

Tognum AG

Report* of the Executive Board to the Annual General Meeting

Volker Heuer

Chairman of the Executive Board and CEO of Tognum AG

Only the spoken German word shall be valid.*

* This version of the report is a translation of the German original manuscript and has been prepared for the convenience of English-speaking readers only. This means that it is neither in general nor legally binding and that for the purposes of interpretation only the spoken German word shall be valid.

UNDER EMBARGO UNTIL 9 June 2009, with the beginning of the report of the Executive Board

My dear Shareholders,
my dear Shareholder Representatives,
dear Friends of our Company,
dear Members of the Supervisory Board,
dear Colleagues all,

Welcome to the second Annual General Meeting of Tognum AG following our IPO in 2007, here in the Friedrichshafen Exhibition Centre. We are delighted that so many shareholders have been able to join us here on the shore of Lake Constance once again to see for themselves how their company is performing.

Since the last Annual General Meeting, as you are aware, a lot has happened. A particularly important event for us this year is that our largest subsidiary, MTU Friedrichshafen, is celebrating its 100th anniversary. Well-wishers include German Chancellor Dr. Angela Merkel, who visited us here in Friedrichshafen at the beginning of May. Before an audience of international customers and distributors at the celebration event that was held here, she stressed the importance of companies with a long tradition, like MTU, for Germany as a business centre and for the “Made in Germany” mark of quality. At the same time, she praised MTU for being what she called a “prestigious piece of German engineering art” and a “prime example of leading edge technology”.

Today, I would to pass on this praise, dear Shareholders, to you. Because you are the ones who, by investing your capital, have created the prerequisites that will enable us in future, with great passion, to continue to develop the best solutions in the field of propulsion and energy.

A company that can look back on a history that is equally as long and as successful as MTU's is our subsidiary L'Orange: the specialist in fuel injection systems for medium and high speed diesel engines turned 75 last year.

A second change that you certainly noticed as you came through the entrance foyer has strategic importance for our future.

Our MTU brand of long standing now has a new sister brand. Since autumn 2008, we have bundled our activities in the field of decentralised energy generation under the umbrella brand of MTU Onsite Energy – and that means everything, whether the systems are based on diesel and gas engines or fuel cells. The introduction of the brand was preceded by a restructuring of the organisation that has made our company even more clearly defined and transparent. To increase transparency in our accounting system, we have made adjustments to our reporting system as the final step from 2009 onwards. This will make the separation of the key figures for our operating subsegments “Engines” and “Onsite Energy & Components” even clearer.

We will of course continue to market our large high speed diesel engines and propulsion systems for numerous off-highway applications under the well-known and traditional name of MTU. The only on-highway components in our portfolio are propeller shafts from Rotorion, a field in which we agreed with the IFA Group at the end of February this year that we would examine the possibilities of a collaboration of the two propeller shaft units of our two companies. We expect the examination to be completed sometime in the second half of this year.

The road to this future-driven strategy and at the same time almost a third of the 100-year history of MTU has been travelled by a man who was always dedicated, and with a great passion, to developing the best solutions for our customers in the fields of propulsion and energy: my former colleague on the Executive Board, Dr. Gerd-Michael Wolters. I would like therefore, at the start of my report, to turn my attention to him in particular, because in this anniversary year he will be leaving us. He retired from the Executive Board at the end of April, but will be available to the company in an advisory capacity until the end of June – Mr. Eckrodt mentioned this briefly a short time ago.

For over three decades, Dr. Wolters has shaped the fortunes of the company like no other senior manager at MTU. As his last major project, he launched the new 1600 engine series a

month ago. His successor is Dr. Ulrich Dohle, to whom I would now like to extend a warm welcome. He has been on the Executive Board since 1 May and has taken over the responsibility for the “Technology and Operations” segment from Dr. Wolters.

May I at this point, dear Mike, express my personal, heartfelt thanks – and I’m saying this on behalf of all Tognum shareholders – for your commitment and your dedication, which were always exemplary, energetic and visionary, and wish you all the very, very best.

Review of 2008

Ladies and Gentlemen,

Let us now, after these words of introduction, take a look together at the financial year just ended. In 2008, Tognum continued to put in an excellent performance. This can ultimately be seen in our successful balance sheet, which we presented at the end of March.

As I spoke to you here a year ago, it was not possible to foresee with any accuracy at that time that the financial crisis would develop into a global economic crisis. Now we know: the bank failure in September 2008 triggered the worst economic crisis since the Second World War. Particularly in view of this situation, we are very pleased with the way business developed last year.

Order intake and revenues

Take order intake, where we reported an increase of four per cent to over 3.2 billion euros.

Or revenues of over 3.1 billion euros and thus almost 11 per cent more than in the previous year.

This means that order intake in 2008 was once again above the level of revenues.

Profit and margin

We take special pride in the fact that we achieved our profit and margin targets for 2008, despite the difficult economic environment. This is not something to be taken for granted, since we specified these targets at the end of 2007, in other words at a time when it was not possible to foresee that the US real estate crisis would trigger global recession.

We generated an adjusted EBIT, i.e. comparable earnings before interest and taxes, of 407 million euros. This represents growth of four per cent – and a new all time high for our company.

This means we also achieved our return on sales target for 2008: adjusted EBIT in relation to sales was 13 per cent.

Year-on-year net profit for the Group was also up by around 33 per cent to 264 million euros.

This enabled us to achieve our targeted adjusted earnings per share of over 2 euros – to be precise, 2.01 euros per share.

Balance sheet structure

Financially, we are also firmly established for the long term on a strong foundation. In the year just ended, we increased our equity once again, this time by 137 million euros. This

means that, at the end of 2008 our equity was 26 per cent, and at the end of the first quarter in 2009 had actually risen to more than 27 per cent. And end of period we had undrawn credit lines of over 300 million euros.

Net financial debt remains at a sound level: as at 31 December 2008, it amounted to 336 million euros and 283 million euros at the end of the first quarter of 2009.

Segment performance

The excellent performance at Group level is reflected in the two former reporting segments, both of which saw increases in order intake, revenues and adjusted EBIT.

This means that, for the former “MTU Engines” segment, revenues were up ten per cent to 2.66 billion euros.

The adjusted EBIT of the “MTU Engines” segment rose seven per cent to 401 million euros. This growth was attributable primarily to the revenues generated by the Marine, Power Generation, Defence, After Sales and Industrial subsegments.

In “Onsite Energy Systems & Components”, our second former reporting segment, we increased segment revenues by no less than 18 per cent to 621 million euros.

And at 34 million euros, the former “Onsite Energy Systems & Components” segment achieved an adjusted EBIT that was nine per cent higher than in the previous year.

We achieved organic growth in this segment primarily as a result of the increased revenues in diesel systems for use in energy systems.

But our business in components has also grown. Revenues in fuel injection systems from L’Orange, for example, were up ten per cent to 157 million euros.

The business volume in propeller shafts from Rotorion, despite the slump in the automotive market, was marginally above the level of the previous at 226 million euros.

Annual financial statements of Tognum AG

In addition to the consolidated figures for the Group, under the provisions of the German Commercial Code, the separate financial statement of a public limited company in particular is important for resolutions taken at the Annual General Meeting. Among other things, it is the determining factor for the appropriation of profits.

For this reason, I would now like to present Tognum AG’s key figures:

In the 2008 financial year, we achieved a net income around 228 million euros. Taking into account the profit of 87.5 million euros carried forward, this result in net profits of around 201.4 million euros.

The equity of Tognum AG thus amounts to around 709 million euros as at 31 December 2008.

Dividends

Dear Shareholders, you should also benefit from this excellent performance of course.

For this reason, under item 2 of the agenda, we are proposing an increase in the dividends in comparison with the previous year of approximately 17 per cent to 70 euro cents per share.

In view of the improved performance of the Group on an adjusted basis and our sound, long-term financing, we consider this increase appropriate, even in what is currently a difficult phase.

With a current total of 131,375,000 no-par value shares carrying dividend rights, the dividend payment – subject to the approval of today's Annual General Meeting – will thus amount to 91,962,500 euros. This dividend payment thus corresponds to around 40 per cent of the net income of Tognum AG and 35 per cent of the adjusted Group net income for 2008.

This means that we are acting in accordance with the dividend policy we announced at our IPO, which was to pay a dividend of between 30 and 50 per cent of the Group net income.

Share price

With this reliable dividend policy, it is our intention that all of you who to date as investors have had to accept a share price that was lower than you originally expected are able to share in the fundamentally positive performance of our company.

Because one thing is clear: neither you, dear shareholders, nor we can remain satisfied with the way our share has performed since going public.

On the one hand, our company's excellent results in the year just ended are not reflected adequately in the 2008 share price performance. On the other hand, we cannot be so presumptuous as to believe that we can somehow distance ourselves from the current exceptional economic circumstances. The stock markets in 2008 and at the start of this year saw extreme selling pressure. And right now, in the opinion of many stock market experts, we are still a long way from a steady, long-term upward trend on the stock exchanges.

As a basic principle, however: companies that have only one product for only one market in only one region are more prone to economic fluctuations than companies with numerous products for numerous markets in numerous regions. And this is true particularly in times of crisis. It is interesting to note, by the way, that the term "crisis" in Chinese is composed of two characters. One means "danger", while the other means "opportunity". With our diversified business portfolio, therefore, our view is that we have the opportunity to emerge from this crisis stronger than ever. And this, I hope, would be rewarded on the stock market in both the medium and long term.

Market situation

But what does the situation really look like on our markets? Previously, each of the many end markets in which we are involved have their own particular cycle. This has enabled us to offset the lean periods in one market with successes in another market. At the moment, the extremely difficult economic situation overall is affecting all our markets. However: the crisis is not hitting us with a full broadside, because our markets do not react in the same way. Our advantage – and this is not only true in the current economic crisis – is that we operate in more than 20 different application fields and we do that all over the world in regions that are relevant to the business in which we are involved.

On the one hand, our marine and defence business and the growing after sales business are very stable markets that report virtually no adverse reactions to the current situation. The gives us stability.

On the other hand, we are involved in markets that are normally affected by fluctuations in the economy to only a limited extent, but right now – in this new, and quite unique crisis – are reacting more strongly. Examples of this can be seen in the business we do in diesel-based, decentralised energy systems, commercial vessels and mining. The last two areas are currently suffering from the decline in freight shipments and the reduced demand for raw materials.

And ultimately, of course, we serve markets that have been severely hit by the current crisis, such as our business supplying propeller shafts to the automotive industry and the market in yacht engines for boats under 30 metres in length – a market that, at the moment at least, is very quiet.

Performance in the first quarter of 2009

As a result of the global recession – the extent of which, I believe, nobody had anticipated – and the changes in the development of the markets I have just described means that for business performance in 2009 we can't yet give the all-clear.

We are currently going through a phase that, after many years of continuous growth at Tognum, is moving, for the moment at least, in another direction.

Our figures for the quarter are meaningful to a limited degree only, since they do not adequately reflect our business as a whole, which is in many areas determined by our project business with in most cases long project completion times. But they do show how the ordering behaviour of our customers has changed. In 2008 – particularly in the energy systems market, due to the global restrictions on production – they were ordering large quantities for an entire year in advance. Today, many customers are only placing orders for the next six to eight weeks, because in the current situation nobody is afraid any more of not receiving the quantities ordered.

This can be seen very clearly in the order intake, which declined by around 26 per cent in the first three months of this year compared with the same period last year, while revenues were down by around 12 per cent to 642 million euros. The adjusted gross profit margin of over 25 per cent remained stable. However, cost of sales and development costs have risen as a result of implementing our strategy. All of this has resulted in a significant 36 per cent reduction in the adjusted quarterly earnings before interest and taxes to 64 million euros.

Outlook for 2009

Due to the current crisis, it is difficult to present a reliable outlook. In spite of this, we published a forecast at the end of March, which we subsequently confirmed in the middle of May.

We made this forecast after carefully considering to what degree negative influences were to be expected on our markets and market segments in the individual regions under known conditions and what form they would take.

From today's point of view, we must therefore assume there will be a decline in revenues of ten to twenty per cent by comparison with 2008. Nevertheless, we intend to keep our adjusted return on sales in the upper single-digit range. Accordingly, earnings per share will be below level of last year, which was extremely successful.

In our view today, despite the overall weak economic situation, we would also like to remain true to the dividend policy I mentioned earlier. We therefore plan to distribute an appropriate dividend for the current financial year, too.

And in terms of our performance, we stand by what we have said before: our medium-term goal is to continue to grow on average faster than the market and average a double-digit return on sales.

Short-term measures to stabilise our business

In order to achieve our annual targets, we have introduced short-term measures designed to stabilise our business that fit perfectly into our medium and long-term corporate strategy.

As a matter of principle, being a large Swabian company, we don't immediately begin to save our money when things get tight. For five years now, we have had a successful programme in place, known as "Tognum TOP", which is designed to increase efficiency and reduce costs, and which we have now extended to include all Group companies.

In response to the global recession, we developed an additional action package to stabilise our business at the end of last year, which we call our "Robust Action Plan". This plan not only allows us to create a framework for action based on clear directives. It also enables members of the entire workforce to respond independently in the spirit of our corporate philosophy as "In-house entrepreneurs". This means showing initiative and responsibility in the current difficult situation wherever they happen to be.

Allow me to look more closely at the four action areas: the market, cash and risk management, budget and investment planning, and employment.

In terms of our markets, we are adjusting our activities to bring them in line with the new situation. This takes place in addition to list price increases that were introduced at the beginning of the year. A key focus is on the launch of new products or new versions of existing products. Another important point for us is the expansion of our sales organisation in order to establish business relations with OEMs, distributors and end customers we have not worked with before. We are now looking at new markets that, due to their size, had previously not been given much attention. And to expand our systems business, we are setting up new local competence centres. A targeted, proactive approach when dealing with our customers is also very important to us. We are therefore providing our customers with more detailed information and advice than we have done before on how they can actually save money with our premium products, particularly in difficult economic times, as a result of the low operating costs over the entire life cycle. We also advise them on the possibility of obtaining state funding when they purchase our products. And we have also launched new marketing activities.

In the area of cash and risk management, we are putting in a lot of hard work to optimise our Net Working Capital and on the continuing improvement of our receivables management system. In addition, we continually monitor the stock levels of our customers and distributors, and the financial situation of key accounts and suppliers.

In terms of budget and investment planning, the increase in production capacity that was evident in 2008 is at the moment no longer a key focus. The new plant that was to have been erected in the United States, for example, has now been put on hold. And in-house, we are putting every effort into significantly reducing our overhead costs.

Regarding our workforce, we have now combined numerous individual actions to create a supplementary collective agreement we have called "Job Aktiv 2009", which was concluded with IG Metall at the Friedrichshafen location. Our common goal is to keep our core workforce and avoid introducing short time work as much as possible. To this end, commencing in June 2008, over 560 temporary workers and contract workers were made redundant worldwide.

Our employees in Friedrichshafen working under collective wage agreements are all pulling together with the management – by agreeing to take no pay for a total of over 51,000 hours of overtime, for example, and to waive a negotiated one-time payment in September 2009. In addition, our company's workforce have accepted a postponement of part of the agreed increase in pay rates. It has also been agreed that production and assembly workers, if necessary, will be able to debit their flexible working time account by an average of up to 300 hours. However, company executives and also members of the Executive Board, of course, have agreed to do without holidays and parts of their variable reimbursement. I would like, here and now, to express my most sincere thanks to the entire workforce for this support.

What is important is that the “Robust Action Plan” includes very specific personnel and budget cuts but not standard reductions on the “one size fits all” principle. And, what is important for the continuing success of our company in the future: under no circumstances do we want to delay key projects. Quite the opposite in fact: we have once again significantly increased the budget planned for new developments in 2009 compared with last year, as you have already seen in the figures for the first quarter. Expenditure for research and development, for example, increased by 25 per cent in first three months of 2009 to 30 million euros. Our aim for the year as a whole is to increase our R&D activities by over 20 per cent compared with 2008.

Corporate strategy

As you can see, we have prepared the ground and are now ready to continue to pursue our corporate strategy at full power.

To date, we have focused on four strategic initiatives to support our long-term profitable growth. I would like to present to you briefly now and then move on to a strategic priority we added recently.

Firstly, in after sales, which is still a very high margin business area, we expanded our spare parts business at the beginning of 2008 with a new logistics centre in Überlingen (Lake Constance area). We are also enhancing this business with the acquisition of new major service contracts, such as a contract we signed recently with the Malaysian Navy for an order worth 111 million euros. Regional locations in Germany and Asia for “remanufacturing”, in other words the reconditioning of engines as part of an overhaul schedule, round off our after sales strategy. In our after sales business, we expect medium-term growth on average of around ten per cent per annum.

Secondly, we expanded our product portfolio last year with the addition of many new products and technologies.

In addition to the key technologies of fuel injection, electronics and charging, we are constantly working on the continuing development of exhaust after-treatment as a key technology. Besides numerous field trials in mobile applications, we are now performing continuous tests of the exhaust after-treatment system in Series 1600 and 4000 genset engines. In order to secure the expertise in exhaust after-treatment system for the company over the long term, we also set up “Envirovent” in October 2008 as a joint venture with the Swiss-based Hug company. Our goal is to meet the future emission regulations with the best possible benefits for our customers, by providing the best combustion process, the most efficient exhaust after-treatment system, the lowest fuel consumption or the smallest possible installation space.

And – as I mentioned at the beginning of my report – in May of this year, we launched our new Series 1600 engines to extend the lower power range. We were only able to cover this power range to a limited extent and solely with engines from third-party manufacturers, such as Mercedes-Benz. The first engines will go into series production as from October in Überlingen. With the introduction of the Series 1600, we will not only be replacing discontinued series from third-party manufacturers, but will primarily be developing completely new applications, particularly in the field of decentralised energy systems. The new series not only represents a technological innovation. In the long term, it represents for us even higher production quantities. We are assuming that the new series will bring about a change in our company in the course of the next ten years much as the development and launch of the Series 2000 and 4000 did in the nineties.

Ladies and Gentlemen, with the introduction of the Series 1600, we will develop into a provider of off-highway engines in the power range from 250 to circa 10,000 kilowatts and will supplement our onsite energy product portfolio with engines of our own in the lower power range.

And that brings us to our third strategic initiative, the expansion of our energy business with own systems. With the acquisition of US-based Katolight in 2007, we prepared our entry into the end customer business for energy systems. This summer, we will gradually introduce the first MTU onsite energy standard gensets into the end markets. As a premium provider of diesel engines for decentralised energy systems, we are thus expanding our portfolio with the addition of complete systems designed specifically for the end customer.

Overall, we still see great potential here for future growth. As a result, in onsite energy business, we anticipate annual revenue increases in the long term of up to 15 per cent.

In our Asian strategy focusing on China, our previous fourth initiative, our joint venture with the Chinese Norinco Group represents a key milestone. The first fruits of this partnership are the major orders for emergency power gensets for Chinese nuclear power plants with a total estimated value of 150 million euros, which we received last year as the lead manager.

As a result of this successful development in China, our fourth initiative is now known as “Regional Expansion”. We will ultimately, of course, not only be seeking greater involvement in China, but also in other Asian countries and other regions. A good example is India. But we also have our sights set on other markets, at the moment these are primarily Japan, Eastern Europe and both Central and South America.

Our intention is to further expand our regional balance. And not only in terms of markets where we can sell our propulsion systems and energy systems, but also in terms of production.

And now we have added a fifth initiative: The word “Propulsion” here stands for the expansion of our system business in the propulsion field, where our key focus is on intelligent, innovative solutions, such as hybrid technology. The new hybrid propulsion system for diesel-powered railcars, for example, was one of last year’s highlights.

For the future, we are absolutely convinced that low-emission and environment-friendly propulsion system solutions in a variety of applications in long term will be of key importance for our sustainable success.

Corporate vision

The successes we achieve in our strategic initiatives are important steps to implementing our vision:

To set standards and to become the preferred partner for the best solutions in the fields of energy and propulsion.

I presented this new vision to you last year, if you remember.

It is the result of many in-depth discussions inside the company and also with customers and business partners.

Its roots, however, go much deeper. Back in the days of Karl Maybach and his father Wilhelm, the founding fathers of the predecessor of MTU Friedrichshafen, what was feasible was not the benchmark. Karl Maybach, for example, always wanted to be better than the standard. With this ideal as his benchmark, he and his company rapidly became the “ideal partner” in propulsion matters.

For us this ideal has lost none of its validity. And that is why it appears again in the new corporate vision of MTU’s parent company, Tognum.

But what does our vision mean for our strategy?

- » It means we will continuously increase our technology and innovation leadership to make our customers even more successful.
- » It means we will expand our application and product portfolio wherever it will be profitable to do so in the long term and makes good sense.
- » And it also means that we will provide our customers with tailor-made system and service products, and tie our customers even closer to us.

Ladies and Gentlemen, if you want to build a ship, the French writer and aviator Antoine de Saint-Exupéry is once supposed to have said, then don't drum up people together to collect wood and don't assign them tasks and work, but rather teach them to long for the endless immensity of the sea.

With this in mind, we encourage our workforce of around 9,000 men and women to develop the products today that will set the standards of tomorrow – primarily in terms of cost-effectiveness, availability, reliability and environmental impact. And we encourage them to surprise our customers again and again and to fascinate them with the best solutions. And to do it all with the aim of continuing to successfully expand our market position.

The fact that we all experience this fascination and apply it successfully is evident in the results for the 2008 financial year, which we have presented to you in the course of today's Annual General Meeting, and in which we would like to share with an approximately 17 per cent increased dividend payment of 92 million euros. Even if we cannot avoid the current turbulence on the market – we will continue to work hard to remain successful in the future and will do everything we can to ensure that your company, my dear shareholders, continues to grow and make a profit.

Many thanks for your attention.

Disclaimer regarding forward-looking statements et al.:

This report also contains forward-looking statements based on assumptions and estimates of Tognum's Executive Board of Management. Although we assume that our assumptions and estimates on which we have based these forward-looking statements are realistic, we cannot guarantee that they will in the future prove to be correct. The assumptions and estimates, by their nature, may harbour risks and uncertainties that may cause the actual figures to differ considerably from the forward-looking statements. Factors that may cause such discrepancies include, among other things, changes in the economic and business environment, variations in exchange and interest rates, the introduction of competing products, lack of acceptance for new products or services and changes in corporate strategy. Tognum does not undertake any obligation to update, to review or to confirm the forward-looking statements or to release publicly any revisions to any forward-looking statements to reflect events or circumstances after the date of this announcement.