrease of €12.9 million. The main reason for this was the reduction in trade receivables caused by lower demand. The drop in demand also resulted in higher inventories, as there is a time delay between a fall in demand and the scaling back of inventory orders. Trade payables, however, changed only insignificantly. There was an increase in the working capital ratio, i.e. the ratio of working capital (inventories plus trade receivables less trade payables) to revenue despite the drop in working capital. This was due to the reduced volume of business. As at the balance sheet date[1], this ratio was 6.1 per cent compared with 5.6 per cent as at 31 December 2014.

Deferred tax assets The €1.0 million rise in deferred tax assets arose, in particular, from temporary differences between carrying amounts in the tax accounts and in the financial statements under HGB. The carrying amounts in question included those for inventories and those for provisions for pensions and other post-retirement benefits.

Equity ratio Owing to the positive level of net income, equity advanced by €18.3 million to €472.2 million (31 December 2014: €453.9 million). The equity ratio increased slightly to reach 47.7 per cent (31 December 2014: 45.7 per cent).

Provisions At 31 December 2015, provisions stood at €269.4 million (31 December 2014: €284.0 million). This year-on-year decrease of €14.6 million was primarily attributable to the reduction in provisions for potential warranty claims in the future.

Liabilities As at 31 December 2015, liabilities had fallen by €7.8 million to €247.5 million (31 December 2014: €255.3 million). The main factor here was the decline in liabilities to banks, which were scaled back as planned.

EVENTS AFTER THE REPORTING PERIOD

No events occurred after 31 December 2015 that had a material impact on the net assets, financial position or results of operations of DEUTZ AG.

EMPLOYEES

As at 31 December 2015, a total of 2,943 people[2] were employed by DEUTZ AG. This meant that the number of employees had fallen by 182 year on year (31 December 2014: 3,125 employees). We also had a further 124 people on temporary employment contracts as at 31 December 2015, compared with 252 a year earlier. Employing temporary workers enables us to respond flexibly to any fluctuations in demand.

Looking at it by segment, DEUTZ Compact Engines employed 2,454 people as at 31 December 2015, 153 fewer than it had employed a year earlier. The number of employees at DEUTZ Customised Solutions was 489, down by 29 year on year.

[1] Working capital ratio as at the balance sheet date: ratio of working capital (inventories plus trade receivables less trade payables) at the end of the reporting period to revenue for the preceding twelve months.
[2] Number of employees incl. apprentices and trainees.

OPPORTUNITY AND RISK REPORT

DEUTZ AG is integrated into the risk management system of the DEUTZ Group. As a head-office function, risk management for the Group is performed by DEUTZ AG. Information about the structuring and mechanics of the risk management system and of risk management with regard to financial instruments can be found in our notes on page 61 et seq.

Because DEUTZ AG is closely integrated with the other Group companies, its risk situation is essentially the same as that of the Group. Risks arising from subsidiaries may have an effect on DEUTZ AG because of the carrying amount of an equity investment, reduced dividend payments and the internal business relations. The risks and opportunities associated with the DEUTZ Group are described on pages 62 to 65 of this combined management report.

Information about DEUTZ AG's internal accounting-related control system and about risk management with regard to the use of financial instruments at DEUTZ AG can be found on page 64 et seq. of this combined management report.

OUTLOOK

DEUTZ AG performs the head-office functions of the DEUTZ Group and is the biggest production company within the Group by some margin. Because of DEUTZ AG's wide-ranging relationships with other Group companies and because of its size within the Group, the expectations presented in the Group outlook for 2016 are essentially the same as those for DEUTZ AG. We therefore anticipate that the revenue of DEUTZ AG will develop largely in line with the statements made for the DEUTZ Group. We forecast net income in 2016 to be in the low double-digit millions, below the 2015 level. Further information can be found in the outlook for the DEUTZ Group on page 65 et seq.

CORPORATE GOVERNANCE DECLARATION PURSUANT TO SECTION 289A HGB

The corporate governance declaration pursuant to section 289a HGB is an integral element of the combined management report. We refer here to our remarks on pages 133 to 138 of the annual report.

DISCLOSURES PURSUANT TO SECTIONS 289 (4) AND 315 (4) HGB

Composition of the issued capital There were no changes to the issued capital (share capital) of DEUTZ AG in 2015. As at 31 December 2015, the issued capital amounted to €308,978,241.98 and was divided into 120,861,783 no-par-value bearer shares.

Direct or indirect shareholdings representing more than 10 per cent of voting rights Since 12 September 2012, AB Volvo of Gothenburg, Sweden, has held 30,246,582 shares in DEUTZ AG, giving it a voting share of 25.026 per cent.

Restrictions affecting voting rights or the transfer of shares According to the information available to us, the transferability of DEUTZ shares held by AB Volvo is restricted by a pre-emption right of the SAME DEUTZ-FAHR Group S.p.A. of Treviglio, Italy.

Legal provisions and Statute provisions regarding the appointment and removal of members of the Board of Management and regarding changes to the Statutes According to articles 7 (1) and 7 (2) of the Statutes of DEUTZ AG:

"(1) The Board of Management shall comprise at least two members.
(2) The Supervisory Board shall determine the number of members of the Board of Management and the allocation of responsibilities. It may draw up and issue rules of procedure."

As far as the appointment and removal of members of the Board of Management are concerned, sections 84 and 85 of the German Stock Corporation Act (AktG) and section 31 of the German Codetermination Act (MitbestG) also apply.

According to article 14 of the Statutes of DEUTZ AG:

"The Supervisory Board may change the wording but not the spirit of the Statutes." Sections 179 and 133 AktG also apply in the case of changes to the Statutes.

Authority of the Board of Management, in particular with regard to share issue or buyback The authority of the Board of Management is derived from the legal provisions and from the rules of procedure laid down by the Supervisory Board.

The Board of Management is currently not authorised to issue or buy back shares.

FURTHER DISCLOSURES

No bearers of shares have any special rights conferring authority to control the Company.

Numerous employees have direct shareholdings in DEUTZ AG. There are no restrictions affecting the direct exercise of rights of control in connection with these shares.

A consortium of banks has provided DEUTZ AG with a syndicated, revolving cash credit line of €160 million. DEUTZ AG also took out a loan with the European Investment Bank that has a remaining balance of €68.4 million. Under the terms of the loan agreements, the lenders can demand that the outstanding loan be repaid within a specified period in the event of a change of control, i.e. one or more people acting jointly acquire a direct or indirect shareholding of at least 50 per cent of all shares and/or voting rights in DEUTZ AG.

If DEUTZ AG needs to repay a considerable proportion of the loans prematurely in the event of a change of control, it needs to raise the necessary funds some other way in the short term.

The service contracts of the Board of Management members Dr Ing Helmut Leube and Dr Margarete Haase stipulate the following provision in the event of a change of control: if their appointment (1) is revoked within nine months of the change of control or (2) ends within nine months of a change to the legal form of DEUTZ AG and subject to certain other requirements, they will receive 150 per cent of the severance cap pursuant to article 4.2.3 of the German Corporate Governance Code. As set out in the service contracts, a change of control is deemed to occur when one or more other people or other companies acting jointly within the meaning of section 30 of the German Securities Acquisition and Takeover Act (WpÜG) acquire more than 30 per cent of the voting rights and therefore control of the Company. No change of control will be deemed to have occurred if the current major shareholder, AB Volvo, or the former major shareholder, the SAME DEUTZ-FAHR Group, acquires more than 30 per cent of the voting rights in the Company.

The long-term incentive plans (LTI), under which the most senior managers in the DEUTZ Group (executives and managing directors of major subsidiaries) are granted virtual options that they can exercise after a vesting period and upon achievement of certain performance targets (see page 116 et seq. of this annual report), contain the following provision in the event of an entity – either alone or acting jointly with an affiliated company – acquiring a minimum of 50 per cent of the shares in DEUTZ AG: provided one of the performance targets has been achieved, the LTI participants may exercise their options within a short time frame after the acquisition, even if the vesting period has not yet expired.

DEUTZ AG has no indemnification agreements with employees that would come into force in the event of a takeover bid.

EXPLANATORY STATEMENT BY THE BOARD OF MANAGEMENT IN CONNECTION WITH SECTIONS 289 (4) AND 315 (4) HGB

The disclosures contained in the combined management report and management report pursuant to sections 289 (4) and 315 (4) HGB relate to arrangements that may be significant in the success of any public takeover bid for DEUTZ AG. It is the opinion of the Board of Management that these arrangements are normal for publicly traded companies comparable with DEUTZ AG.

REMUNERATION REPORT

REMUNERATION OF THE BOARD OF MANAGEMENT

The annual remuneration paid to the members of DEUTZ AG's Board of Management consists of fixed and variable components as well as a pension benefit contribution. The fixed component is paid monthly as basic salary. The variable component is performance-related and consists of two parts: the first is a bonus that is based on attainment of specific targets; the other comes in the form of virtual performance shares that offer a long-term incentive. For the pension contribution, an amount is paid into a benevolent fund; there is no other entitlement to a pension or surviving dependants' pension.

The calculation of the annual bonus is based on the degree of attainment of annual performance targets (short-term targets). The number, content and weighting of the short-term targets are set annually by the Supervisory Board at its due discretion after consulting with the respective Board of Management member. The minimum level of target attainment for the payment of a bonus is 75 per cent; the maximum level of target attainment relevant to the payment of the bonus is 150 per cent. The highest amount that can be paid as a bonus in the case of maximum target attainment is determined by the respective service contract. Only 60 per cent of the annual bonus is paid out at the end of the year. The remaining 40 per cent of the bonus is paid out in two equal instalments, subject to the attainment of further medium-term financial targets (medium-term targets), at the end of a further one year and two years, whereby the amount that is paid out is based on the level of attainment of these medium-term targets, to a maximum of 150 per cent. The highest permissible amounts for these further payments are also contractually agreed. The targets are set at the beginning of the year for which the bonus is to be paid.

Details regarding the virtual performance shares are set forth in a long-term incentive plan for the Board of Management (LTI plan BoM), which forms part of the contractual agreements with the Board of Management members. The number of virtual performance shares allocated to a Board of Management member is calculated each year on the basis of the contractually specified euro amount divided by a reference price. The reference price is the average closing price of DEUTZ AG shares in Xetra trading (or a comparable successor system) on the Frankfurt Stock Exchange during the 60 trading days preceding the grant date. Virtual performance shares represent an entitlement to payment of a cash amount in accordance with the provisions of the LTI plan BoM. The cash amount per virtual performance share corresponds to the average closing price of DEUTZ shares in Xetra trading (or a comparable successor system) on the Frankfurt Stock Exchange during the last 60 trading days prior to the expiry of a vesting period of four years after the grant date, and is limited to a maximum of 1.5 times the reference price. Entitlement to the cash payment only arises, however, if either the market price of DEUTZ shares has increased by at least 30 per cent relative to the reference price or the market price of DEUTZ shares has outperformed the MDAX (or a future index replacing the MDAX) by at least 10 percentage points during the vesting period. A further requirement is that the Board of Management member makes a personal investment by holding one DEUTZ share for every 20 virtual performance shares received.

The variable remuneration is designed in a way that the majority of it is measured against performance over several years. The overall remuneration structure is designed to support the sustainable growth of the Company.

Benefits granted

€ thousand

	Dr Ing Helmut Leube Chairman of the Board of Management			
	2014	**2015**	2015 (min)	2015 (max)
Fixed remuneration	725	725	725	725
Additional benefits[1]	174	175	175	175
Total	**899**	**900**	**900**	**900**
One-year variable remuneration[2]	360	360	–	540
Multi-year variable remuneration				
2015–2016 deferral[2]	240	–	–	–
2016–2017 deferral[2]	–	240	–	360
LTI 2014–2018[3]	196	–	–	–
LTI 2015–2019[3]	–	222	–	300
Total	**796**	**822**	**–**	**1,200**
Total remuneration	**1,695**	**1,722**	**900**	**2,100**

Instead of the target values for one-year variable remuneration and for deferrals from one-year variable remuneration required under the German Corporate Governance Code (DCGK), the figures in the table below for total remuneration indicate the remuneration figures that are required to be disclosed under the applicable accounting standards. For the one-year variable remuneration, these represent the provision for the annual bonus for 2015, adjusted for any over- or under-allocation in the previous year. With regard to the deferrals from the one-year variable remuneration, the figures represent the amounts vested and recognised in provisions in 2015.

One-year variable remuneration	7	227		
2014–2015 deferral	51	26		
2015–2016 deferral	–	23		
2016–2017 deferral	–	–		
Total remuneration	**1,153**	**1,398**		

[1] Includes payment into a life insurance policy.

[2] The figures given for one-year variable remuneration and for deferrals from one-year variable remuneration represent the amount granted for full achievement of targets.

[3] Share-based remuneration represents the fair value of the options on the date of grant. Please refer to Note 30 in the consolidated financial statements for a description of the structure of the share-based remuneration agreements. General contractual conditions are identical for all members of the Board of Management.

Additional benefits received by the members of the Board of Management include, in particular, a company car, reimbursement of travel expenses and allowances towards insurance policies.

If the employment contract of a member of the Board of Management is terminated prematurely without good cause, the member of the Board of Management receives a severance payment equivalent to the total remuneration for the period until the original termination date of his or her contract of employment up to a maximum of two years. For the purpose of this severance payment, the amount of total remuneration is determined by the total remuneration paid for the last full financial year, or the anticipated total remuneration for the then current financial year, if appropriate (cap on severance pay in accordance with article 4.2.3 of the German Corporate Governance Code).

The service contracts of the Board of Management members Dr Ing Helmut Leube and Dr Margarete Haase stipulate a special provision in the event of a change of control. Further details can be found in the section 'Disclosures pursuant to sections 289 (4) and 315 (4) HGB' on page 57.

The table below presents the total remuneration of the Board of Management in accordance with the recommendation in the German Corporate Governance Code dated 5 May 2015. In line with this recommendation, the benefits granted in 2015 and those actually paid are reported separately.

The following table shows the breakdown of benefits granted to members of the Board of Management:

	Dr Margarete Haase				Michael Wellenzohn			
	2014	**2015**	2015 (min)	2015 (max)	2014	**2015**	2015 (min)	2015 (max)
	573	580	580	580	420	420	420	420
	148	147	147	147	107	111	111	111
	721	**727**	**727**	**727**	**527**	**531**	**531**	**531**
	270	270	–	405	210	210	–	315
	180	–	–	–	140	–	–	–
	–	180	–	270	–	140	–	210
	147	–	–	–	127	–	–	–
	–	166	–	225	–	144	–	195
	597	**616**	**–**	**900**	**477**	**494**	**–**	**720**
	1,318	**1,343**	**727**	**1,627**	**1,004**	**1,025**	**531**	**1,251**
	1	138			1	107		
	38	20			25	13		
	–	17			–	14		
	–	–			–	–		
	907	**1,068**			**680**	**809**		

The following table shows the breakdown of benefits actually paid to members of the Board of Management:

Benefits paid

€ thousand

	Dr Ing Helmut Leube Chairman of the Board of Management		Dr Margarete Haase		Michael Wellenzohn	
	2015	2014	**2015**	2014	**2015**	2014
Fixed remuneration	725	725	580	573	420	420
Additional benefits	175	174	147	148	111	107
Total	**900**	**899**	**727**	**721**	**531**	**527**
One-year variable remuneration	227	359	138	192	107	125
Multi-year variable remuneration						
2014–2015 deferral	60	–	45	–	29	–
Total	**287**	**359**	**183**	**192**	**136**	**125**
Total remuneration	**1,187**	**1,258**	**910**	**913**	**667**	**652**

REMUNERATION OF THE SUPERVISORY BOARD

The remuneration paid to the Supervisory Board is specified in article 15 of the Company's Statutes. This stipulates that the members of the Supervisory Board of DEUTZ AG receive fixed annual remuneration of €22,500. They also receive a fee of €2,500 for each Supervisory Board meeting they attend and are reimbursed for their out-of-pocket expenses. The chairman of the Supervisory Board receives double these amounts, and his deputy one-and-a-half times.

In addition, each member of a Supervisory Board committee receives an attendance fee of €2,500 for each committee meeting attended. The chairman of a committee is entitled to twice this sum, his deputy to one-and-a-half times the amount.

In addition, DEUTZ reimburses the members of the Supervisory Board for any VAT they incur in connection with the performance of their mandate.

The following table shows the breakdown of total remuneration paid to members of the Supervisory Board for their work as Supervisory Board members:

€	Fixed remuneration	Attendance fees	**Total**
Lars-Göran Moberg (until 29 April 2015) Chairman until 12 March 2015	11,712	22,500	34,212
Hans-Georg Härter Chairman from 12 March 2015	40,623	62,500	103,123
Werner Scherer Deputy Chairman	33,750	56,250	90,000
Sabine Beutert	22,500	20,000	42,500
Hans-Peter Finken (from 1 February 2015)	20,589	10,000	30,589
Dr Ing Hermann Garbers (from 29 April 2015)	15,226	10,000	25,226
Göran Gummeson	22,500	15,000	37,500
Michael Haupt (until 29 April 2015)	7,336	7,500	14,836
Leif Peter Karlsten (from 29 April 2015)	15,226	10,000	25,226
Herbert Kauffmann	22,500	45,000	67,500
Alois Ludwig (from 29 April 2015)	15,226	10,000	25,226
Dietmar Paust	22,500	12,500	35,000
Eva Persson (until 29 April 2015)	7,336	2,500	9,836
Dr Witich Roßmann	22,500	12,500	35,000
Dr Herbert Vossel	22,500	12,500	35,000
Egbert Zieher (until 31 January 2015)	1,911	–	1,911
Total	**303,935**	**308,750**	**612,685**

RISK REPORT

RISK MANAGEMENT SYSTEM

To ensure their long-term survival, companies must act quickly – and react even faster – in a world in which economic conditions and the individual markets are constantly in a state of rapid change. Against the background of increasingly complex corporate structures and growing internationalisation, systematic risk management therefore forms an important basis for long-term business success.

DEUTZ operates in a variety of industries and regions worldwide and manages its business through various organisational units: the operating segments of the Group's parent company, subsidiaries, sales offices and authorised dealers. This organisational structure presents the Company with a large number of opportunities, but also gives rise to business-specific risks.

Our objective is to generate profits on a sustained basis and to increase these profits significantly over the medium and long term in order to develop the Company and secure its future. It is therefore critically important to identify and assess business risks at an early stage and take corrective action where required. DEUTZ has an appropriate risk management system to ensure it can meet this requirement.

Such a system heightens employees' sense of responsibility and raises their awareness of potential or existing risks. It also helps everyone involved to identify, analyse and communicate risks in good time and to initiate effective corrective action.

The basic principles, monitoring standards, personnel responsibilities, functions and procedures in the risk management system have been defined by the Board of Management of DEUTZ AG and summarised in a manual that is continually updated. A systematic reporting structure provides the basis for the work of the Risk Management Committee and ensures that all major risks are documented and communicated, and that appropriate corrective action is taken and documented at an early stage.

The DEUTZ Group conducts risk inventories four times a year. These risk inventories are carried out in all functions and areas of the Company and in the main affiliated companies to identify whether new risks have arisen compared with the Company's short-term and medium-term planning. The risks are categorised by importance, based on estimated probability of occurrence and potential impact. At the same time, a review is carried out to establish whether and how action that has been agreed and implemented has successfully minimised the known risks or whether there is still a need for further action. The Risk Management Committee then analyses the risks and the progress of the action that is being taken and reports to the Board of Management on the results of the risk inventory. To enable the Company to respond promptly at all times to any possible risks that may arise, risk officers and their employees are under an obligation to submit immediate reports on any new material risks or if there is an increase in the threat from known risks. These reports are to be separate from the regular reporting requirements.

Each year, the Group internal audit department and the independent auditors carry out an audit of DEUTZ AG's system for the early identification of risks pursuant to section 91 (2) AktG to assess whether the system is functioning efficiently. As in prior years, suggestions for improvements proposed by the internal audit department, Risk Management Committee or the auditors were promptly implemented by DEUTZ.

RISK MANAGEMENT IN RELATION TO FINANCIAL INSTRUMENTS

Basic principles Owing to its global business operations, the DEUTZ Group is exposed to various financial risks that can arise from adverse movements and trends in the international sales, procurement, interest-rate and foreign-exchange markets. The overarching risk management strategy used is designed to mitigate potentially negative effects on the DEUTZ Group's financial position.

The management and early identification of financial risks is based on annual financial planning, together with updates and regular analyses of variances during the course of the year. Financial management in the Group is the responsibility of DEUTZ AG as the parent company.

The treasury department identifies, measures and hedges financial risk in close collaboration with the Group's operating segments. The Board of Management specifies principles for the Group's overarching risk management strategy as well as guidelines for certain aspects, such as how to manage currency risk, interest-rate risk and credit risk and how to hedge them using derivative and non-derivative financial instruments.

The Finance Committee, which meets roughly every three months, provides a forum at which operational issues relating to risk management and other financially relevant decisions are discussed. The Finance Committee consists of the relevant member of the Board of Management plus representatives of the treasury and finance departments.

The objective of risk management is to mitigate fluctuations in profits and cash flows caused by volatility in commodity, interest-rate and foreign-exchange markets. Derivative financial instruments are used only for hedging purposes, i.e. only in connection with corresponding underlying transactions arising from the Group's ordinary business activities or financial transactions that have a countervailing risk profile to that of the hedging transaction. The nature and scope of the hedged items are specified in a binding financing directive.

DEUTZ works exclusively with leading banks in order to minimise counterparty risk.

The treasury department manages the lines of credit in accordance with the Group's financing principles. Subsidiaries are funded primarily by DEUTZ Group loans.

We manage the financial risk as follows:

Risk from bad debts We protect ourselves against the risk of bad debts by constantly monitoring our situation, including through electronic means, and by regularly analysing receivables and their breakdown. The Company takes out credit insurance to cover a large proportion of its receivables unless payment is made in advance or by letter of credit.

Currency risk arising from operating activities Currency risk, primarily in US dollars, which arises as a result of transactions with third parties denominated in foreign currency, is monitored by means of a central currency management system and mitigated by the use of derivative financial instruments. The DEUTZ Group's net currency exposure is normally hedged by forwards equivalent to 50 to 80 per cent of open items, or 100 per cent in the case of selected project-based firm commitments. DEUTZ is also taking specific action to increase the volume of purchasing in US dollars; this enables the Company to counteract exchange-rate risks from sales invoiced in US dollars by way of natural hedging.

Interest-rate risk arising from funding arrangements The DEUTZ Group is exposed to risk from interest rate changes, above all in relation to floating-rate loans and other loans that it has taken up. We hedged the interest-rate risk arising from the funding arranged in mid-2012 with the European Investment Bank. This means that, as far as some of our financial arrangements are concerned, we will not be affected by any rises in short-term interest rates in the future.

Liquidity risk The funding agreements concluded provide the Company with adequate liquidity for its further development. During the term of the agreement, DEUTZ AG must ensure that the DEUTZ Group complies with certain financial covenants (ratio of financial debt to equity and ratio of financial debt to EBITDA). The financial covenants have a comfortable buffer in line with our medium-term balance sheet and profit planning. Only if there is a dramatic deterioration in the general economic situation is there a risk of the covenants being breached.

Further information on financial risk management can be found in Note 25 on page 103.

RISK ASSESSMENT

The assessment of risks in the DEUTZ Group is based on the estimated probability of occurrence in conjunction with the potential impact of the risk on the business objectives. In the following risk report for the DEUTZ Group, the risks are categorised as either 'low', 'moderate' or 'high'. Risks that have been classified as 'low' would be expected to have a low impact of up to €10 million on financial position and financial performance. Risks classified as 'moderate', however, would have a significant impact (between €10 million and €50 million) and risks classified as 'high' would have a major impact of over €50 million on financial position and financial performance. Risks to the Company's survival as a going concern are described as such.

DEUTZ Group: Risk assessment

Probability of occurrence (%)	Impact: minor	moderate	significant	critical	very critical
80–99	low	moderate	moderate	high	high
60–79	low	moderate	moderate	high	high
40–59	low	moderate	moderate	moderate	high
20–39	low	low	moderate	moderate	moderate
1–19	low	low	low	moderate	moderate

RISK

As with the internal risk report, the following presentation of the current risk situation is focused on the risk factors that are important for the DEUTZ Group. Consequently, risks that are referred to were categorised at least as 'low' before measures to counter the risk were taken into account. In contrast to the internal risk management, the risks in the following description are more strongly aggregated and are listed by risk category. Unless otherwise stated, the risks refer to 2016 and relate to both the DCE and DCS segments.

EXTERNAL RISK

Market risk We operate in sales markets that are characterised by particular sensitivity to cyclical influences. This can have a negative impact on the financial position and financial performance of the DEUTZ Group. As well as having a direct effect on unit sales and revenue, this may also impact negatively on the value of the assets on our balance sheet. We operate in very cyclical markets in our main application segment, Mobile Machinery, and in our principal sales regions of Germany, western Europe and North America. Our objective is to continue to reduce this cyclicality from a regional and application segment perspective. One of the ways in which we are doing so is by continuing to focus further efforts on expanding our Agricultural Machinery application segment, as it follows a different economic cycle to the other application segments.

In the medium and long term, we seek to mitigate regional and application-related sales risks by aligning our development activities with our product strategy and by entering into alliances. Close alliances with key customers such as AB Volvo and AGCO are of considerable importance in enabling us to achieve these sales targets.

We are very well diversified and well positioned for the future in terms of the geographical and sectoral distribution of our customers. We supply the market-leading manufacturers in the various application segments. Despite the countermeasures that are in place, we cannot completely control the external risks. We therefore continue to categorise the market risk as 'moderate' because the economic situation in our sales markets remains volatile.

STRATEGIC RISK

Our business strategy is focused on expanding our customer and product base and on further globalisation and internationalisation. This strategy presents the DEUTZ Group with numerous opportunities but is, of course, also associated with risks.

We attempt to mitigate these risks by precisely analysing trends in our markets and by taking into account external market research. We also enter into close alliances with our major customers in the target markets. Finally, we closely monitor our strategic projects so that we are able to respond immediately to changes.

In view of the measures in place, we categorise the strategic risks with regard to the attainment of our financial targets in the coming year as 'moderate'.

OPERATIONAL RISK

Quality risk The DEUTZ Group is exposed to liability and warranty risks. Potential warranty claims and claims for compensation could have a negative impact on our financial position and financial performance.

We have set up local quality departments to ensure quality in all plants and relevant areas of the Group. These departments systematically analyse sources of errors and defects, optimise production processes, take action to minimise the risk in production start-ups and reduce warranty risks. A central quality management organisation ensures that standardised processes and methods are in place and carries out regular audits. In addition, DEUTZ has defined uniform standards for the selection of suppliers and, in close cooperation with the suppliers, continuously improves the quality of supplied parts. Regular certification audits and additional quality initiatives enable us to handle the significant technical complexity of engines and to satisfy the steadily increasing quality requirements of our customers.

Sufficient provisions are recognised on the balance sheet to account for warranty risks. In view of the precautionary measures that have been taken, we categorise any further quality risks that could negatively impact on our financial targets as 'low'.

Production risk Fluctuations in capacity utilisation in production that result from our level of dependency on the general economic situation can, like breakdown-related production delays, have a negative impact on profitability.

In order to avoid mistakes in planning and capital expenditure, the necessary production capacity is regularly reviewed and planned using different timescales: over a number of years as part of the medium-term planning process, which is revised each year, and for the following financial year as part of the budget planning process, which is then updated quarterly for the current year. Production programme meetings and capacity planning meetings are held monthly to ensure that our capacity is adjusted in line with sales. We are using temporary employment contracts more and more as a way of flexibly adjusting capacity to the level of orders on hand.

In view of the measures in place to avoid or minimise these risks, we categorise the level of production risk with regard to our financial targets as 'low'.

OTHER RISKS

Data security We are a technology-driven company that is heavily focused on research and development. Being an innovation leader gives us a competitive advantage that forms the basis of our long-term success. The risk associated with this is that strictly confidential information, particularly concerning new technologies or partnerships in research and development, could find its way to our competitors through illegitimate means. This could have a negative impact on our market position.

We have put a series of measures in place to protect confidential information. As well as IT security training, these include security measures for computer hardware and IT security guidelines that have been laid down by management. In view of the precautions that have been taken, we categorise the data security risk as ‘low’.

Legal risks As a Group with multinational operations, DEUTZ is subject to a variety of regulations under tax, competition and patent law as well as to other legal and statutory requirements. Existing and potential legal disputes are recorded and analysed on an ongoing basis at DEUTZ; they are assessed in terms of their legal and financial impact and an appropriate amount is recognised in the risk provisions in the accounts. The outcome of legal disputes is uncertain, however. This means that there are further risks, not accounted for through provisions on the balance sheet, that could negatively impact on our financial targets.

Groupwide standards such as the general terms and conditions of business, sample contracts for various uses and implementation provisions in the form of organisational guidelines are refined on an ongoing basis and reduce the level of new legal risks at DEUTZ. The legal affairs department and external lawyers are also regularly consulted about projects and the finalisation of contracts that fall outside the scope of the standards developed for day-to-day business. In view of the measures that have been taken either to avoid or minimise risk, we categorise the legal risk as ‘moderate’.

OVERALL ASSESSMENT OF THE RISK SITUATION

Material risks have been identified and evaluated using our risk management system. Appropriate action is taken to manage these risks and, as far as possible, bring them under control. Changes in material risks are monitored regularly at Group level. Currently, the DEUTZ Group has not identified any risks that either individually or in their totality could jeopardise the continued existence of the enterprise as a going concern. Individual risk factors have changed only slightly from the previous year, meaning the overall risk situation is largely the same. Because of the precautions that have been taken and our position in the market, we are confident in our ability to successfully manage the existing risks and overcome the resulting challenges – despite conditions remaining difficult.

ACCOUNTING-RELATED INTERNAL CONTROL SYSTEM

The internal control system is an integral part of the risk management system. Whereas risk management focuses on the identification, analysis, assessment, communication and management of strategic risk, the internal control system (ICS) brings together activities aimed at avoiding or limiting risk at operational level through use of control instruments.

The Board of Management is responsible for setting up, monitoring, refining and ensuring the effectiveness of the ICS. Even a properly structured ICS is unable to provide absolute security; it can only provide a relative amount of security in helping to achieve targets and/or avoid material misstatements.

The aim of the internal accounting-related control system is to ensure that accounting is carried out consistently and in accordance with statutory requirements, generally accepted accounting principles and internal guidelines. The accounting process itself includes those operating processes that provide the value flows for financial reporting, the process for preparing the consolidated financial statements, and all information sources and processes from which the significant disclosures in the consolidated financial statements are derived.

In order to ensure that the consolidated financial statements are properly and consistently prepared, the Group adheres to the fundamental principles of separation of functions, having work checked by a second member of staff and IT access restrictions to prevent unauthorised access to relevant data. There are written procedural instructions and, in particular, Group accounting guidelines that are regularly updated at head office and communicated throughout the Group. Each reporting entity is responsible for compliance with the guidelines, and the data reported to DEUTZ’s Group accounting department is validated on an ongoing basis during the preparation of monthly financial statements. Data is reported to the Group head office using a standard reporting tool that has been implemented throughout the Group. Additional control mechanisms covering the risks in the main processes, thereby guaranteeing a reliable accounting and reporting system, are normally set up locally at departmental level. Where necessary, we also use external service providers, such as independent assessors of pension liabilities. The Group accounting department ensures that these requirements are adhered to across the Group.

Information relevant to accounting is shared on an ongoing basis with the Head of Finance, Accounting and Compliance and passed on to the Chief Financial Officer in regular meetings.

Besides discussing the single-entity and consolidated financial statements, the Audit Committee set up by the Supervisory Board regularly discusses the quarterly financial reporting. In addition, the Audit Committee's monitoring function includes the ICS set up by the Board of Management as well as the accounting process itself.

The internal audit department prepares a risk-based audit plan and verifies whether the statutory regulations and the DEUTZ Group's internal guidelines for its entire control and risk management system are being complied with. As part of its monitoring function it reviews whether the defined controls are functioning effectively. The findings of these reviews are reported directly to the Board of Management and allow us to eliminate any deficiencies that have been identified and ensure that the ICS is continually refined.

OPPORTUNITIES REPORT

In the fast-paced, dynamic markets in which the DEUTZ Group operates, there are, in addition to the aforementioned risk factors that can negatively impact on the attainment of the business objectives, also opportunities that can have a positive effect on the business objectives of the Group for 2016. Identifying and harnessing these opportunities is the responsibility of the individual operating segments of the Group. Unlike risks, opportunities are not collated and assessed centrally.

Unless otherwise stated, the opportunities described below refer to 2016 and relate to the DCE and DCS segments.

Economic situation in relevant markets Developments in the global economy have a major effect on the financial position and financial performance of the DEUTZ Group. If our expectations regarding the macroeconomic situation in our most important markets of Europe, the USA and Asia are exceeded, this can lead to us performing better than we predicted.

Research and development Increasingly stringent emissions standards and general technological progress are placing huge demands on our entire industry. We are one of the innovation leaders and have a very strong competitive position thanks to our proven expertise, our many years of experience and our efficient processes in the research and development of diesel engines and other drive systems. The stricter emissions standards for construction equipment and agricultural machinery that were introduced in China with effect from 1 October 2015 present us with the opportunity to capitalise on this competitive edge and increase our share of the Chinese market in the short to medium term.

Production and quality The digital transformation of manufacturing, referred to as Industry 4.0, is exploring new approaches to production. In combination with projects to improve quality, this may lead to substantial efficiency increases and greater customer satisfaction in the short to medium term.

OUTLOOK

GLOBAL ECONOMIC FORECASTS LOWERED

The International Monetary Fund (IMF)[1] has lowered its forecast for global economic growth once again. Nonetheless, at 3.4 per cent for 2016 and 3.6 per cent for 2017, this forecast is still higher than the 2015 figure of 3.1 per cent.

In particular, the predictions for developing countries and emerging markets have been revised slightly downward. For the industrialised nations, the IMF anticipates an overall growth rate of 2.1 per cent in 2016 and 2017 (2015: 1.9 per cent). The eurozone economy is expected to expand again, by 1.7 per cent both this year and next year, following 1.5 per cent in 2015. The growth forecasts for Germany are the same. In Spain, the buoyancy seen recently will taper off slightly. The US economy is expected to grow at a rate of 2.6 per cent in both 2016 and 2017, compared with 2.5 per cent in 2015. In China, the pace of growth will probably slow again, falling from 6.9 per cent in 2015 to 6.3 per cent this year and 6.2 per cent next year.

The business climate index[2] published by the ifo Institute of Economic Research dropped slightly in January 2016. This index, which covers trade and industry in Germany, stood at 107.3 points most recently, compared with 108.6 points (seasonally adjusted) in December 2015. Expectations have particularly deteriorated. The ISM purchasing managers' index[3] in the USA stood at 48.2 points on 1 February 2016. This indicates that economic activity is currently contracting.

DIESEL ENGINES MARKET

For construction equipment in 2016, we anticipate that the market in both Europe and North America will move within a narrow range of –5 per cent to +5 per cent and that the Chinese market will see a further decline of around 10 per cent to 20 per cent. For agricultural machinery, we predict that the market in Europe will either remain at its current level or contract by up to 5 per cent. We also expect the medium and heavy-duty truck sector in China to remain within a narrow range of –5 per cent to +5 per cent.

[1] IMF World Economic Outlook Update, January 2016.
[2] ifo Institute of Economic Research, January 2016.
[3] ISM Institute for Supply Management, February 2016.

As a rule, the diesel engines market largely follows the applications and markets of the machinery and equipment in which the engines are installed.

NEW ORDERS, UNIT SALES, REVENUE

In view of the subdued market outlook and persistent reluctance to invest, we expect our engine sales to remain static. European customers still have engines in their inventories that they had bought in 2014 ahead of the introduction of new emissions standards. The resulting adverse impact on engine sales will be less pronounced than in 2015, however. This, coupled with production ramp-up for new customer projects, should compensate for any weaknesses in end customers' markets, particularly in the agricultural sector. We believe the service business's revenue will continue to go up.

Owing to the increasing proportion of higher-value engines to meet the new emissions standards in Europe and America, the value of the diesel engines market will continue to increase at a faster rate than its unit sales.

Overall, we assume that revenue will stagnate or, at best, rise slightly. We expect revenue in both the DCE and DCS segments to follow a similar pattern. Given the current environment, our forecasts are of course subject to great uncertainty. The flexibility of our business therefore remains a key factor in our competitiveness. Although we have significantly improved our flexibility over the last few years, we will continue to work hard on increasing it still further.

EARNINGS

The focus this year – in addition to the successful implementation of new customer projects, the site optimisation process and a quality offensive – is primarily on measures designed to further reduce costs and increase efficiency.

We expect the EBIT margin to increase moderately. As capacity utilisation is likely to change only insignificantly, this will be predominantly achieved with further cost-saving measures and the first positive effects from the optimisation of our site network. We are likely to benefit from the current movements in the US dollar exchange rate. We expect both our DCE segment and our DCS segment to achieve earnings growth.

As a result of the anticipated slight increase in earnings, we believe there will be a small year-on-year rise in return on capital employed (ROCE) in 2016.

COMMODITIES, COLLECTIVE PAY AGREEMENTS

Commodity prices We expect price levels in the primary markets to weaken again in 2016, driven by a slowing global economy and low demand in Asia.

Collective pay bargaining in the spring The current collective pay agreement for the metalworking and electrical engineering industries in Germany expires on 31 March 2016. We believe the negotiating parties will start the negotiation process soon after and reach an agreement in the second quarter on the basis of current economic data.

RESEARCH AND DEVELOPMENT EXPENDITURE

We predict expenditure on research and development of just over €50 million, thus slightly higher than the very low level of spending in 2015. The R&D ratio is therefore likely to increase marginally year on year.

CAPITAL EXPENDITURE

We forecast that our capital expenditure in 2016 (excluding capitalisation of research and development expenditure) will be around €55 million. This includes capital expenditure on site optimisation. Including capitalisation of research and development spending, we anticipate that capital expenditure will total approximately €75 million.

JOINT VENTURES ACCOUNTED FOR USING THE EQUITY METHOD

The market environment in China is likely to remain challenging and volatile in 2016. We are expecting the revenue of our DEUTZ (Dalian) Engine Co., Ltd. joint venture to remain flat but its earnings to improve slightly on the back of cost savings. Its performance will depend heavily on its capacity utilisation and thus on market conditions.

WORKING CAPITAL RATIO, FREE CASH FLOW AND EQUITY RATIO

Our prediction for the working capital ratio is around 17 per cent as the quarter-end average. Given that capital expenditure will remain well below the level of depreciation and amortisation, we forecast positive free cash flow in the low to mid-double-digit million euro range in 2016.

We intend to maintain our equity ratio above 40 per cent, a level that it currently comfortably exceeds. The good level of equity reduces our dependency on capital markets in a volatile market environment.

EMPLOYEES

Flexible headcount adjustment Our aim is to end all short-time working as soon as possible and to return to full employment, although this will depend heavily on the level of orders on hand. If we require additional workers, we will again significantly increase the proportion of flexible contracts, whether fixed-term or temporary. As we operate in a cyclical industry, this is the best way that we can protect ourselves against fluctuations in demand.

Collective agreement on pre-retirement part-time employment We continue to offer older employees the opportunity to retire early by switching to pre-retirement part-time employment. Our expectation is that a significant number of our employees will take up this option in 2016.

STATUTORY REGULATIONS, EXHAUST EMISSIONS STANDARDS

The most stringent exhaust emissions standards yet for diesel engines have now been introduced in all power output categories in the European Union, in the form of 97/68 Stage IV, and in the USA, with EPA Tier 4. Stage V is scheduled to come into effect in the European Union in 2019[1]. Our TCD engines equipped with a diesel particulate filter in the 2.9 to 7.8 litre cubic capacity range already meet this new standard. No further tightening of exhaust emissions limits in the USA is on the horizon at the time of writing.

OUTLOOK FOR THE YEARS AHEAD

We forecast that global demand for capital equipment will recover in 2017. Moreover, we anticipate that, by then, European customers will have largely exhausted their inventories of engines bought ahead of the new emissions standards taking effect. From a current perspective, we therefore expect a marked improvement in the business situation in 2017, in terms of both revenue and the EBIT margin.

Global megatrends, such as increases in the world's population, advancing industrialisation in the agricultural sector and urbanisation, along with accompanying investment in infrastructure, are driving the further structural expansion of the global engine market. This will open up good opportunities for the continued advancement of the DEUTZ Group in the years to come. We plan to seize these opportunities in order to generate profitable growth.

Disclaimer This management report includes certain statements about future events and developments, together with disclosures and estimates provided by the Company. Such forward-looking statements include known and unknown risks, uncertainties and other factors that may mean that the actual performances, developments and results in the Company or those in sectors important to the Company are significantly different (especially from a negative point of view) from those expressly or implicitly assumed in these statements. The Board of Management cannot therefore make any guarantees with regard to the forward-looking statements made in this management report.

[1] The EU Commission's Stage V proposals as published on 25 September 2014.