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## MAN GROUP MANAGEMENT REPORT

for fiscal year 2007

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# HIGHLIGHTS

## 2007: ANOTHER RECORD YEAR

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- Expansion continuing: order intake €19.4 billion (up 17 %), sales €15.5 billion (up 19 %)
- Operating profit again outpacing sales: up 57 % from €1.1 billion to €1.7 billion
- ROS: 11.2 % (up from 8.5), ROCE: 31.9 % (up from 28.0)
- Earnings per share €8.24 (up 63 %), EpS excl. nonrecurring result €7.99 (up 58 %)
- Dividend surging from €2.00 to €3.15

## VIGOROUS CAPACITY EXPANSIONS

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- Production start-up at commercial vehicle plants in Poland and India, for the first time over 100,000 vehicles sold inside a year
- Fine-tuned diesel engine production structures and capital expenditures allowing added engine production
- New turbo machinery plant in China
- Alongside expanded capacities also enhanced production flexibility

## PROSPECTS FOR 2008

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- Prospects for our capital goods remain bright; all business areas with brimming order books
- Global economic growth jeopardized mainly by financial market turmoils
- Commercial Vehicles production capacity to rise to 110,000 trucks in 2008
- Sales to mount by over 5 %
- ROS in line with the high 2007 level
- MAN celebrating its 250th anniversary in 2008

## THE MAN GROUP: BUSINESS AND STRATEGY

### The MAN Group

The Group's origins date back to 1758 when in Oberhausen, Rhineland, the St. Antony iron mill was founded. From this and two other metallurgical plants emerged later Gutehoffnungshütte (GHH). A second accretion was Sander'sche Maschinenfabrik, founded in Augsburg in 1840, which following the merger with Nuremberg-based Klett & Comp. in 1908, adopted the name Maschinenfabrik Augsburg-Nürnberg AG (M.A.N.). M.A.N. was taken over by GHH in 1920. In 1986, GHH and M.A.N. merged to form the MAN Group, which in 2008 is celebrating its 250th birthday.

Concentrating on transport, propulsion and energy, today's MAN is among Europe's foremost engineering groups. In their respective markets, the MAN companies all rank among the top three. With a workforce of around 55,000 in 120 countries, the Group operates in four core areas of business: Commercial Vehicles, Diesel Engines, Turbo Machinery, and Industrial Services. Heading the MAN Group is MAN AG, the Group's corporate headquarters and parent. In 2007, the MAN Group generated sales of €15.5 billion and an operating profit of €1,730 million.

#### The business areas: an overview

MAN Nutzfahrzeuge is among the foremost manufacturers of commercial vehicles in Europe, with production plants in four European countries and India. The product range reaches from trucks with a GVW between 7.5 and 60 t for both short- and long-haul service, trucks for military use and public purposes, regular service and tourist buses and coaches to combustion ignition (CI) and spark ignition (SI) engines for vehicles, ships, and power generation. MAN Finance provides financing arrangements for commercial vehicle customers, in particular leasing options. These activities are backed by an international marketing and service network. With sales of €10.4 billion and an operating profit of €1,039 million, MAN Nutzfahrzeuge is the MAN Group's biggest business area.

MAN Diesel is one of the world's leading developers and manufacturers of large-bore diesel engines, chiefly for marine applications but also for stationary use. The business area commands a strong market position both in the development of two-stroke diesels for the propulsion systems of large ships and in the manufacture of four-stroke diesel engines built into smaller vessels and as stationary engines for power plant energy production. Whereas the two-stroke engines are chiefly built by licensees, MAN Diesel itself manufactures most of the four-stroke variety at its locations in Germany, Denmark, and France. The area's sales added up to €2.2 billion; the operating profit reached €313 million.

MAN Turbo is a manufacturer of turbo compressors, industrial turbines, and chemical reactor systems. This business area markets a complete range of turbo machines for a variety of industries such as oil and gas, refinery, and chemical as well as for the production of industrial gases and electricity. The product range is supplemented by comprehensive after-sales service operations. This business area reported sales of €1.1 billion and an operating profit of €104 million.

MAN Ferrostaal is a global supplier of industrial services and systems while also acting as general contractor for project development, management, and financing arrangements. The lineup focuses on turnkey projects for industrial plant including the related financing and operator concepts, as well as on the marketing of capital goods. Another specialty is just-in-sequence assembly services for the automotive industry. Sales in 2007 reached €1.4 billion; the operating profit amounted to €179 million.

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## The MAN Group's strategy and strengths

The MAN Group's business goal is profitable growth and added value through competitive products and services. In sustainable pursuit of this goal we have set out a strategy matching the following requirements.

### **Focus on Transport-Related Engineering**

MAN's manufacturing areas focus on sectors relating to the growth markets of transport, propulsion, and energy. These areas are required to grow through investment and acquisition spending, thus expanding their foremost positions.

### **Industrial Governance leadership system**

The MAN Group's strategic leadership system—Industrial Governance—strengthens the entrepreneurial forces within the business areas through clear strategic focus. The strategic leadership of the Group is the responsibility of the Management Board of MAN AG on which all the core areas are represented. Each of the MAN business areas must be able to develop independently within the Group; each must measure itself against the strongest competitor in its market. Benchmarks have been set for the business areas and these must be achieved on average within any one economic cycle. Losses are not tolerated; neither is cross-subsidizing among the business areas. It is the task of Corporate Center to develop group strategy and structure, advance and deploy management staff, ensure target-oriented controlling, and provide central finance to the Group.

### **International expansion and growth**

MAN is a global group that is further expanding its international presence in terms of production and its marketing and after-sales service networks in order to more efficiently exploit existing market potentials and seize the opportunities offered by attractive growth markets, all through acquisitions, alliances, and capital expenditures for production, marketing and services.

### **Strengthening the business areas' competitiveness and profitability**

MAN concentrates on expanding markets with strong earning potential. Concurrently, one of our chief objectives is to rank among the most profitable suppliers in the respective markets. We measure our business areas against our strongest rivals and base our managerial de-

isions on the outcome of such comparisons. With the aid of ultramodern production facilities and marketing and logistics structures, on the one hand, and an after-sales service organization in close customer proximity, on the other, we will further enhance our profitability while devoting special attention to achieving financial indicators that are both strong and stable.

### **Steadily adding value**

Profitable growth in attractive markets is essential to upgrading MAN's value. This we measure with the aid of a control system based on operating profit, the return on sales (ROS) and the return on capital employed (ROCE). A key factor we see in the addition of such value is excellent cash conversion that allows us to transform high operating profits into high cash inflow and, through a judicious expenditure policy, into a high free cash flow.

### **Harnessing group synergies**

The synthesis of individual strengths and the product expertise of the individual business areas offers potential synergies that are exploited through close cooperation among the business areas and the selective support by MAN AG's corporate functions, thus furthering the Group's expansion potential. Highly significant is also the sharing of R&D results for achieving further emission reductions at Commercial Vehicles and Diesel Engines.

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## Acquisitions and divestments

In 2007, we rigorously pushed ahead with our strategic focus on Transport-Related Engineering.

### Acquisitions

With a view to bolstering MAN Nutzfahrzeuge's growth strategy, MAN Finance International GmbH (MFI) has extended its activities to include vehicle rental and leasing. The measures included the acquisition by MFI as part of a capital increase, of a 25.13-percent stake in EURO-Leasing GmbH, Sittensen, Germany. The deal was closed in early 2008.

### Divestments

A majority stake in MAN Ferrostaal's steel trading unit was transferred to CCC Steel GmbH & Co. KG, Hamburg, a move that will sustainably strengthen the competitive position of this business. The new limited partnership started operations on January 1, 2008, under the name of Coutinho & Ferrostaal GmbH & Co. KG. MAN Ferrostaal holds a 33.33-percent interest in the newcomer.

At the end of September, Siemag-Invest GmbH exercised its call option for the remaining 25.5-percent stake in SMS GmbH.

MAN Nutzfahrzeuge AG contributed to MAN Region West B.V., Vianen, Netherlands, its wholly-owned sales companies in France and Belgium. MAN and PON each hold a 50-percent stake in the company. PON, in turn, in-putted PON Equipment & Power Systems B.V., a Dutch sales company headquartered in Almere, Netherlands. The purpose of the deal is improved market penetration.

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## BUSINESS TREND AND RESULTS OF OPERATIONS 2007

### Economic environment

In all, global economic growth at around 5 percent was robust in 2007. However, in the latter half of the period, the uptrend flattened with the US subprime mortgage crisis, a sharp surge in commodity prices and the strong dollar inhibiting international business. In the USA, in particular, the economy subsided as the year advanced although our growth markets of Asia and C&E Europe did maintain their momentum.

Within the eurozone, business again prospered in 2007, albeit at a somewhat slower pace than in 2006. It was the solid demand for capital goods and a further decline in unemployment that propelled the economy. Spain and the UK appear to be moving in directions parallel to the US property and mortgage markets.

In Germany, business has slightly tapered, too, with growth nonetheless 2.5 percent (down from 2.9). Moreover, industry has tall order backlogs. Still, the appreciation of the euro, the financial market upsets and rising commodity prices have damped optimism although companies are still quite confident regarding economic trends especially given the barely abated expectations regarding capital goods. A sharp reduction in unemployment has partly offset the burdens imposed by the VAT hike, albeit private spending had little impact on the economy in 2007.

Worldwide demand in the transport, propulsion and energy sectors, of particular significance to MAN, was again voracious in 2007. In our most important market, Europe, unit sales of commercial vehicles leapt 6.8 percent from 397,000 to 424,000. In shipbuilding, the biggest market for our diesel engines, tonnages ordered worldwide in 2007 surged by 75 percent to 157 million gross tons. The rise in energy prices and the worldwide robust demand for energy again fueled business in turbo machinery.

## Order situation

MAN managed to once again vigorously boost its performance in 2007 with strong gains in both order intake and sales.

### Surge in new orders

Given the worldwide buoyant demand for capital goods, the MAN Group boosted order intake in 2007 once again double digit by 17 percent to €19.4 billion (up from €16.6 billion).

The burgeoning global economy is spurring worldwide demand for haulage services and concurrently for energy. These are factors reflected in order intake by our manufacturing areas, viz. Commercial Vehicles, Diesel Engines, and Turbo Machinery. Commercial Vehicles and Diesel Engines again clearly exceeded their record prior-year figures.

At €1.9 billion (down from €2.2 billion), the MAN Group in 2007 again reported a sizable volume of megaorders (contracts each worth at least €15 million). Given the steep surge in regular business (up 21 percent), such megacontracts have slipped in significance for the Group's order intake, particularly at the manufacturing

areas. At Industrial Services, in contrast, the very nature of megaproject business and the disposal of the steel trading unit have developed into steeper order intake ups and downs. At the end of 2007, this business area signed a contract worth €379 million for the construction of an ammonia production plant in Venezuela. Orders booked by Commercial Vehicles mounted 26 percent, by Diesel Engines by as much as 29 percent; Turbo Machinery order intake was just 3 percent shy of the high 2006 level. Essential if this area is to achieve further gains are the capacity expansions presently underway. Order intake at Industrial Services was down by 22 percent from 2006, a period which had reflected an €833 million megacontract from Trinidad.

### Order intake by business area

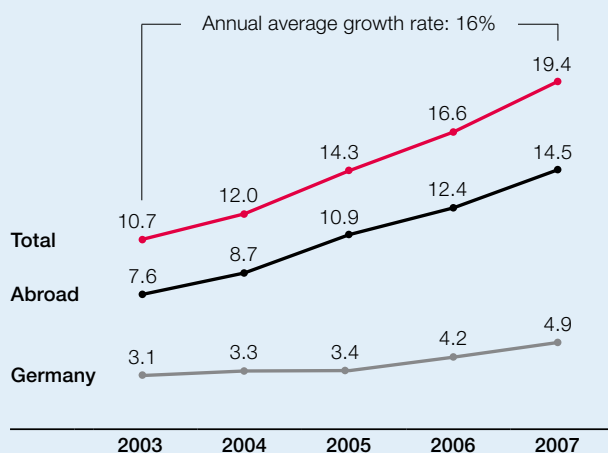
€ million	2007	%	2006	%
Commercial Vehicles	12,684	65	10,103	61
Diesel Engines	3,371	17	2,619	16
Turbo Machinery	1,454	8	1,498	9
Industrial Services	1,556	8	1,982	12
Others/Consolidation	309	2	365	2
<b>MAN Group</b>	<b>19,374</b>	<b>100</b>	<b>16,567</b>	<b>100</b>

### Order intake by region

€ million	2007	%	2006	%
Germany	4,929	25	4,151	25
Other EU	7,150	37	5,683	34
Other Europe	2,039	11	1,667	10
Asia	2,907	15	2,369	14
Americas	1,354	7	1,817	11
Africa	858	4	749	5
Australia and Oceania	137	1	131	1
<b>MAN Group</b>	<b>19,374</b>	<b>100</b>	<b>16,567</b>	<b>100</b>

**5-year order intake trend**

€ billion



Data like-for-like excluding discontinued operations

In 2007 we reported double-digit gains in orders booked both in and outside Germany. Domestic orders mounted 19 percent to €4.9 billion, international by 16 percent to €14.5 billion, these latter thus accounting for 75 percent of the total.

The sharpest rise of 26 percent to €7.2 billion was achieved with the other EU members; elsewhere in Europe order intake climbed 22 percent to €2.0 billion. The still burgeoning regions of Asia contributed orders worth €2.9 billion (up 23 percent) while the Americas lost 25 percent due to the above-mentioned Trinidad contract of 2006. The European markets accounted for the lion's share of new orders (73 percent), followed by Asia (15 percent).

**Sales once again robust**

MAN boosted sales in 2007 by 19 percent to €15.5 billion. Commercial Vehicles contributed €10.4 billion (up €1.7 billion or 20 percent), including €512 million from the sale of leased vehicles held by MAN Finance. Excluding this nonrecurring factor, Commercial Vehicles raised its sales by 14 and the MAN Group by 15 percent. Whereas Truck's sales jumped 25 percent to €9.0 billion (excluding the sale of the leased vehicles, by 18 percent), Buses' sales slipped 6 percent to €1.4 million. Diesel Engines likewise reported a double-digit sales increase, by 21 percent to €2.2 billion. Turbo Machinery's sales mounted 22 percent to €1.1 billion. The 5-percent rise to €1.4 billion at Industrial Services resulted from additional service business; project-related sales edged down from the prior-year level.

**Sales by business area**

€ million	2007	%	2006	%
Commercial Vehicles	10,410	67	8,685	67
excl. sale of leased vehicles	9,898	-	8,685	-
Diesel Engines	2,179	14	1,802	14
Turbo Machinery	1,108	7	908	7
Industrial Services	1,445	9	1,379	10
Others/Consolidation	366	3	275	2
<b>MAN Group</b>	<b>15,508</b>	<b>100</b>	<b>13,049</b>	<b>100</b>

**Sales by region**

€ million	2007	%	2006	%
Germany	4,343	28	3,394	26
Other EU	5,549	36	4,784	37
Other Europe	1,492	10	1,281	10
Asia	2,288	15	1,989	15
Americas	1,011	6	802	6
Africa	702	4	671	5
Australia and Oceania	123	1	128	1
<b>MAN Group</b>	<b>15,508</b>	<b>100</b>	<b>13,049</b>	<b>100</b>

The extra revenue from the sale of leased vehicles meant that domestic growth in 2007 outpaced foreign. The former rose by 28 percent to €4.3 billion and, excluding this one-off contribution, by 13 percent. Commercial Vehicles accounted for 80 percent of domestic sales and generated 33 percent of its sales in the German market. Domestic sales at Diesel Engines amounted to 12 percent, at Turbo Machinery and Industrial Services in each case 19 percent.

Sales outside of Germany in 2007 moved up 16 percent or €1.5 billion to €11.2 billion, thus continuing our international expansion. Non-German sales made up 72 percent of the total (down from 74 percent). Europe accounted for 74 percent of total sales (up 20 percent to €11.4 billion), Asia, where we pushed up sales by 15 percent to €2.3 billion, also contributed 15 percent to the total.

Over the past five years sales have surged, growing from 2003–2007 by an annual average of some 11 percent, by €5.1 billion from €10.4 billion to €15.5 billion.

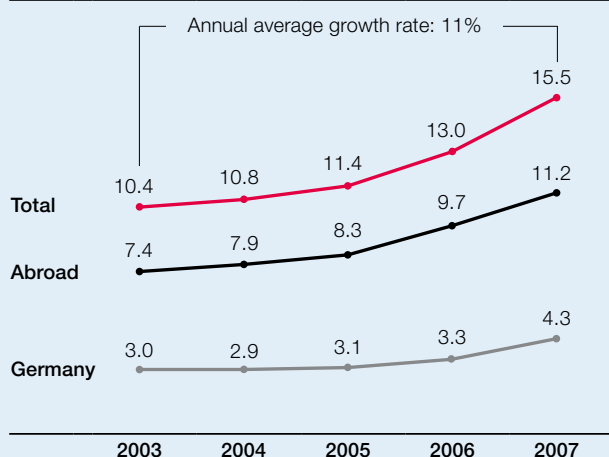
**Order backlog at all-time high**

During 2007 our production plants were once more working to capacity and hence sales were unable to keep up with the rush of incoming orders. Orders on hand were well above the previous prior-year record of €11.3 billion to reach €14.8 billion (up 31 percent). All the manufacturing areas reported sharp growth rates, with order backlog at Commercial Vehicles showing the steepest hike of 49 percent to €6.3 billion, followed by Diesel Engines (up 38 percent to €3.9 billion), and Turbo Machinery (up 23 percent to €1.7 billion). Orders on hand at Industrial Services mounted 3 percent to €2.4 billion. These bulging order books together form a solid launch pad for repeated growth in 2008. Concurrently, our customers have stepped up their insistence on quick, on-time delivery. The international expansion of our production and assembly facilities will enable us to address these rising demands.

Order backlog figures mirror the booming demand for our products and in fact, have almost trebled over the past five years from €5.5 billion to €14.8 billion, enough to keep us busy for 11+ months (book-to-bill ratio as of end-2007).

5-year net sales trend

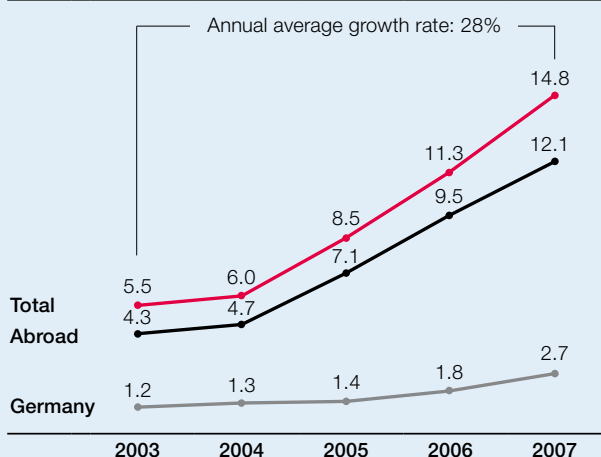
€ billion



Data like-for-like excluding discontinued operations

5-year order backlog trend

€ billion



Data like-for-like excluding discontinued operations

## Operating profit

€ million	2007	2006
Commercial Vehicles	1,039	698
Diesel Engines	313	229
Turbo Machinery	104	71
Industrial Services	179	119
Others/Consolidation	95	(12)
<b>Operating profit</b>	<b>1,730</b>	<b>1,105</b>

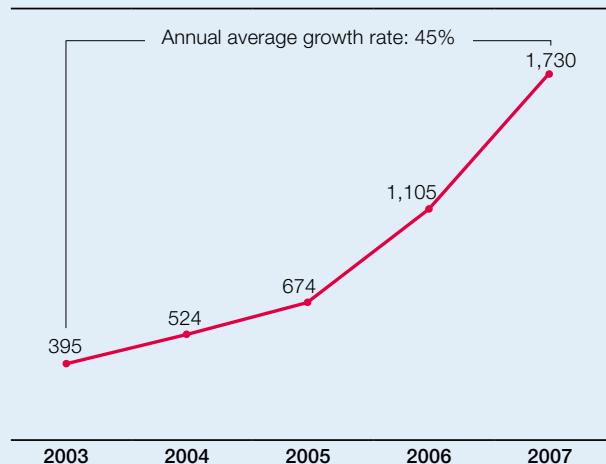
Following its 64-percent surge the previous year, the MAN Group's operating profit was in 2007 again vigorously boosted to a new all-time high of €1,730 million (up 57 percent from €1,105 million). Given the ongoing growth in business volume and the repeated efficiency enhancement efforts, all business areas shared in the marked improvements. Once again, the advance in operating profit outpaced the 19-percent sales rise by far.

The operating profit at Commercial Vehicles rose by 49 percent or €341 million to €1,039 million. Diesel Engines upgraded its by €84 million or 37 percent to €313 million, Turbo Machinery its operating profit by 47 percent or €33 million to €104 million, Industrial Services improving its by 50 percent or €60 million. Others/Consolidation (which consolidates the earnings from the RENK industrial subsidiary, MAN AG plus its shared-service companies and includes the prorated earnings from the MAN Roland stake and the Scania dividend) improved its performance mainly thanks to RENK (up from €38 million to €68 million), the first-time collection of the Scania dividend, and the absence of the prior-year one-off costs and expenses.

Business and performance by business area are set forth in detail starting from page 120 of this management report.

### 5-year trend of operating profit

€ million



Data like-for-like excluding discontinued operations

During the past five years the MAN Group's operating profit has improved considerably. In the period from 2003 through 2007, we have more than quadrupled earnings, from €395 million to €1,730 million, and pushed up sales by 49 percent.

## Income statement

	2007		2006	
	€ mill.	%	€ mill.	%
Net sales	15,508	100.0	13,049	100.0
Cost of sales *	(11,901)	(76.7)	(10,161)	(77.9)
Gross margin	3,607	23.3	2,888	22.1
Other operating income *	738	4.8	609	4.7
Selling expenses	(911)	(5.9)	(813)	(6.2)
General administrative expenses	(749)	(4.8)	(679)	(5.2)
Other operating expenses *	(1,096)	(7.1)	(950)	(7.3)
Net investment income *	141	0.9	50	0.4
<b>Operating profit</b>	<b>1,730</b>	<b>11.2</b>	<b>1,105</b>	<b>8.5</b>

\* In 2007 excl. the proratable nonrecurring result of a total €183 million

Sales in 2007 climbed 19 percent. Since cost of sales grew 17 percent in the period, the relative gross margin edged up from 22 to 23 percent.

Selling expenses in 2007 mounted 12 percent to €911 million, also due to the expansion of our international distribution networks. The rate of increase of general administrative expenses remained below that of sales, they advanced to €749 million.

Other operating income surged €129 million to €738 million (excluding nonrecurring factors), primarily thanks to higher gains from financial instruments, the remeasurement according to IAS 39 of currency hedges and hedged underlyings, as well as from interest rate hedges. These gains contrast with virtually same-amount losses, which largely explains the €146 million rise of other operating expenses to €1,096 million (excluding nonrecurring factors). Moreover, R&D expenditures were leveled up.

The €91 million increase in investment income is basically attributable to the €43 million Scania dividend and higher prorated profits from investments carried at equity, that from methanol and ammonia plants rising by €26 million and that from MAN Roland by €12 million.

## Reconciliation from operating profit to net income

€ million	2007	2006
<b>Operating profit</b>	<b>1,730</b>	<b>1,105</b>
Net nonrecurring result	183	–
Net interest expense	(61)	(82)
<b>EBT</b>	<b>1,852</b>	<b>1,023</b>
Income taxes	(631)	(273)
Posttax profit of discontinued operations	4	175
<b>Net income (EAT)</b>	<b>1,225</b>	<b>925</b>
EpS of continuing operations in €	8.24	5.05
Total cash dividend per share in €	3.15	2.00

In fiscal 2007, several factors and circumstances produced nonrecurring income and expenses that do not impact on operating profit. For instance, as early as the first half of 2007, we had planned a restructuring program for Buses since, despite enormous efforts, this unit failed to get even close to our ROCE benchmark. As Buses business continued poor even in the latter half, we decided to purge the product portfolio and delisted several models from our range. With the agreement made in

early 2008 for the Salzgitter location, we further streamlined production structures, besides integrating Buses more closely into Trucks. We predict the Buses restructuring expenses to total €65 million. In the period, we fully wrote off the €85 million goodwill from the Neoplan acquisition. Accruals of €35 million provide for warranty obligations for delisted products, bringing the total Buses-related nonrecurring expense to €185 million.

In favorable contrast, the settlement after years of litigation of the ERF case upon agreement with Freightliner resulted in an indemnification of £250 million. In this context, the residual €34 million goodwill from the ERF acquisition was derecognized since the indemnity paid reduced to nil the original cost, thus also removing the basis for any goodwill capitalization. The nonrecurring result further reflects a €33 million gain from the Scania stock split and repurchase, bringing the net total for 2007 to a black €183 million.

The net interest expense of €61 million mirrors not only interest from bank credit and debit balances but also the net interest portion from pension obligations and was slashed by €21 million as bank interest charges were downscaled. The MAN Group's EBT soared by €829 million to €1,852 million.

The MAN Group's tax expense surged €358 million to €631 million, the tax load ratio—determined from the income tax rates of German and foreign subsidiaries, as well as from earlier-period taxes and tax-exempt income and gains—rising from 26.7 to 34.1 percent.

The posttax profit of discontinued operations came to €4 million and represents the net from the disposal of MAN Ferrostaal's Steel Trade and additions to accruals for guaranties and warranties in connection with divestments in previous years.

The MAN Group earned net income (EAT) of €1,225 million (up 32 percent); earnings per share of continuing operations improved from €5.05 to €8.24.

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**Proposed dividend: €3.15 per share**

MAN AG's Executive and Supervisory Boards will propose to the annual general meeting to distribute a total cash dividend of €3.15 per share (up from €2.00), corresponding to a 58-percent or €1.15 upgrade per share

**Again beyond expectations**

The excellent overall business success has by far surpassed all expectations we had when writing last year's management report, and substantially been spurred by an outstanding order situation, which resulted in higher workloads and sales, and also by the impact of our efficiency enhancement programs. The originally envisaged high single-digit growth rate was considerably outnumbered by the actual 19-percent sales increase. The return on sales of 11.2 percent also well outperformed the 9.0 percent we budgeted a year ago. Operating profit, too, exceeded our January 2007 predictions. When this general uptrend emerged in sufficiently specific outlines in the course of the period, we commensurately revised upward and communicated our expectations.

## Controlling system and VA management

Focal financial controlling parameters within the MAN Group are operating profit, ROS (operating profit returned by sales), and ROCE (operating profit returned by annual average capital employed). These indicators are used to assess performance not only at MAN Group level but also at the level of each business area, as well as major portions of variable management compensation.

### Performance benchmarks raised

For the period 2005 through 2007 we had set for the MAN Group a 6.0-percent ROS and an 18.0-percent ROCE benchmark in each case as an average for an economic cycle. Recent years' structural improvements enabled us to already achieve these benchmarks and so we decided to adopt new more ambitious ones. For the years ahead, the ROS benchmark is now 8.5 percent and for ROCE we are targeting figures in excess of 22 percent. The former applies to the Group as such and all the subgroups. For Commercial Vehicles and Turbo Machinery the ROS bandwidth across an economic cycle is  $\pm 2$  percentage points, for Diesel Engines, because of the greater long-term volatility of the 2-stroke licensee business, the bandwidth is  $\pm 4$  percentage points, and for Industrial Services it is  $\pm 1$  percentage point.

### Operating profit

Prime parameter for assessing and controlling a business area's profitability is the operating profit. As a rule, operating profit equals EBIT. Significant income and expenses that originate from extraordinary events or sources outside ordinary business operations are eliminated restrictively on a case-by-case basis. While in fiscal 2006, no such adjustments had been made, fiscal 2007 produced a net nonrecurring income of €183 million which is reflected in EBIT but not in operating profit.

For the breakdown of operating profit by business area, see page 194.

## ROS

%	2007	2006
Commercial Vehicles	10.0	8.0
Diesel Engines	14.4	12.7
Turbo Machinery	9.4	7.8
Industrial Services	12.4	8.6
<b>MAN Group</b>	<b>11.2</b>	<b>8.5</b>

With an ROS of 11.2 percent (up from 8.5), the MAN Group clearly again topped its target in 2007. All business areas contributed by substantially raising their ROS and hence their operating profit hike again outpaced sales increases.

With its business volume again up and thanks to efficiency measures Commercial Vehicles raised its ROS from 8.0 to 10.0 percent, despite losses at Buses; truck business alone achieved 11.3 percent (up from 8.8). The previous year Diesel Engines' ROS had reached a substantial 12.7 percent and in 2007 this climbed even higher to 14.4 percent making Diesel Engines easily MAN's most profitable business area. Turbo Machinery likewise attained a notable improvement from 7.8 to 9.4 percent as did Industrial Services whose ROS surged from 8.6 to 12.4 percent thanks in particular to the lucrative stakes in the methanol and ammonia complexes.

**ROCE**

€ million	2007	2006
<b>Equity</b>	<b>5,177</b>	<b>3,779</b>
Pension obligations	132	946
Financial liabilities	1,967	2,108
	<b>7,276</b>	<b>6,833</b>
Volume not funded by MAN Finance equity	(1,939)	(1,727)
<b>Total CE of the MAN Group at Dec. 31</b>	<b>5,337</b>	<b>5,106</b>
<b>Annual average CE of the MAN Group</b>	<b>5,488</b>	<b>4,222</b>
<b>Operating profit *</b>	<b>1,752</b>	<b>1,181</b>
<b>ROCE in %</b>	<b>31.9</b>	<b>28.0</b>

\* Incl. the discontinued operations' operating profit of €22 million (down from €76 million)

The return on capital employed (ROCE) relates operating profit to the annual average capital employed (CE). For the MAN Group, we determine CE from how capital employed is funded. CE breaks down into the MAN Group's equity, pension accruals and financial liabilities, less the volume not funded by MAN Finance equity. The operating profit also accounts for that of discontinued operations up to the date of their disposal as these operations are funded from the Group's capital. The rise in annual average capital employed is chiefly due to the equity surge after a steep earnings upswing.

The capital employed by a business area is derived from the asset side. An Industrial Business area's CE comprises its entire assets other than financial and tax assets, less all accruals and liabilities other than financial liabilities, pension accruals and tax liabilities.

Prepayments received are only deducted to the extent that they have already been appropriated to work in process.

Despite the higher average CE, the MAN Group's ROCE was boosted from 28.0 to 31.9 percent.

**WACC**

The Group's weighted average cost of capital (WACC) corresponds to the minimum return investors expect to earn for their capital and the investment risk. It is determined as the weighted average cost of equity and debt, equity cost being calculated on a CAPM (capital asset pricing model) basis by applying an interest rate for long-term risk-free investments plus a premium for the specific risk from investing in MAN stock. Debt cost, too, is based on an interest rate for risk-free investments plus a risk premium for long-term investments in corporates.

We maintain WACC (based on 11.0 percent pretax) as control parameter for ROCE benchmarking and hence at this level over a longer period of time.

**MAN Value Added (MAN VA)**

This financial indicator shows if the MAN Group and its business areas have earned their cost of capital and added value beyond. MAN VA equals the differential between our ROCE and WACC, multiplied by CE.

The MAN Group added value of €1,148 million in 2007, 60 percent above the prior year's €717 million. All business areas outearned their WACC, generating MAN VA beyond. Absolute outperformer was Commercial Vehicles, adding value of €762 million to MAN's (up from €404 million including Financial Services).

**MAN VA by business area**

€ million	2007	2006	2007	2006	2007	2006
	Operating profit	Operating profit	Average CE	Average CE	MAN VA	MAN VA
Commercial Vehicles	1,039	698	2,497	2,640	762	404
Diesel Engines	313	229	444	492	264	175
Turbo Machinery	104	71	216	232	81	45
Industrial Services	179	119	485	382	126	77
<b>MAN Group * **</b>	<b>1,752</b>	<b>1,181</b>	<b>5,488</b>	<b>4,222</b>	<b>1,148</b>	<b>717</b>

\* Incl. the €22 million operating profit of discontinued operations

\*\* Due to different CE formulae, the business areas do not add up to the MAN Group's total.

## FINANCIAL POSITION

### Principles and objectives of financial management

The MAN Group's finances are centrally managed by MAN AG which decides on the intragroup allocation of financial resources, secures the Group's financial independence and liquidity at all times, and communicates on the entire Group's behalf with the capital markets. MAN AG's Executive Board is responsible for the due and proper conduct of financial transactions, as well as for the deployment of an appropriate financial risk management system, throughout the Group.

The tasks and purposes of financial management are to secure liquidity at all times, contain financial risks, and add value to MAN.

Securing liquidity at all times includes the use of suitable financial instruments, guaranty commitments and other master agreements which ensure reliable access to debt and equity markets and financial institutes. Thus, the MAN Group has always the necessary financial scope for funding business operations and capital expenditures.

It is essential that financial risks affecting enterprise value and profitability be contained by efficiently hedging (mainly through the capital markets) against such risks as currency, interest rate and price risks inherent in commodities or any other price risks whatsoever, as well

as by actively managing counterparty and country risks as well as collateral received.

Financial management adds value to MAN by optimizing the results of all financial moves and transactions in proactively adapting the Group's liquidity and asset and capital structure according to requirements, shifting financial risks cost-effectively and ensuring the efficiency of handling and processing these tasks.

### Cash flow

For the MAN Group's consolidated statement of cash flows, turn to pages 146 and 147. For a conclusive, explanatory analysis of the financial position, financial information is broken down into Industrial Business and Financial Services; the latter includes customer financing transactions of MAN Finance for commercial vehicles leased to customers.

The table below analyzes the movement of our net liquid assets, a financial controlling parameter consisting of cash and cash equivalents, securities and financial liabilities.

€ million	Industrial Business		Financial Services	
	2007	2006	2007	2006
<b>Net liquid assets/(Net financial debt) at Jan. 1</b>	<b>572</b>	<b>1,270</b>	<b>(1,518)</b>	<b>(1,097)</b>
Cash earnings	1,656	923	5	40
Change in net CE	433	271	15	(457)
Cash flow from operating activities	2,089	1,194	20	(417)
Cash flow from investing activities	(421)	(1,321)	(5)	(8)
Free cash flow	1,668	(127)	15	(425)
Cash flow from net financial debt financing activities	(953)	(549)	(46)	(17)
<b>Cash-based changes in net liquid assets/net financial debt</b>	<b>715</b>	<b>(676)</b>	<b>(31)</b>	<b>(442)</b>
Other changes in net liquid assets/net financial debt	(139)	(22)	(46)	21
<b>Net liquid assets/(Net financial debt) at Dec. 31</b>	<b>1,148</b>	<b>572</b>	<b>(1,595)</b>	<b>(1,518)</b>

The MAN Group's free cash flow amounted to €1,683 million in 2007, Industrial Business's to €1,668 million (including the £250 million from the ERF settlement less a net €26 million from the purchase of further Scania shares, the Scania dividend, and the Scania stock split with share repurchase). Adjusted for these nonrecurrent factors, Industrial Business generated in 2007 a free cash flow of €1,326 million, well in excess of Industrial Business's posttax profit (EAT) of €1,121 million after adjustment for the net nonrecurring income of €183 million, the Scania dividend of €43 million and the related income taxes, the reason being the €433 million slash in net capital employed. Financial Services' free cash flow of €15 million reflects the cash inflow from the sale to Hannover Mobilien Leasing GmbH of leased vehicles from the MAN Finance pool, net after offset against the extended customer financing volume of commercial vehicles.

We used the higher free cash flow not only to distribute a total cash dividend of €297 million but also to bolster our financial position by downsizing our financial liabilities by €288 million and endowing our pension fund with another €702 million. The MAN Group's net financial debt was substantially upgraded, from €946 million a year ago by €499 million to a net debt of €447 million. Industrial Business improved its net liquid assets by €576 million, from €572 million at year-end 2006 to €1,148 million as of December 31, 2007, while Financial Services stepped up its net financial debt from business volume refinancing to €1,595 million (from €1,518 million).

## MAN Group funding

Current net liquid funds suffice to largely finance the MAN Group's operating activities. Debt-funded finances are ensured through a syndicated variable-rate credit facility of €2.0 billion granted by a consortium of 25 banks for a term up to December 2010. This credit facility was utilized neither as of December 31, 2007, nor as of year-end 2006.

Another group-funding cornerstone is the €300 million 5.375-percent 2003/2010 Eurobond issue floated by MAN AG in December 2003 through MAN Financial Services plc, Swindon, UK. Repurchases in 2007 scaled back the total par value of the bond issue to €240 million.

Under the floating-rate credit facility agreement with a banking syndicate to fund the acquisition of Scania stock, a facility portion of €1,000 million was utilized as of December 31, 2007, after repayments in 2007. The unutilized balance of this facility (originally €11 billion) expired. The credit facility portion utilized carried interest in 2007 at an average 4.45 percent annually.

Equity-based financing is ensured by authorities conferred on MAN AG's Executive Board by the annual general meeting, including authorized capital of €188 million (50 percent of the capital stock) for the issuance of fresh shares against cash contributions or—up to 20 percent of the capital stock—in return for contributions in kind. Moreover, the Executive Board is authorized to issue convertible or warrant bonds at a total par value of €1.5 billion for a maximum term of 20 years.

## Asset and capital structure

In a year-on-year comparison, total assets of Industrial Business soared €720 million to €14.1 billion. The main reason was the Scania stock price rally (at €450 million) which boosted the value of investments accordingly. Besides the prorated profits for 2007 from investees carried at equity, the addition of the 50-percent stake in MAN Region West B.V., Vianen, Netherlands, and the 33.33-percent interest in Coutinho & Ferrostaal GmbH & Co. KG contributed to the increase.

The business volume expansion not only drove up inventories (by €256 million) and trade receivables (by €233 million) but, on the liabilities side, also prepayments received (up €472 million). The €1.4 billion equity surge is primarily ascribable to the high EAT for 2007 and the Scania stock price soar (which boosted OCI). The €813 million shrinkage of pension obligations was largely caused by the additional €702 million endowment for the pension plans.

The net cash inflow was used not only for the additional pension fund endowment but also to repay financial liabilities. Intragroup funding of Financial Services from Industrial Business's liquid assets was leveled down by €111 million to €975 million.

Following the great leap of equity, the cover ratio of fixed assets (tangible/intangible assets, investments) to equity

€ million	Industrial Business		Financial Services	
	2007	2006	2007	2006
Tangible and intangible assets	2,092	1,997	4	91
Investments	2,259	1,595	7	1
Assets leased out	1,074	1,590	727	805
Tax assets	563	717	6	5
Inventories	3,239	2,983	40	49
Trade receivables	2,557	2,324	1,148	663
Assets of disposal groups	13	244	–	–
All other noncurrent and current assets	809	783	103	237
Financial funds	1,494	1,147	26	15
<b>Total assets</b>	<b>14,100</b>	<b>13,380</b>	<b>2,061</b>	<b>1,866</b>
Equity	5,054	3,643	123	136
Pension obligations	130	943	2	3
Financial liabilities	1,321	1,661	646	447
Intragroup finance	(975)	(1,086)	975	1,086
Accruals	1,579	1,507	9	8
Prepayments received	2,029	1,557	2	0
Tax liabilities	1,084	817	16	33
Trade payables	1,560	1,513	245	89
Liabilities of disposal groups	–	95	–	–
All other noncurrent and current liabilities	2,318	2,730	43	64
<b>Total capital</b>	<b>14,100</b>	<b>13,380</b>	<b>2,061</b>	<b>1,866</b>

was upgraded by 14 percentage points from 102 to 116 percent. Industrial Business's equity ratio climbed from 27.2 to 35.8 percent. For the MAN Group as a whole, equity outcovered fixed assets by 19 percent (up from 3), the equity ratio jumping from 24.8 percent to 32.0.

Flourishing business meant that total assets of Financial Services mounted from €1.9 billion to €2.1 billion. Liabilities of €646 million are debt-funded, €975 million being refinanced through intragroup financial resources.

As of December 31, 2007, the MAN Group improved its net financial debt to €447 million (down from €946 million). This 2007 net is the balance of cash and cash equivalents of an aggregate €1,266 million (up from €1,162 million plus securities of €254 million (up from €0 million) and financial liabilities of €1,967 million (down from €2,108 million).

## Noncapitalized assets and off-balance financing instruments

Besides its capitalized assets, the Group also resorts to noncapitalizable assets, such as the MAN brand as a major incorporeal asset, plus patents from internal R&D and our services and sales networks for customers. For us, the associated expenses are investments in the future and safeguard our market success for the years ahead.

MAN AG's capital stock amounts to an unchanged €376,422,400, divided into 147,040,000 no-par bearer shares, these subdivided into 140,974,350 shares of common, and 6,065,650 shares of nonvoting preferred, stock.

For further details of our capital stock, stock classes, the annual general meeting's approval of the Authorized Capital 2005 and the issuance of convertible and warrant bonds, including the associated authorized but unissued

capital thus created (Contingent Capital 2005), as well as the 2007 authorization to acquire treasury stock, see the section below, *Statutory disclosures pursuant to Art. 315(4) HGB and explanatory report according to Art. 120(3) clause 2 AktG*.

## Statutory disclosures pursuant to Art. 315(4) HGB and explanatory report according to Art. 120(3) clause 2 AktG

### Breakdown of capital stock, stock classes

MAN AG's capital stock amounts to an unchanged €376,422,400, divided into 147,040,000 fully paid-up no-par bearer shares, these subdivided according to Art. 4(1) of the Memorandum & Articles of Incorporation (the "Bylaws") into 140,974,350 shares of common, and 6,065,650 shares of nonvoting preferred, stock. Each no-par share represents a notional €2.56 interest in the capital stock. According to Art. 4(2) clause 2 of the Bylaws, no stockholder may insist on the issuance of a physical share certificate.

Both stock classes rank for dividend, however, a cumulative preferred dividend of €0.11 per share of preferred stock being payable in advance from net earnings and another €0.11 per share of common stock subsequently. If net earnings do not suffice to pay the preferred dividend, the balance short is payable in arrears (without carrying interest) from the succeeding year's net earnings prior to the distribution of any dividend to common stockholders.

Common stock is voting, preferred stock nonvoting. Pursuant to Art. 140(2) German Stock Corporation Act ("AktG"), this does not apply in cases where (i) the preferred dividend has not or not fully been paid for any one fiscal year and (ii) the arrears plus the full preferred dividend have not been paid in the succeeding fiscal year. In any such case, (i) preferred stockholders have a voting right until such arrears have been duly paid and (ii) the preferred stock is included when calculating any capital majority required by the law or Bylaws. Moreover, preferred stockholders are entitled to vote pursuant to Art. 141(1), (2) clause 1 in conjunction with Art. 141(3) AktG. According to these provisions, a resolution of approval is required of the preferred stockholders when adopting a resolution at a general meeting which would cancel, revoke or limit the preferred dividend, or result in the issu-

ance of preferred shares that rank prior to, or *pari passu* with, the existing nonvoting preferred stock in terms of distribution of profits or corporate assets.

In all other respects, the same rights and obligations attach to all the shares.

### Restrictions on voting or share transfer

We are not aware of any voting restrictions except for those on preferred stock and imposed by the law, such as under the terms of Art. 136 AktG. The same applies *mutatis mutandis* to share transfers except that shares granted to Executive Board members under the MSP (MAN Stock Program) are subject to a waiting period. For details see the Board Compensation Report.

### Shareholdings above 10 percent

The provisions of Sec. 21(1) German Securities Trading Act ("WpHG") require any investor that, by way of acquisition, disposal or otherwise, reaches or crosses above or below a threshold of 3, 5, 10, 15, 20, 25, 30, 50 or 75 percent of a listed company's voting capital, is obligated to report so to the listed investee (i.e., MAN AG) and to BaFin (German Federal Financial Supervisory Authority). Sec. 28 WpHG prevents a stockholder who has failed to comply with this reporting obligation from exercising voting rights for as long as the violation of Sec. 21(1) continues.

Pursuant to Sec. 21(1) clause 1 WpHG, Wolfsburg-based Volkswagenwerk AG notified MAN AG in February 2007 that its voting interest in MAN AG had crossed above the 25-percent mark, then coming to 29.9 percent. No further direct or indirect shareholdings in MAN AG which equal or exceed 10 percent of the voting rights have been reported or are known to us.

### **Appointment and removal of Executive Board members, amendments to the Bylaws**

The appointment and removal of MAN AG's Executive Board members are governed by Arts. 84 and 85 AktG as well as Art. 31 German Codetermination Act ("MitbestG") in conjunction with Art. 5 of the Bylaws. Accordingly, the Executive Board shall have not less than two members. The Supervisory Board is entitled and authorized to appoint an Executive Board member for a maximum 5-year term of office and revoke the appointment if for good cause.

The provisions of Arts. 179 et seq. AktG apply to any amendment of the Bylaws. Accordingly, any amendment to the Bylaws requires a special resolution (i.e., with a minimum 3-quarter majority) of the capital stock present or represented at the vote thereon. Art. 10(5) of the Bylaws entitles and authorizes the Supervisory Board to vote on amendments that affect only the wording of the Bylaws.

### **Executive Board powers, also to issue and repurchase stock**

The Executive Board's powers are governed by the provisions of Arts. 76 et seq. AktG in conjunction with Art. 6 of the Bylaws. Accordingly, the Executive Board is responsible for managing and conducting the business of the Company and representing the Company in and out of court.

The disclosures below describe the Executive Board's powers to issue and/or repurchase MAN shares. In 2007, none of these authorities was exercised.

### **Authorized Capital 2005**

According to the resolution by the annual general meeting of June 3, 2005, MAN AG's Executive Board is authorized, after first obtaining the Supervisory Board's approval, to increase the Company's capital stock on or before June 2, 2010, by an aggregate maximum of €188,211,200 (50 percent of the capital stock) through one or several issues of bearer shares of common stock in return for cash and/or contributions in kind (Authorized Capital 2005).

While stockholders must generally be granted a subscription right, the Executive Board is authorized, subject to the Supervisory Board's prior approval, to exclude

the stockholders' subscription right in the case of a non-cash capital increase for the purpose of acquiring other enterprises, any equity interest therein or other material assets from these. In a stock issue in return for cash contributions, the Executive Board is authorized, subject to the Supervisory Board's consent, to exclude the stockholders' subscription right (i) where required to grant the creditors of convertible, or holders of warrant, bonds issued or issuable by the Company or its subsidiaries the right to subscribe for new stock to the extent they would be entitled to upon exercise of their conversion or option rights (antidilutive provision), and/or (ii) if the issue price of new shares is not more than 5 percent below market and provided that the total stock issued pursuant to Art. 186(3) clause 4 AktG does not exceed 10 percent of the capital stock. Such shares shall be counted toward this limit as (i) by application of this proviso (whether direct or extended by virtue of other authorizations) have been issued or sold during the term of this authority up to the date of its exercise, and (ii) have been or will be issued in accordance with the terms of convertible or warrant bonds issued when this authority is exercised hereunder, and/or (iii) to apply fractions toward the rounding of the capital stock. For additional details, see Art. 4(3) of the Bylaws.

According to the statement of May 24, 2005, the Executive Board will exercise this authority when increasing the capital against noncash contributions for the purpose of acquiring other enterprises or equity interests therein or other material assets, only up to an aggregate €75,284,480 (20 percent of the current capital stock).

### **Issuance of convertible/warrant bonds; Contingent Capital 2005**

At their annual meeting on June 3, 2005, the stockholders further authorized the Executive Board (endorsing this resolution on May 10, 2007), subject to the Supervisory Board's consent, to raise an aggregate maximum of €1.5 billion on or before June 2, 2010, by issuing once or several times in return for cash convertible and/or warrant bonds with a maximum term of 20 years as from issuance date. The bondholders will in this case be granted warrants or conversion privileges for subscribing for new bearer shares of MAN AG common stock at a maximum of €76,800,000 (around 20 percent) of the capital stock, all subject to the detailed convertible or warrant bond terms.

This authority also covers the option of guaranteeing bonds issued by other MAN companies and granting MAN AG shares in settlement of the conversion or option rights conferred by such bonds.

Concurrently, by resolution of the annual general meeting of June 3, 2005, the capital stock was conditionally increased by up to €76,800,000 (authorized but unissued capital), divided into a maximum of 30,000,000 bearer shares of common stock. The contingent capital increase will only be implemented to the extent that (i) holders of convertible or warrant bonds which had been issued by MAN AG or MAN companies by dint of the resolution of authorization of June 3, 2005 (endorsed by resolution of the annual general meeting of May 10, 2007) in return for cash, exercise their bond rights and (ii) such rights are not settled or satisfied other than by stock issue. The new stock will for the first time rank for dividend for the year of issuance (Contingent Capital 2005).

### **Stock repurchase**

The authority conferred by resolution of the annual general meeting of May 19, 2006, to repurchase treasury stock was superseded at the effective date of the resolution of the annual general meeting of May 10, 2007.

The resolution adopted by the stockholders at their annual meeting on May 10, 2007, authorized the Executive Board, after obtaining approval from the Supervisory Board, to repurchase on or before November 9, 2008, once or several times MAN AG common and/or nonvoting preferred stock. The authority is capped throughout at an aggregate 10 percent of the capital stock, any other treasury shares held by, or assigned under the terms of Arts. 71d and 71e AktG to, the Company always being counted toward this cap. Such treasury stock may also be reacquired by other MAN companies and/or third parties for the account of MAN AG or other MAN companies.

Such treasury shares may be acquired via stock exchange or by public offering to the holders of the respective stock class. If acquired via a stock exchange, the purchase price excluding incidentals may not be more than 10 percent above or below the price quoted for the respective stock class at the opening auction of that market day's Xetra trading (or any comparable successor system). In a public offering, the bid price or bid price range per share (excluding purchase incidentals) may not be

more than 20 percent above or below the closing price quoted for the respective stock class in Xetra trading (or any comparable successor system) on the third market day prior to the bid's public announcement. If the total stock offered for repurchase exceeds MAN's bid volume, the share offers shall be accepted pro rata. The preferential acceptance of small share numbers may be stipulated to the legally permitted extent, however, not in excess of 100 shares offered by any one stockholder for repurchase by MAN.

The Executive Board is further authorized, subject to the Supervisory Board's prior approval, to use repurchased treasury shares of common stock also in a way other than by (i) sale on stock markets or (ii) public offering to all stockholders, such as for any other lawful purposes while excluding stockholders from subscription. This option shall, in particular, also apply in cases where the repurchased common stock (i) is sold at a price that is not significantly below market, and/or (ii) is used as consideration in a business combination or for the acquisition of other enterprises or any equity interest therein, and/or (iii) is used to settle or satisfy conversion or option rights granted to holders of convertible or warrant bonds which had been issued by MAN AG or MAN companies. The shares transferred by dint of this authority may not exceed an aggregate 10 percent of the capital stock if used to settle or satisfy conversion or option rights granted while excluding the stockholders' statutory subscription right pursuant to Art. 186(3) clause 4 AktG. Such shares shall be counted toward this cap as (i) by direct or indirect application of this provision were issued or sold up to the date of their use while this authority was in force and effect, and (ii) were issued or are issuable at the date of their use in conformity with the terms of convertible or warrant bonds floated in accordance with this provision.

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As resolved by the annual general meeting of May 10, 2007, the Executive Board is further authorized, subject to Supervisory Board approval but without any further vote by a stockholders' meeting, to redeem and withdraw any treasury shares of common and/or nonvoting preferred stock.

**Major MAN agreements terminable upon a change of control in the wake of a takeover bid**

As mentioned above under *Funding of the MAN Group*, MAN AG made agreements with banking syndicates for credit facilities of €2.0 billion and €1.0 billion.

Such agreements can be terminated with immediate effect if and when one or several entities or individuals (either jointly or severally) gain control over MAN AG.

## RESEARCH AND DEVELOPMENT

€ million	2007	2006
<b>R&amp;D expenditures</b>	<b>433</b>	<b>396</b>
R&D expenditures by the manufacturing business areas (% of sales)	3.1	3.4
Internally funded R&D	331	297
Annual average R&D headcount	3,156	3,174

### R&D expenditures by business area

€ million	2007	2006
Commercial Vehicles	234	215
Diesel Engines	129	119
Turbo Machinery	56	45
Industrial Services	0	3
Others	14	14
<b>Total</b>	<b>433</b>	<b>396</b>

The Intergovernmental Panel on Climate Change (IPCC) submitted its keenly anticipated three-part study in 2007 which describes the possible consequences of the greenhouse gas emissions generated by humankind. Since publication of this report at the latest, the causal link between emissions of greenhouse gases, such as CO<sub>2</sub>, and climate change on our planet has been perceived as scientifically substantiated. For many years, the MAN Group has been contributing through its R&D activities to the reduction of greenhouse gas emissions and thus to climate protection. Achieving the maximum possible efficiency in energy use, conserving scarce fossil resources and improving the emission properties of our products remained the focus of our efforts in 2007.

For example, MAN's Commercial Vehicles played an active part in a study initiated by the Federation of German Industries (BDI) and entitled, "The cost and potential for avoiding greenhouse gas emissions in Germany." This study is the first of its kind because it explores the causes of greenhouse gases. In the Commercial Vehicles business area, the two new TGX and TGS truck series were unveiled and crowned as the Truck of the Year 2008 shortly after their market launch. Sophisticated aerodynamics reduce the already low fuel consumption

of the common-rail diesel engine in the TGX series by another 3 percent. The development of innovative and forward-pointing gas, biofuel and hybrid drive systems remains an additional focus of activity. MAN's hybrid buses, for example, have been successfully running within the Nuremberg public transit system on up to 25 percent less fuel than buses equipped with a conventional diesel drive.

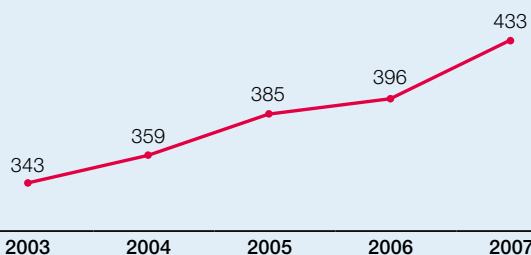
The developments being pursued by Diesel Engines offer our customers the greatest possible flexibility in the choice of fuels used—depending on regional availability. The big engines are already operating on biogas, vegetable oil and other biofuels with considerably lower CO<sub>2</sub> emissions than engines run on fossil fuels. At our CHP diesel power plants, the big engines operate especially efficiently in terms of energy input, achieving energy efficiency levels of up to 95 percent, making them extremely environment-friendly.

One example of the breakthroughs in the Turbo Machinery business area is what is known as geological carbon sequestration, which involves pumping CO<sub>2</sub> into oilfields whose reserves are virtually depleted with the aim of prolonging the production life. Turbo Machinery has developed an eight-stage gear-type compressor for this technique. It compresses the carbon dioxide from a company in the USA, which manufactures synthetic natural gas from coal, from ambient pressure to almost 190 bar. The gas is then piped some 370 kilometers to the north to be fed into a Canadian oilfield in order to increase the latter's yield. The technique has proved effective, thus underpinning Turbo Machinery's technological supremacy in this segment.

In 2007, Industrial Services unveiled together with industrial partners and renowned research institutes a solar thermal demonstration plant in Almería, Spain, based on so-called Fresnel technology. Thanks to the especially flat and low-cost mirrors used at this plant as well as the easily obtainable standard components, such facilities are more economical and efficient than rival technologies. The new technology is scheduled to go into commercial operation following a successful productivity test at the end of 2008. In the long term, solar thermal power plants in the sun-drenched regions around the Mediterranean could produce sufficient electricity to supply the whole European continent.

**5-year R&D expenditure trend**

€ million



Data like-for-like excluding discontinued operations

The MAN Group is investing in its future, consistently spending on the development of innovative products offering high customer benefits and improvements in production at a high level. R&D outlays came to €433 million, representing 3.1 percent of sales by the manufacturing areas.

Internal funding accounted for €331 million, equivalent to 76 percent of total R&D expenditures. An amount of €102 million was spent on order-related R&D activities and publicly subsidized R&D. Some 36 percent of the Group's own funds were invested in basic research and the development of new products.

3,156 employees were engaged in research and development activities in 2007 (down from 3,174).

## CAPITAL OUTLAYS

€ million	2007	2006
for tangible assets and investment properties	411	340
for intangible assets	67	106
for investments	286	1 214
<b>Total</b>	<b>764</b>	<b>1,660</b>
thereof Scania stock purchase	228	1,174
Outlays excl. Scania stock	536	486
thereof in Germany	391	333
thereof abroad	145	153
Amortization/depreciation/write-down *	425	328
Investment ratio in % **	126	148

\* excl. discontinued operations

\*\* excl. Scania stock purchase

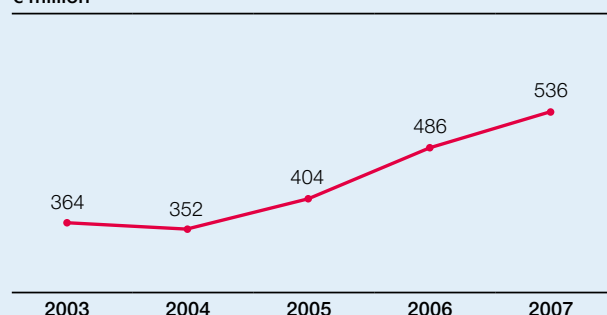
### Capital outlays by business area

€ million	2007	2006
Commercial Vehicles	357	350
Diesel Engines	48	49
Turbo Machinery	39	53
Industrial Services	46	22
Others	274	1,186
<b>Total</b>	<b>764</b>	<b>1,660</b>

Total investing activities in 2007 amounted to €764 million (down from €1,660 million), including €228 million for the purchase of Scania stock (down from €1,174 million). Excluding the Scania shares acquired, our capital outlays for tangibles, intangibles and investments totaled €536 million (up from €486 million), including €145 million or 27 percent spent outside of Germany.

### 5-year trend of capital outlays \*\*\*

€ million



\*\*\* 2006 and 2007 excl. Scania stock purchase.

Data like-for-like excluding discontinued operations.

Capital spending focused on measures to alleviate capacity bottlenecks in production areas that are pivotal to the Group's growth and on acquiring stakes in key-sector companies.

€51 million was expended in 2007 on completing and commissioning the new truck assembly plant at Niepolomice near Kraków in Poland. In all, this plant accounted for capital expenditures of €99 million. Industrial Services spent €24 million on acquiring a 34-percent stake in specialty chemicals company Eurotecnica.

Turbo Machinery and Diesel Engines directed their expenditures toward expanding their servicing, testing and production capacities.

## PROCUREMENT

### Cost of materials by business area

€ million	2007	2006
Commercial Vehicles	5,996	4,763
Diesel Engines	959	900
Turbo Machinery	507	429
Industrial Services	1,028	972
Others/Consolidation	62	23
<b>MAN Group</b>	<b>8,552</b>	<b>7,087</b>

### Cost of materials

in % of sales	2007	2006
Commercial Vehicles	58	55
Diesel Engines	44	50
Turbo Machinery	46	47
Industrial Services	71	70
Others/Consolidation	17	8
<b>MAN Group</b>	<b>55</b>	<b>54</b>

The MAN Group's business areas are expanding their global procurement activities. Through MAN FORCE TRUCKS Private Limited, Akurdi, Pune, India, MAN Nutzfahrzeuge will source locally all the parts needed for truck production in India. Diesel Engines and Turbo Machinery are purchasing in low-wage countries increasingly without having to compromise the quality of MAN products. The cost of materials procured by the MAN Group amounted to €8.6 billion (up from €7.1 billion) or about 55 percent of sales.

So as to generate synergies through the effect of pooling, shared procurements are coordinated from a central department. With the business areas pooling their requirements, the Group's purchasing power in the marketplace is fortified.

The basic procurement volumes are covered by master agreements which guarantee good terms and conditions for the MAN Group while ensuring reliable sources of supply. All major material categories are continually monitored within the purchasing organization through employees, known as lead buyers, especially assigned to this task.

In 2007, we continued to realign groupwide purchasing activities and started to introduce a new and uniform B2B platform across the group. Procurement processes are being increasingly harmonized and efficiency further enhanced as a result.

As part of our global procurement strategy, existing and newly established MAN Houses throughout the world are being utilized in an effort to pool our purchasing activities. We are systematically studying what savings can be made by including suppliers in low-wage countries.

The MAN Group's products are world-leading, thus guaranteeing the success of our brands. This is underpinned by product properties achieved through reliability, economic efficiency and innovative design as well as technical expertise and a high quality and cost awareness. Such merits, in turn, hinge on a commensurate input on the part of suppliers. Commercial Vehicles acknowledges such input and confers annually its Trucknology® Supplier Award on up to ten vendors.

## EMPLOYEES

### Employees at Dec. 31 \*

	2007	2006
Germany	31,611	31,368
Abroad	23,475	22,347
<b>Total</b>	<b>55,086</b>	<b>53,715</b>
Abroad in %	43	42

### Employees by business area at Dec. 31 \*

	2007	2006
Commercial Vehicles	36,591	36,206
Diesel Engines	7,383	6,862
Turbo Machinery	4,011	3,545
Industrial Services	4,687	4,879
Other industrial investees	1,854	1,654
MAN Shared Services	361	365
MAN AG	199	204
<b>MAN Group</b>	<b>55,086</b>	<b>53,715</b>

\* incl. temporary employees (2006 data restated)

### Headcount up

At December 31, 2007, the MAN Group employed a workforce of 55,086 persons, up 1,371 from 53,715. In Germany, the headcount edged up 0.8 percent, abroad it climbed 5.1 percent. Of the total workforce, 43 percent have their jobs outside of Germany.

By scaling up the number of temporary employees, we also greatly improved workforce flexibility given the sharp rise in production. At December 31, 2007, the MAN Group had a total 4,031 temporary employees (up from 3,425). The number of employees with limited-term contracts advanced by 21 percent to 3,500 at December 31, 2007.

### Pension system

The pension system, groupwide substantially the same, is based on a defined contribution plan under which each employee's contributions are linked to annual pay. When going into retirement, instead of current pension payments, employees receive the pension capital (including interest) that has accumulated through their interest-bearing contributions, either in one sum or on an annuity basis. The pension plan for officers and executives within the MAN Group is based on a capital sum and provides that the postretirement capital sum paid out is linked to the performance of certain investment fund indexes.

At the end of 2007, with the approval of BaFin (the Federal Financial Supervisory Authority), MAN Pensionsfonds AG was incorporated, a separate company to which MAN AG and participating group companies assigned a fully externally funded pension obligation volume of about €850 million for around 26,000 pensioners. Major obligations of the MAN Group from closed pension systems which are confined to the payment of life annuities have thus been bundled transparently in one company.

Pensioners benefit from their pension claims having been fully backed by capital and being directly enforceable against the corporate pension fund. The MAN Group remains liable as debtor in default for the pension obligations assigned. In addition, company pensions continue unchanged to be secured by the statutory insolvency insurance via PSVaG, a mutual pension trust fund.

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After adding another €699 million in fiscal 2007 to the capital cover of German pension obligations, the market value of €1,381 million of the special pension fund (including the pension plan assets) covers 92 percent of the German pension obligations of €1,501 million.

Most of the non-German pension obligations are funded externally in full, some are even outcovered. No special endowments were provided in the period.

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## SUSTAINABILITY MANAGEMENT

The MAN Group's continued long-term growth is based on sustainable economic success. We are thus committed to ensuring that the conditions for profitable operations can be sustainably guaranteed in future.

These conditions are marked not only by the economic environment but also by environmental and societal issues. Only in an intact environment and with the acceptance of society have we been able to operate successfully in the past and will we be profitable in the future. Due to increasingly alarming reports the debate about climate change has been pushed to the forefront of the sustainability issue. As a group whose core competence is transport-related engineering, we are aware of our special responsibility. It is the aim of our sustainable corporate management to combine the requirements of a mobile society and an increasingly global, transport-oriented economy with efforts to protect the environment and conserve resources. MAN has a longstanding tradition of seeking to interlink environmental and economic issues and practicing sound corporate citizenship. This is especially true with regard to CO<sub>2</sub> emissions, which are playing a prominent role in the current debate on climate change.

We incur a large proportion of our R&D expenses for improving the environmental efficiency of our products while maintaining their technological supremacy. Here are just a few examples of our innovative resources geared to sustainability: in the Commercial Vehicles business area our TGX and TGS truck series achieve ambitious environmental targets. We are busily engaged in further developing the common-rail engines already in use in compliance with future emission limits and intend to bring these engines on the market as soon as possible. With their low fuel and lubricant consumption, our engines rank among the most eco-friendly and economical commercial vehicle engines in the marketplace. We have also achieved further improvements in our marine diesel engines: equipped with electronic control and common-rail technology, these big diesel engines now consume about a quarter less fuel than 25 years ago, have much lower emissions and are thus ready for the increasingly demanding requirements of the International Maritime Organization (IMO). In the Turbo Ma-

chinery business area, we have the core technological components to produce synthetic diesel fuels or zero-CO<sub>2</sub> fuel from biomass. This represents an attractive future market for us, combining both environmental and economic interests. Moreover, we signed up to the international 3C Combat Climate Change Initiative in 2007, which is striving to reduce climate-damaging emissions worldwide.

We have made good progress on issues relating to corporate citizenship in recent years as well. With our vocational training programs well beyond MAN's own requirements we offer young people the opportunity to acquire a skilled trade. We have also expanded our contacts with universities through the MAN Campus Initiative aimed at attracting talented top graduates. And, we are adopting new methods in our relationship with our workforce: so as to offer skilled women improved employment prospects we are intensively exploring issues related to child-care provision and an improved work-life balance. In addition, we have also made a commitment to substantially increase the still low proportion of women in managerial positions.

In our relaunched and updated mission statement we stipulate our responsibilities to our key stakeholders—customers, investors, employees, and society as a whole. The mission statement, based on our corporate values of reliability, innovation, dynamism and openness, is put into concrete terms by a code of conduct, which is binding on all MAN Group employees. The code of conduct describes in more detail the basic conditions, outlined in the mission statement, governing our operations while demonstrating how our corporate values can be implemented in our daily activities. A Compliance Board, assisted by external ombudspersons, ensures that this code of conduct is adhered to. With these tools we are continuing to guarantee that our actions comply with the principles of good corporate citizenship.

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These few examples prove that we are serious about our strategy of sustainable corporate governance. This strategy is supported by our leadership concept of industrial governance, which underlines our commitment to an up-to-date corporate culture. Detailed examples, facts and figures on our sustainability policy are summarized in our sustainability report, which can be requested or downloaded at [www.man.eu](http://www.man.eu).

This sustainability report continues our comments on issues affecting the environment and society. We also perceive the report as a commitment to our sustainable corporate governance system which we will continue to enact. After all, we can only prove successful when society and the environment are in good health. In pursuit of such goals we rely on the support of our stakeholders and are confident that, backed by this strategy, MAN will continue to do business in a style that reconciles sustainability and profitability.

## THE BUSINESS AREAS

### Commercial Vehicles

The markets of relevance to Commercial Vehicles maintained their momentum in 2007 and we sustained our growth strategy by branching out within C&E Europe and Russia and winning additional market shares in Western Europe. Order intake rose 26 percent to €12.7 billion, up over the high year-earlier €10.1 billion. At €1,039 million (up from €698 million), Commercial Vehicles reported for the third time running an all-time high in operating profit. Thanks to the bulging order books, 2008 is expected to once again show solid progress..

Commercial Vehicles		
€ million	2007	2006
Order intake	12,684	10,103
thereof Trucks	10,996	8,604
thereof Buses	1,688	1,499
Unit order intake	127,345	97,336
thereof Trucks	119,112	90,120
thereof Buses	8,233	7,216
Net sales	10,410	8,685
thereof Trucks	9,023	7,212
thereof Buses	1,387	1,473
Vehicles shipped out	100,609	87,160
thereof Trucks	93,260	79,822
thereof Buses	7,349	7,338
Headcount *	36,591	36,206
Operating profit/(loss) **	1,039	698
thereof Trucks	1,023	632
thereof Buses	(13)	38
thereof Financial Services	30	28
ROS in %	10.0	8.0

\* Headcount incl. temporary employees at December 31

\*\* 2007 incl. €1 million from consolidation between MFI and Trucks

#### Economic environment

Unit sales of trucks within Europe rose 6.8 percent, from 397,000 to 424,000 in 2007 (in terms of EU enlargement, these figures are comparable). Commercial Vehicles raised its truck shipments by altogether 16.8 percent worldwide. The repeated sharp gain in order intake resulted also from revved-up demand outside Europe. Within Europe, we lifted our share of trucks of over 6 t

by 0.2 percentage points to 16.1 percent. Our like-for-like share of the European bus market slipped from 15.0 to 14.9 percent.

Despite global economic uncertainties we are confident regarding further demand trends, especially since we expect unabated momentum from C&E Europe and the CIS.

#### Business trend

Order intake by Commercial Vehicles mounted 26 percent to €12.7 billion. New orders for trucks surged 28 percent from €8.6 billion to €11.0 billion. The number of trucks ordered climbed from 90,120 to 119,112 (up 32 percent). A breakdown of order influx reflects the successful rollout of the heavy-duty TGX and TGS models. Order intake at Buses climbed 13 percent, from €1.5 billion to €1.7 billion, a total of 8,233 units being ordered (up from 7,216).

With 100,609 shipments (up 15 percent) for the first time we delivered over 100,000 units (93,260 trucks, 7,349 buses) within a year. Sales at Commercial Vehicles rose 20 percent or €1.7 billion to €10.4 billion. Of this addition, €512 million resulted from the sale of leased vehicles from MAN Finance's pool to Hannover Mobilien Leasing GmbH. Excluding this one-off effect, the sales increase at Commercial Vehicles was 14 percent. Whereas Trucks business grew 25 percent to €9.0 billion (excluding the sale of leased vehicles, by 18 percent), sales at Buses fell 6 percent to €1.4 billion. At year-end 2007, orders on hand at MAN Nutzfahrzeuge amounted to €6.3 billion (up 49 percent from €4.2 billion).

Our truck plants in both Germany and abroad were very busy. The beginning of October 2007 saw the start-up of the highly automated assembly plant near Kraków, Poland, set to build 15,000 trucks in single-shift operation as early as 2008.

#### Operating profit

Earnings again surged. At €1,039 million, Commercial Vehicles achieved its best ever operating profit, 49 percent over the high prior-year €341 million. ROS rose from 8.0 to 10.0 percent. This repeated operating profit improvement is the outcome of higher volumes and substantial efficiency enhancements.

At Trucks, we raised our operating profit €391 million (up 62 percent) to €1,023 million, bringing the ROS to 11.3 percent (up from 8.8). Factors in this ongoing improvement are the very high capacity utilization and productivity progress as well as more favorable margins. Buses reported an operating loss of €13 million (down from a €38 million profit). The reasons for this were, in particular, poor capacity utilization, high warranty costs, and deteriorated margins. This prompted us back in the first half of 2007 to draw up a restructuring plan which burdened the nonrecurring result with €185 million (for details, see p. 101, *Reconciliation from operating profit to net income*). Together with the €13 million operating loss, Buses weighed on EBT in 2007 with a loss of €198 million.

### Employees

At December 31, 2007, Commercial Vehicles had a workforce of 36,591 (including 2,443 temporary). 20,541 (up from 20,966) were employed in Germany, 16,050 (up from 15,240) abroad. At the close of the period, the number of apprentices totaled 2,127 (up from 2,101), the proportion rising slightly from 5.8 to 5.9 percent.

### Research and development, capital expenditures

During the period, R&D expenditures added up to €234 million (up from €215 million), equivalent to 2.2 percent (down from 2.5 percent) of sales. The R&D departments employed a workforce of 1,709 (down from 1,737) worldwide.

We intend to advance our technological leadership and continue to set standards in terms of quality, safety, and respect for the environment. Numerous trailblazing technologies which we have developed for passenger and goods haulage, relate to emission standards and alternative modes of propulsion. We are the only commercial vehicle builder with engines between 150 and 480 HP (DIN) all with exhaust gas recirculation (EGR) and PM-Kat® according to existing Euro 4. In the heavy-duty range starting from 320 HP, we can supply SCR technology as from October 2009 in compliance with Euro 5. The new V8 with 680 HP is Europe's most powerful standard-production commercial vehicle engine. The first of these, also complying with Euro 5 additive-free and with EGR, had their public premiere in 2007.

Buses, just as Trucks, will comply with Euro 4 using the zero-additive EGR formula with PM-Kat. On the basis of

this, Euro 5 solutions have been developed and these are already in standard production for local buses on regular service and, combined with a particle filter, will even fulfill the again stricter EEV requirements. For tourist coaches, such engines will come into series production in 2008.

At the moment we are the leading supplier of natural-gas buses besides running our hydrogen buses in Berlin traffic conditions. Still being researched yet already on the road are our series hybrid buses plus the 7.5 to 12-t local distribution trucks featuring parallel hybrid propulsion. Brake-energy recovery on these vehicles allows significant fuel and emission reductions.

Most recent developments in driver-assistance systems are moving from comfort-promoting to safety-relevant features as exemplified by the subject of emergency braking that presently commands priority. At the threshold of conceptual completion is a system that alerts the driver to impending emergencies. Also under research is a downstream version allowing timely braking response. To achieve our research goals we are closely examining such underlying issues as driver attention measured as a realization of the respective traffic situation.

At €357 million, capital expenditures were 2 percent up. A major item on the bill was the construction of a new assembly plant in Niepolomice near Kraków, which accounted for a total €99 million. In 2007, work also started on expanding capacities at the Nuremberg engine plant and this will cost altogether €72 million.

Another expenditure focal point is the Munich location which up to 2009 is being systematically enlarged into a main production plant. In 2007, we also started work on the construction of new head-offices and an engineering center.

### Developments ahead

Commercial Vehicles is rigorously enacting its international growth strategy. Our original goal of selling as from 2010 annually at least 100,000 trucks will probably be reached as early as 2008. It is our intention to significantly lift our truck shipments in future, too. In the market for heavy trucks with over 18 t GVW, we have now launched the TGX and TGS models as successors to the successful TGA series. A jury of international trade jour-

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nalists conferred the industry's most coveted award Truck of the Year 2008 on these new models. Completing our cost-effective highly dependable and modern product line-up at the lower end of the market are the TGL and TGM series. For regions outside of Europe, we have engineered two additional series: the new Cargo Line, being built in India specifically for the needs of the Asian and African markets, and the TGA Worldwide primarily destined for C&E Europe. Our two engine ranges, the D08 Common Rail and the D20 Common Rail plus the new D26 Common Rail are the market's most modern truck and bus engines.

The restructuring measures we have planned will inject profitability into our bus business. The production of complete buses destined for local public transportation will be relocated to Poland, the assembly of bus chassis will be restructured, and a major portion of central functions concentrated in Munich. These measures took effect at the start of 2008 and will this year and thereafter substantially enhance earnings.

Given the generally hospitable economic climate prevailing at present and the tall order backlog we expect for 2008 once again good business progress at a rate that repeatedly outpaces the market. Above and beyond this, our strategic target regions are CIS, India, and China. With a view to promoting international growth and hence securing our long-term profitability, we opened in 2007 our Polish truck plant near Kraków and are pushing ahead with our Indian truck affiliate. At Buses, our efforts in 2008 will be chiefly directed at bolstering profitability. We will progress with the efficiency enhancement programs launched and hence arrive at structural improvements and a productivity hike.

In order to further sharpen our profile toward customers and more effectively exploit earnings potentials, we began in 2007 to realign on a worldwide scale our sales organization and invest in the expansion of our distribution and service network. Parallel to these efforts, are closely focused activities aimed at raising customer satisfaction. We are confident that by rigorously pursuing these plans we will continue to show successful progress and further polish our profitability.

## Diesel Engines

Demand for diesel engines was again most buoyant in 2007. Developments in global trading meant that demand for ships remained vigorous. At the same time, many countries were investing in diesel power plants. Given these trends, Diesel Engines once again succeeded in topping a very high prior-year order intake. Sales mounted 21 percent from €1.8 billion to €2.2 billion. The operating profit rose thanks to the appreciably larger sales volume and the resulting high capacity utilization at the production plants, to €313 million, a 37-percent hike. Given the very tall order backlog and the projects for integrating all parts of the company as well as for restructuring the production network, we expect 2008 to see yet another rise in sales and operating profit.

Diesel Engines		
€ million	2007	2006
Order intake	3,371	2,619
thereof Two-Stroke	953	659
thereof Four-Stroke	2,418	1,960
Net sales	2,179	1,802
thereof Two-Stroke	650	576
thereof Four-Stroke	1,529	1,226
Operating profit	313	229
thereof Two-Stroke	144	106
thereof Four-Stroke	169	123
Headcount *	7,383	6,862
ROS in %	14.4	12.7

\* Headcount incl. temporary employees at December 31

### Economic environment

Contrary to the expectations of most experts, 2007 showed another increase in the number of ships ordered and this, in turn, meant for us yet another record 12 months. China's appetite for commodities led to record freight rates for bulk cargo freighters and unleashed a torrent of new orders. Also in strong demand were container, conventional freight, passenger and ferry vessels. Demand for ships employed by the offshore sector stabilized at a high level. The shipbuilding centers were once again located in Asia, especially South Korea, followed by China and, well behind, Japan. Shipyard order books are brimful through 2010.

The repeated global surge in energy consumption again fueled demand for our energy production plant. We are also benefiting from the trend in favor of smaller, locally installed power plants. Gas has gained in significance as a primary source of energy. The sharp rise in oil prices and acuter environmental awareness are factors compelling ship and power plant builders to develop even more efficient solutions.

### Business trend

A spillover of the brimming order books at the shipyards was strong demand for our marine diesel engines with the result that even the very high 2006 order intake was topped. Despite steep oil prices and the repeated erosion of the dollar, order intake for stationary engines was again strong. The power plants are designed for operation by both public utilities and a wide variety of industrial enterprises. A downside of the present market situation: delivery times in some cases stretching up to 2011.

Order intake at €3.4 billion was €0.8 billion up over the very high prior-year volume, order backlog swelling from €2.8 billion to €3.9 billion.

In the market for two-stroke marine engines, the Diesel Engines business area again achieved a share well above 80 percent, thus further expanding its unique position as the foremost developer of large low-speed diesel engines. Total orders on hand for our two-stroke engines at the licensees was equivalent to around 80,000 MW at the end of 2007—enough to keep production busy over the next three years. Deserving special mention are orders for several K98 14-cylinder engines which given the capacity of around 115,000 HP, are presently the most powerful diesel engines sold worldwide and are intended for supersized container ships.

The order situation for four-stroke medium-speed diesels was likewise most congenial, both as propulsion units and for powering onboard equipment. An outstanding contract was for the propulsion of the world's biggest offshore multipurpose vessel Pieter Schelte. Measuring 360 m in length and 117 m in width, this specialty ship will be fitted with nine engines from the new 32/44 CR series delivering a total 95 MW. The first order was placed for the 51/60 DF diesel-gas engine series. Five 8-cylinder engines delivering a total 40 MW will be in-

stalled on a liquefied-gas tanker operated by a Spanish shipping line. Other important applications for our 4-stroke engines included mid-sized container vessels, oil and specialty tankers, RoRo/ferry vessels, cruise ships, dredges, as well as offshore tugboats and supply vessels.

Contracts concluded for four-stroke power plant diesel engines likewise were well above the prior-year level. Highlights included orders for two power plants for Brazil and Pakistan requiring together 19 large V48/60 engines outputting a total of about 360 MW. Other important sales regions were North and Central America, the Caribbean Basin, and Western Europe, this latter prioritizing biofuel engines. The 32/40PGI and 51/60DF roll-outs will make easier for us to share in the gas-engine growth market.

If we consider the total medium-speed engine market of over 0.5 MW including both marine and stationary power generating units, with a market share of 34 percent, here, too, we are leaders.

Within a market characterized by further economic growth, the MAN Diesel Group at its European locations in fiscal 2007 booked orders for 796 four-stroke engines with a total output of 3,990 MW. Of this output, 73 percent is destined for marine applications. During the same period, our licensees sold altogether 3,973 four-stroke engines with a total output of 4,898 MW.

### Operating profit

The operating profit at Diesel Engines rose thanks to the advance in sales volume and the resulting high capacity utilization from €229 million to €313 million (up 37 percent). ROS at 14.4 percent (up from 12.7 percent) was well above the 12.5 percent for years of economic boom (average benchmark of 8.5 percent with an economic cycle-related bandwidth of 4 percent).

### Employees

At December 31, 2007, the MAN Diesel Group employed a workforce of 7,383 (including 546 temporary). Accounting for the extra headcount were alongside the first-time consolidation of the Indian company, additional hirings at Augsburg. In order to cope with the tall order backlog and enhance flexibility, we repeatedly resort to temporary labor, limited-term employment contracts and flexitime arrangements. With its international oper-

ating environment, outlays for advancing employee skills and the establishment of new locations, Diesel Engines is an attractive employer.

### Research and development, capital expenditures

A substantial share of expenditures in fiscal 2007 went toward the restructuring of the business area's diverse production plants into a global production network. In particular, funds during the past period were invested at Saint-Nazaire, France, in order to provide the capacities necessary for the production of the V48/60 engines. Heavy expenditures were also allocated to injection component production facilities.

In order to expand our aftermarket business, we acquired in 2007 from PON Holdings B.V. the diesel-engine related operations of MAN Rollo B.V., The Hague and Zoetermeer, Netherlands, and MAN Rollo Belgium N.V., Antwerp. Services companies were also established in Panama, Italy and Latvia and bases opened in Spain, Sweden, Brazil, Australia, and the United States.

Also accentuated during the period was the development of the 51/60 DF dual-fuel engine for liquefied-gas tankers, its certification by the classification societies representing an important milestone. Since April 2007, we have had the first order for five engines of this type. Additionally, we have applied our efforts toward fine-tuning our engines in terms of fuel consumption, performance, and emission reduction. Associated with such activities is the launch of additional versions with common-rail injection and innovative systems such as the variable nozzle ring and multistage turbocharging. We have also made further progress with regard to the flexible use of fuels. Our big four-stroke engines will run on vegetable oils, frying fat and animal fats. A power plant has placed an order for our two-stroke engines to be operated on vegetable oil.

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**Developments ahead**

Propelled by the very tall order backlog and projects for integrating all MAN Diesel units as well as restructuring the production network, we expect 2008 to once more show rising sales and another hike in operating profit. The workload at the international shipyards is again extremely good. Although the trend is for a slight departure from the all-time high, the expected level over the months ahead will remain very robust. Regarding order intake in 2008, we generally expect stabilization at a still high level. In addition to freighters, feeder, container and cruise vessels, our marketing efforts will be directed in particular at LNG tankers, the offshore and naval sectors.

Worldwide rising energy consumption will sustain demand for stationary diesel, gas and biofuel engines at a high level for some time. We also expect growth from expanding business in turnkey power plants and further stepping up our entire aftermarket operations. The greatest challenge presently confronting the MAN Diesel Group is for the contracted engines to be shipped out in good time. In the medium term, the European production network currently being woven will play a major role in reducing the lead times for the engines we build ourselves.

## Turbo Machinery

Turbo Machinery again expanded its operations in 2007. At €1.5 billion, order intake once more matched the very high year-earlier level. Sales surged 22 percent or €200 million. The operating profit mounted to €104 million, ROS reached 9.4 percent (up from 7.8 percent).

Turbo Machinery		
€ million	2007	2006
Order intake	1,454	1,498
Net sales	1,108	908
Operating profit	104	71
Headcount *	4,011	3,545
ROS in %	9.4	7.8

\* Headcount incl. temporary employees at December 31

### Economic environment

Despite extended delivery times, demand for turbo machinery and drive turbines was sustained. Repeatedly, Asia was the geographical focal point, with business operations again branching out on the Chinese market. Demand was again vigorous on the European market.

### Business trend

New orders matched the very high year-earlier magnitude, a period largely influenced by the Shell Pearl megaproject. Order intake was strong both for new plant and in the service business. We again raised orders booked from the chemical/petrochemical, fertilizer and air separation sectors. Again vigorous sales of steam and gas turbines as compressor drive units cemented our position as single-source suppliers. We also raised shipments of generator steam turbines for energy production using biomass and waste incineration. Profit margins from new equipment again showed marked improvement. The acceleration of our marketing activities, started up in the previous period, enabled us to increase our service business, too.

The expansion of our capacities pushed up sales by 22 percent in 2007. Sales reached €1,108 million (up from €908 million). For 2008, we are planning for a further increase with a view to downsizing the tall order backlogs and shortening the lengthy delivery periods. Capacity expansions will play a decisive role in this regard. In the area of purchasing, steps were also taken for shortening delivery periods at our subcontractors and these will likewise take effect over the coming year and lead to rising sales.

Waves of incoming orders outpacing sales due to capacity bottlenecks impelled order backlog to €1.7 billion by year-end, 23 percent or €0.4 billion over the prior-year total. Bulging order books and the negotiated delivery dates will keep all locations busy, in some cases beyond 2008.

### Operating profit

This jumped from €71 million to €104 million thanks to added sales, improved margins, and the enormous workloads. ROS rose from 7.8 to 9.4 percent.

### Employees

The headcount was again raised to cope with the towering order backlogs, by 466 to 4,011 (including 401 temporary). The growth plans envisage further gains in 2008. At December 31, 2007, the German locations had a workforce of 2,815, the non-German 1,196. The German, Swiss and Italian locations employed 197 youngsters serving apprenticeships in blue, gray and white-collar trades (up from 177). HR efforts focused on integrating the newly hired employees. Topstart is a project comprising a guide for superiors during new-employee induction. In-company and external courses were stepped up and intensified. In order to tie undergraduates to the company at an early stage we have devised a program that provides support for those engaged in university studies parallel to their jobs.

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**Research and development, capital expenditures**

As in the previous year, demand continued unabated for gas-to-liquid (GTL) and other (xTL) liquefaction technologies. The necessary products at both the steam turbine and turbo compressor ends call for heavy R&D outlays since the plants are growing bigger and bigger. MEGA 160 is an ambitious program devised by Turbo Machinery that is beginning to bear fruit. The prototype for a new generation of industrial axial compressors was successfully tested. Existing ranges were significantly upgraded by applying new technologies for maximum achievable pressures and mass flows. The MEGA league requires, moreover, steam turbines with much higher performances. Such machines are only manufacturable using state-of-the-art technologies. Highly advantageous in this context is the steam turbine modular system developed by Turbo Machinery.

Of growing importance in the oil and gas industry is the tapping of deposits hitherto hardly used and the more efficient exploitation of existing resources. Turbo Machinery's response is to develop high-pressure compressors of up to 1,000 bar. For the first time such a machine was successfully tested during the past period as were newly engineered underwater compressors. The high-frequency motor built into these compressors demonstrated its operability in the course of an extensive test program. Tapping virgin oil and gas fields also requires small gas turbines. An important step in this direction was taken with the development and testing of a new gas turbine compressor. These are efforts that will cement for us our worldwide supremacy in such equipment.

One aspect of the ongoing public debate on CO<sub>2</sub> emissions and their impact on the climate is the haulage and storage of CO<sub>2</sub>, and for this purpose turbo machinery is required. For the first time, newly developed standardized gear components were tested for the CO<sub>2</sub> compressors.

Repeated project-independent development work combined with ongoing market intelligence enables Turbo Machinery to come up with timely and marketable attractive products for more and more applications.

The business area pressed ahead with its growth plans launched in 2006 for upscaling capacities. Work started on a new production facility in China as well as on new buildings and extensions at Oberhausen, Deggendorf

and Zurich with a view to boosting production and testing capacities. On the manufacturing front, newly acquired machinery will enhance our productivity. The expenditure program will run on into the new period for a substantial advance in sales. On completion of the building and start-up of the machinery, production will commence at Turbo Machinery's plant in China around Q3/2008. The business area also started out on the construction of a service workshop at the Oberhausen location in 2008 which in time will turn into a competence center for repair work in Europe, thus enabling us to fully exploit growth potentials in the aftermarket. The Hamburg location is revamping its turbine vane manufacturing facility in order to cope with the heavier workload. This, we expect, will lead to much shortened throughput times.

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**Developments ahead**

With the market still congenial, we are confident of booking in 2008 orders at the level of the two preceding periods. Business is expected to again rise especially in oil and gas products as well as air separation equipment. Aftermarket activities will once more be stepped up in order to increase our share of servicing work on our own machine population and our proportion of service contracts. In all, demand is likely to remain strong for all types of equipment and from all regions.

For 2008 we are planning to again hire employees, especially at the new production plant in China. This, combined with another increase in manufacturing and testing capacities, will help us shrink the order backlog, avoid delivery delays, and further shorten lead times.

Rising sales and widened margins will bring about a higher operating profit both in absolute and ROS terms. Ongoing process optimization, cost-reduction initiatives and further product standardization will trigger another accelerated gain in operating profit over the years ahead.

## Industrial Services

Industrial Services continued the strong progress of the previous year. Sales climbed 5 percent to €1.4 billion, the operating profit improved from €119 million to 179 million. At €1.6 billion (down from €2.0 billion) order intake again topped sales. ROS surged from 8.6 to 12.4 percent.

Industrial Services		
€ million	2007	2006
Order intake	1,556	1,982
thereof Projects	849	1,352
thereof Services	707	630
Net sales	1,445	1,379
thereof Projects	694	747
thereof Services	751	632
Operating profit	179	119
Headcount *	4,687	4,879
ROS in %	12.4	8.6

\* Headcount incl. temporary employees at December 31

### Business trend

The entry into the growth market of energy and fuels has again sharpened the international profile of Industrial Services. Alongside our focus on the traditional markets such as petrochemicals and conventional power plant construction, we are developing a promising foothold in the market for renewable energies. A joint venture founded in 2007 together with Solar Millennium will develop and implement solar-thermal plant projects. Through additional partnerships we have also secured for ourselves exclusive access to key technologies in this sector. Renewable fuel sources are other markets in which our activities are pressing ahead.

Order intake at Projects in 2007 fell from €1,352 million to €849 million, due to the extraordinarily high year-earlier order influx as a consequence of the AUM project in Trinidad as well as, in certain cases, a more critical screening of potential projects. Among our most important customers were, especially, petrochemical companies and the power-generating industry.

Sales at Projects added up to €694 million (down from €747 million). The construction of a methanol plant in Oman was successfully completed. From Venezuela we booked a megacontract for an ammonia complex worth

€379 million and modeled on our Trinidad deal. Work has started according to schedule. Also progressing according to plan is the AUM complex in Trinidad, booked the previous period.

International service business proved favorable in 2007, with order intake climbing 12 percent, from €630 million to €707 million. As a consequence, sales jumped from €632 million to €751 million. Triggering this improvement, among other factors, was the decision to supplement our range of high-price machinery with an additional segment for marketing mid-priced equipment of Asian origin. We have thus succeeded in accessing new groups of customers that, in time, can be weaned to the high-price segment.

### Operating profit

Industrial Services' operating profit mushroomed 50 percent from €119 million to €179 million, especially due to our equity interests in the methanol and ammoniac complexes; operating profit from service business likewise showed a sharp improvement. ROS jumped from 8.6 to 12.4 percent.

### Employees

As a company engaged in project development and project management, human resources are our most important asset. Hence the priority we attach to professional personnel management and development. So far 57 employees in and outside of Germany have obtained certification as part of an internationally recognized project management program. Employees also have the option of selecting from a broad range of recognized courses. The headcount fell by 192 to 4,687 (including 512 temporary).

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### Developments ahead

A majority stake in our steel trading business was sold in 2007 to CCC Steel GmbH & Co. KG, Hamburg. The new company came on stream as of January 1, 2008, under the name of Coutinho & Ferrostaal GmbH & Co. KG. Industrial Services holds a 33.33-percent interest in this new limited partnership which will command a leading position in international mill-independent steel trading. With 320 employees at 56 locations in 34 countries, the partnership is budgeting sales in the region of €2.1 billion for 2008. The central locations in Hamburg, Houston and Essen will continue. The merger of CCC Steel and Ferrostaal Metals represents a milestone toward improving the competitive position within a global environment.

As part of our efforts to expand capacity in handling large-scale plant construction projects, we acquired the Portuguese company Koch de Portugal. Its longstanding experience particularly in power plant construction, dovetails outstandingly with our own capabilities.

The establishment of international MAN Houses is proceeding according to plan. Alongside the shared facility opened in Mexico the year before, MAN Houses were opened in Beijing, Dubai and Lima in 2007. Further ones will follow in Moscow, Mumbai and elsewhere in 2008.

Given the inquiries presently being processed, we expect for 2008 growing order intake and advancing sales. In order to achieve a leading position in the rapidly growing market for renewable energies, we intend to expand our activities in the solar power and biofuel sectors.

## Others/Consolidation

€ million	2007	2006
Order intake	309	365
thereof RENK	439	417
thereof shared services/ consolidation	(130)	(52)
Net sales	366	275
thereof RENK	430	356
thereof shared services/ consolidation	(64)	(81)
Headcount *	2,414	2,223
thereof RENK	1,854	1,654
thereof shared services	361	365
thereof MAN AG	199	204
Operating profit	95	(12)
thereof RENK	68	38
thereof MAN AG and shared services	(41)	(68)
thereof Scania dividend	43	-
thereof investee Roland (at equity)	24	12
thereof consolidation	1	6

\* Headcount incl. temporary employees at December 31

Others/Consolidation (which consolidates the earnings from the RENK industrial subsidiary, MAN AG plus its shared services companies and includes the prorated earnings from the MAN Roland stake and the Scania dividend) improved its performance thanks in particular to RENK, the first-time collection of the Scania dividend, and the absence of the prior-year one-off costs and expenses.

RENK slightly upped its prior-year all-time high in order intake to €439 million, with Large-Gear Units maintaining a strong market position. Orders for Drive Elements/Slide Bearings again picked up appreciably. By making the most of existing capacities RENK managed to raise sales 21 percent to €430 million; the operating profit climbed 80 percent to €68 million on account of busy production plants, further productivity improvements and a general upgrade in profit margins. ROS reached 15.7 percent (up from 10.5 percent), an all-time high. With order books bulging RENK expects business in 2008 to continue at the high level of 2007.

## Separate financial statements of MAN AG

Prepared in accordance with German Commercial Code (“HGB”) provisions, MAN AG’s separate financial statements are summarized below. The full financial statements (in German) are available from MAN AG or downloadable from our website: [www.man.eu](http://www.man.eu)

### Results of operations

€ million	2007	2006
Net investment income	1,033	639
Remaining pretax P/L, net	(157)	(136)
<b>EBT</b>	<b>876</b>	<b>503</b>
Income taxes	(379)	(169)
<b>Net income</b>	<b>497</b>	<b>334</b>
Transfer to reserves retained from earnings	(34)	(40)
<b>Net earnings</b>	<b>463</b>	<b>294</b>

MAN AG’s EBT soared in fiscal 2007 by €373 million to €876 million, substantially thanks to the surging investment income in the wake of the greatly booming operating business areas and the divestments. The remaining pretax loss is the net balance of general administrative expenses, net interest income and other income and expenses. The €210 million rise in income tax expenses is largely ascribable to those for prior periods and MAN AG’s higher taxable income.

After transferring €34 million to the reserves retained from earnings, MAN AG reports net earnings of €463 million. The Company’s Executive and Supervisory Boards will propose to the annual stockholders’ meeting on April 25, 2008, to distribute per share a total cash dividend of €3.15 (up from €2.00).

### Asset and capital structure, financial position

€ million	2007	2006
Fixed assets	2,909	2,878
Current assets	3,597	2,983
<b>Total assets</b>	<b>6,506</b>	<b>5,861</b>
Equity	2,216	2,013
Financial liabilities	3,444	3,208
All other liabilities and accruals	846	640
<b>Total capital</b>	<b>6,506</b>	<b>5,861</b>

Most fixed assets comprise investments.

Current assets mainly include the intragroup finance receivables and the cash and cash equivalents which originate from MAN AG’s central group financing system, as do the financial liabilities which have been incurred by MAN AG to centrally fund the Group, their rise chiefly resulting from higher total of cash, cash equivalents, and securities.

In the year under review, the pension accruals for eligible employees and the related security assets were assigned and transferred to newly incorporated MAN Pensionsfonds AG.

### Additional information

The rules governing the appointment and removal of MAN AG’s Executive Board members as well as the amendment of the Bylaws conform with the law.

The principles of the compensation system for Executive and Supervisory Board members are described in the Board Compensation Report, an integral part of the management report for the purposes of Art. 315 HGB. For the itemized breakdown of each board member’s compensation, see Notes (35) and (36) to the consolidated financial statements.

At December 31, 2007, MAN AG’s workforce numbered 199 including temporary employees (down from 204).

## RISK REPORT AND PROSPECTS

### Risk management

Doing business entails a constant exposure to risks. We define risk as the danger that certain events, decisions or actions prevent the Group from achieving defined goals and/or successfully implementing certain strategies. For us, this means seizing opportunities only if we can expect a reasonable addition to MAN's value. Any undertaking consciously accepts risks in order to exploit opportunities surfacing on the market. However, such a policy is only affordable with a risk management system that is effective and tailored to the needs of the business operations.

Risk management within the MAN Group is an inherent component of the various business, business-planning and controlling mechanisms. Together, strategic corporate planning, the internal reporting system and, since 2007, the group ombudsman constitute the core elements of the risk management system. Among the objectives of the strategic planning progress is the early identification and assessment of long-term risks and rewards for the purpose of adopting structural measures. Additionally, the internal reporting system is designed at all levels of the Group to supply up-to-date and relevant information concerning the status of major risks. These elements were supplemented in 2007 with the institution of a group ombudsman for assisting management in identifying in good time any compliance-related risks and responding appropriately.

Our Industrial Governance system is such as to employ local decision-making mechanisms at MAN combined with a risk management system organized in a parallel manner. Despite this, some kind of uniform and standardized framework is necessary and assured by MAN's risk management manual which has groupwide applicability. This contains binding rules for identifying, recording, analyzing, assessing, controlling and monitoring any significant risks within the MAN Group. The risk-related principles and policies it contains ensure groupwide common understanding of risk management. Risks and rewards are identified and quantified quarterly, and discussed and evaluated at review meetings attended by the Executive Board and Corporate Controlling. Where nec-

essary, adequate action is initiated. The Supervisory Board is periodically briefed on the MAN Group's risk position. On the basis of a standardized risk catalog, all of the business areas are required to conduct (at least) quarterly updated risk assessments. Uniformly defined risk areas and evaluation parameters allow the Group to spot risks and, at an early stage, identify and contain any accumulating major risks. The introduction of threshold values for each business area ensures that risks are adequately subdivided into four categories commensurate with the business area's size.

It is up to each business area's management to make sure that the group companies are integrated into the risk management system so that within the areas risk management is practiced according to our principles. Throughout the business areas we have installed risk boards authorized to exercise control and monitoring functions within the MAN Group. These are staffed by representatives from financial, engineering, and legal departments plus the operating units. The job of the risk boards is to identify and assess, in their respective areas, hitherto unidentified risks as well as to initiate and follow up on any risk-control measures and mechanisms.

Internal Auditing and the statutory auditors are responsible for reviewing the workability of the MAN Group's risk management system. The system also explores continuously any possibilities of fine-tuning its mechanisms and improving the processes, data management and reporting tools deployed.

### Risks and rewards

In line with the organization of the MAN Group's risk management system, the following comments explain the significant risk and reward categories that might severely impinge on the asset and capital structure, financial position, or results of operations. In the Risk Management Manual and risk reporting systems, they are broken down into market, product, process, human resources, and finances.

#### Market

The global business climate during the past year was clouded by the emergence of new imponderabilities. Accumulating mortgage repayment problems in the US

property market led to property price adjustments in the United States and liquidity problems for a number of banks. Moreover, years of US balance-of-payment deficits have eroded the value of this nation's currency. In addition, still strong demand on the part of the emerging markets has fueled commodity and food prices, thus entailing the risk of further inflation. For the MAN Group, exchange rate trends might stifle demand in those economies that are tied to the dollar. These risks would be aggravated if exchange and interest rate trends were to jeopardize the economy in our own core European markets. In contrast, rising interest rates and credit restrictions imposed by the banks provide us with an opportunity to bolster customer loyalty through financing terms and conditions in the commercial vehicle market. The strained commodity markets are leading to profit margin risks throughout MAN's business areas wherever rising purchase prices are not downloadable onto customers. There is also the risk of bottlenecks occurring in the supply of parts. In the medium term, nonetheless, the worldwide rise in haulage mileages and volumes, capital expenditures on the part of the oil and gas industries and innovative challenges posed by trends in global climate politics are seen to offer opportunities for profitable growth throughout the Group. Through measured expansion of our sales and distribution networks in the growth markets we are attempting to expand sales potentials and thus effectively absorb short-term risks triggered by economic cycles.

### Products

As a leading supplier in the market for advanced technology, the MAN Group develops products of foremost engineering and cost efficiency which are then launched onto their markets in outstanding quality. Any deviation from this policy would mean an irresponsible risk of market share shrinkage. Nonetheless, the rollout of new products is tied to certain conceptual and market uncertainties which we counter through careful strategic planning processes that scrutinize trends in the markets and corporate environment. The resulting product plans are used for controlling our extensive R&D efforts. R&D outlay by the manufacturing areas has for years now ranged between 3 and 4 percent of sales by these areas. The TGX and TGS market launches by Commercial Vehicles in 2007 demonstrated that these risks can successfully be circumvented; their successful rollout and the repeated

Truck of the Year 2008 award point to the market opportunities open to these models.

In the case of products already launched, there are certain quality risks. Since these products are essential to the smooth functioning of various industries and trouble-free overland and sea haulage, any shortcomings can cause considerable loss or damage. Substandard quality may result in obligatory or nonobligatory (goodwill) warranty costs and/or, in the long run, an erosion of market share or margins. In extreme cases, product liability and compensation claims are conceivable. Identifying and containing such risks is a process commencing right from the product gestation phase at MAN. Our standardized product gestation process ensures that only well-functioning and reliable product concepts are approved for downstream development. Suppliers and their products are required to undergo a strict approval process in order to ensure compliance with our high quality standards. After production start-up, defined quality assurance measures within the production process make sure that manufacturing defects are identified and remedied in good time while when the products themselves are subsequently in operation, together with the service shops any defects are collected, analyzed, and then eliminated. Forthright communication with our suppliers and customers minimizes, where possible, quality-related risks.

Finally, MAN as a manufacturer of capital goods is exposed to risks due to the often extended period between order and delivery. Such risks may, on the one hand, be of a political or economic nature if there is a change in the general market conditions under which a megacontract is being handled. Other sources of risk are contractual, such as buyback and warranty obligations. Buyback obligations at Commercial Vehicles represent a risk whenever the future cash inflow from the sale of used vehicles substantially falls short of expectations entertained at the time the contract was signed. Financing guaranties are part of the Industrial Services business model and cover a wide array of obligations under funding-related bonds or guaranties. These, however, are often covered by third-party guaranties or, where in the form of downpayment bonds, by prepayments received from customers. By meticulously scrutinizing the standing before and after furnishing a guaranty or bond, we have to date been able to keep defaults at a minimum.

### Processes

We perceive the repeated re honing of our processes and mechanisms in R&D, Purchasing, Production, Sales, and Administration as a central and never-ending challenge since any deficiencies lead to excessive capital employed and hence financial risks. Moreover, overstocked inventories regularly entail loss through shrinkage and/or the need to scrap. Too high receivables entail the risk of default. In order to alleviate these risks the MAN Group in 2007 introduced a groupwide and all-embracing optimization project in order to arrive at improvements and lastingly reduce the Group's financing needs. The project has already resulted in the first improvements in terms of materials scheduling and A/R management.

Plant construction and megaproject handling are businesses exposed to special risks including contracting deficiencies, miscosting, post-contracting changes in the economic and technical parameters and poor performance on the part of consortium partners. We address these risks through comprehensive project and contract controlling. Industrial Services, for instance, deploys a special instrument kit to ensure a systematic and comprehensive risk management system right from the bidding phase. This also involves powerful simulation techniques. Megaprojects are additionally scrutinized and assessed by MAN Corporate Controlling and submitted to MAN AG's Executive Board for approval. Should any approved contracts depart significantly from budget or plan they are monitored in a special reporting system for critical contracts.

As in any modern enterprise, the MAN Group's processes largely rely on IT systems which, besides promoting efficiency, also harbor risks. Parts of the system may fail as a result of accident, disaster, malfunction or technical defect, thus impinging on a wide variety of business processes. Unauthorized access is also a risk as are theft and the destruction of business information. Following the spin-off of MAN IT Services GmbH we started in 2007 to harness the potential synergies from the spin-off. We also commenced the systematic introduction of service management processes according to ITIL (IT Infrastructure Library) in order to inject added transparency and reliability into the IT infrastructure.

MAN Internal Auditing regularly reviews the extent to which the risk avoidance measures are efficiently imple-

mented. The latest hardware and software ensure uninterrupted data availability and protection from unauthorized access. Modern data backup procedures abate any risk of total loss. Any potential Internet threat to the operability of our systems is combated by the latest and most efficient data security mechanisms.

### Employees

Our highly qualified specialists and managerial staff, who set technological standards with MAN products, represent an essential success ingredient. HR rewards are tied to the skills, international focus and innovative capabilities of our employees who are developing continuously improved products, services, and processes. The risks, on the other hand, surface whenever key positions cannot be staffed in line with our future requirements, especially within the context of globalization and growth. We therefore need a holistic attitude toward talent management. With the aid of a variety of personnel marketing efforts we have succeeded in tying to our group outstanding specialists and managers. Next year we will focus on positioning the MAN Group even more strongly as an attractive place for people to work. Such a reputation helps us in reverting worldwide to the human resources we require. Filling leadership vacancies from within our own ranks is another aspect of our efforts to promote our global growth strategy. As part of its internationalization strategy, the MAN Group will in future concentrate on promoting intercultural talents in the ongoing training of its specialists and managerial staff.

Our employees work around the world in their efforts to negotiate and conclude transactions on behalf of MAN. Any misconduct on their part may tarnish MAN's reputation while possibly eroding assets and profitability. These considerations prompted MAN back at the start of 2006 to adopt a Code of Conduct for its employees and to set up a Compliance Board. Additionally, two external ombudspersons were appointed in 2007 and entrusted with the role of examining and assessing, in particular, suggestions of possible misconduct by employees and, wherever such suspicions are founded, of forwarding the matter for further handling to MAN's Compliance Board. Steps were also intensified to train employees, especially in sales, in questions and procedures regarding compliance with existing laws. Compliance with the Code of Conduct is being monitored by Corporate Controlling and in 2007, this issue was a focal point in audit planning.

## Finances

The financial functions of the MAN Group and its operating companies are handled centrally by MAN AG.

One key task is to ensure cash supplies sufficient for short-term cash requirements, based on a 3-tier financial plan for the MAN Group. Liquidity and finance requirements are estimated as part of the triennial corporate plan, supplemented by rolling quarterly financial budgeting for the succeeding four quarters, and fine-tuned by estimating short-term cash requirements for three months.

When investing any liquidity reserves, we generally incur the risk that a bank's failure also results in the loss of invested funds. We therefore focus our surplus cash investments on conservative instruments, distributing them among several financial institutions (all well-reputed and of prime credit standing).

Varying exchange rates may impact on the prices for goods and services as well as on profit margins. The MAN Group generally hedges all firm customer contracts, its own foreign-currency purchase orders and other transactions against currency risks. Hedges are also contracted for budgeted or planned sales from standard-production business and high-probability forecasted transactions with customers. Despite these efforts we remain exposed to a certain residual risk if timing or amount of customer payments departs from budgeted sales.

Currency risks also emanate from the repercussions of exchange rate volatility on the purchasing power of our customers. Adverse forex trends may produce short-term losses in the markets concerned. In the long term, MAN endeavors to market, notwithstanding current exchange rates, competitively priced products and services through the ongoing enhancement of efficiency and productivity.

Adverse effects may also result from capital market rates. To absorb or contain such risks, we contract caps or floors, thus hedging, in particular, our customer financing arrangements which, as a rule, are made at fixed interest rates.

Financial derivatives and other hedges are exclusively contracted via MAN's Group Treasury and are subject to stringent internal controls. We confine our currency and interest rate risk management to the use of marketable instruments for the sole purpose of hedging current underlyings and, to some extent, forecasted transactions, never for any speculations.

The manufacture of our products consumes substantial quantities of commodities and other raw materials. Unfavorable commodity market price trends or escalator clauses in supplier contracts could ensue in risks that may adversely affect our operating profit. Where material, such commodity requirements are covered by appropriate futures.

Operating worldwide, the MAN Group is exposed to a plurality of financial market risks which we manage through organizational procedures and suitable financial instruments.

Major strategic risks may arise from changes in our shareholding portfolio. Examples include M&A where certain assumptions underlying purchase pricing fail to materialize after the acquisition, such as when potential synergies cannot be harnessed.

Moreover, M&A transactions may alter the MAN Group's financing structures, thus potentially entailing higher financing costs and/or a narrower financial scope.

For the envisaged combination with Scania, we held 105,873,036 shares equivalent to 13.23 percent of Scania AB's capital stock and 15.57 percent of the voting rights as of December 31, 2007. This stake's current market value is substantially above historical cost but is subject to stock market volatility and may entail the need for write-down. However, any such decline in fair value would not affect operating profit but be recognized in equity only (accumulated other comprehensive income).

Counterparty and country risks are reduced by carefully selecting our transactions and counterparts as well as through appropriate contract and payment terms and conditions. Any residual risks are classed according to debtor standing and largely shifted or assigned to banks or insurers, using suitable hedging tools. Guaranty bonds are provided centrally by or through MAN AG to

ensure that standardized and restrictive rules are observed. In this context, our attention is focused on the avoidance, wherever possible, of any unjustified enforcement of such bonds.

With a view to downsizing the accounting risks attaching to pension obligations, the MAN Group has externally funded parts of its pension liabilities and accruals by separating certain assets from its operating assets. These special pension plan assets are managed and administered by MAN Pensionsfonds AG (incorporated in 2007) and placed by external investment companies, based on the rules of a prudent investor. The fair value of such plan assets is nonetheless subject to the concomitances of interest rate and stock price swings.

#### **Assessment of MAN's risk situation**

On the basis of the risk management system set up by the MAN Group, the Executive Board notes that at the present time there are no perceivable risks that might have a material long-term adverse effect on the Group's asset and capital structure, financial position, or results of operations. The risk management system including the related organizational mechanisms enable the Executive Board to obtain early warning of any risk situation in order to take adequate action.

In itself, risk management is a lasting and never-ending corporate activity that, naturally, is continuously undergoing development. For MAN this means that in 2008, we will again repeatedly hone our systems to match them to changing parameters. High significance will again be assigned to financial risk management and with this in mind, the contractual and technological risks inherent to our business operations will again be scrutinized with great vigilance.

#### **Significant subsequent events**

The January 2008 swap of further class B for class A Scania shares raised our voting interest to 17.01 percent while our shareholding remained at an unchanged 13.23 percent.

During the past weeks, the MAN Group has gone through a corporate rating process: The two agencies, Standard & Poor's and Moody's, have rated MAN at A- and A3, respectively. These grades place MAN among the 10 top-rated DAX industrial corporations. The rating grades assigned further improve the MAN Group's access to the capital market and will add to MAN's financial flexibility and a more diversified finance structure.

No other subsequent events occurred that are of material significance for the MAN Group and might result in a different assessment of MAN. Business in early 2008 has endorsed the statements made in the *Prospects* chapter.

## Prospects

	2008
Order intake	→
Sales	↗
Operating profit	↗
ROS	→
ROCE	→

### Global economic trend

The general prospects for worldwide growth are jeopardized by the crisis on the financial markets and hence international economic growth in 2008 is currently forecasted at about 4 percent following the around 5 percent of 2007. What lies ahead will largely be influenced by how quickly the US economy succeeds in overcoming its property and financial market crises and to what extent the Asian and C&E growth markets manage at least in part to compensate for weak US demand.

Current forecasts envisage a GDP growth for the eurozone of just under 2 percent and for Germany around 1.5–2 percent following the 2.5 percent of 2007.

The prospects for the capital goods markets continue bright and demand for transport services and hence commercial vehicles is likely to remain robust. In other markets of significance to MAN, propulsion and energy, we also count on a continuation of strong demand. Over the period ahead it is especially important to be able to respond to economic trends with the necessary flexibility.

### Order intake and sales

Assuming that the global economy develops as forecasted in 2008 we expect the congenial capital goods market to continue. Given the already towering order backlog throughout the business areas and the related, in some cases very lengthy, delivery periods, we expect order intake in 2008 to match the prior year's volume.

Sales by the MAN Group in 2008 are expected to again advance, also due to the tall order backlog, by over 5 percent above the 2007 figure of €15.5 billion.

### Returns, operating profit

This year we expect another rise in the MAN Group's operating profit and an ROS on par with the strong perfor-

mance of 2007, with the biggest advance once more being reported by Commercial Vehicles, the other manufacturing areas raising their operating profit, in some cases appreciably. Both EAT (€1,225 million in 2007) and EpS (€8.24 in 2007) will decelerate compared with the operating profit due to the absence of 2007's nonrecurring income.

### Long-term growth strategy

We will press ahead along the path of growth and, parallel to rising revenue, further fine-tune the flexibility of our cost structures. This will enable us to actively respond to economic and demand fluctuations without jeopardizing our long-term growth goals. The growth regions for Commercial Vehicles are C&E Europe, the Middle East, and parts of Asia. Diesel Engines will vigorously expand worldwide its four-stroke diesel engine business, especially for stationary applications, while Turbo Machinery will again implement its growth plans for a sustainable high business volume. Industrial Services will benefit from focusing on its key activities and strong presence on international expansion markets.

Throughout the manufacturing areas an additional emphasis, besides extending new business, will be a significant strengthening of aftermarket business.

### Capital outlays, R&D, procurement

Fiscal 2007 saw major outlays directed at the ongoing re-vamping of production and, especially the planned growth at Commercial Vehicles, Turbo Machinery, and Diesel Engines. Capital expenditures in 2008 will match the year-earlier magnitude of €536 million (excluding the purchase of Scania stock), with emphasis on further rationalization and adapting capacities to growing business. The budgeted amounts are fully fundable from our cash flow from operating activities.

R&D is of elementary significance for MAN since we are required to address with repeatedly refined engineering solutions the challenges set by markets and legislators. At the same time, R&D is not an end in itself but rigorously aimed at generating competitive advantages for our customers. Given these considerations, our R&D efforts spotlight such issues as advancing our commercial vehicle and diesel engines for enhanced performance, fuel efficiency and emission abatement, developing our truck and bus models, and improving our turbo ma-

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chinery product range. In comparison to the €433 million in 2007, the R&D budget for 2008 will show a slight increase.

In order to sustain the success of our purchasing efforts and achieve further synergies, our common purchase-pooling strategy will be expanded in 2008 to systematically embrace further international supply sources.

**Cash flow**

In 2008 we will continue boosting our cash flow from operations by turning the unfaltering uptrend of our operating profit into net cash provided from operating activities, raising it to a level well above that of 2007 and supported by the groupwide working capital enhancement program. We will readjust our business process fine-tuning in order to further downscale the capital employed in inventories and receivables, the budgeted sales upthrust notwithstanding.

**Workforce**

The number of employees in the MAN Group will remain in the region of 2007 (around 55,000).

**Imponderabilities in Prospects**

The above forward-looking statements and information are based on our present expectations and certain assumptions. As a consequence, they harbor a series of risks and uncertainties. There are numerous factors, many of them beyond our control, that impact on our business operations and their results. These factors may mean that the actual performance and results shown by the MAN Group are widely at variance with the predictions stated.