

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.