

The engine company.



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DEUTZ AG

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- Convenience Translation -

Report of the Board of Management pursuant to section 221 (4) sentence 2 and section 186 (4) sentence 2 AktG on agenda item 11

Issuing convertible bonds, warrant-linked bonds, profit-sharing rights and/or income bonds (or combinations of these instruments) (together referred to as 'bonds') offers not only traditional ways of raising debt and equity capital but also allows the Company to make use of attractive alternative financing options in the capital market depending on market conditions. In particular, the authorisation to issue profit-dependent or profit-oriented instruments such as profit-sharing rights and income bonds expands the range of methods available to the Company to strengthen its funding by issuing this type of instrument, and thereby to lay and secure the foundations for its future performance. The Annual General Meeting will therefore propose that a new authorisation be granted for the issuing of convertible bonds, warrant-linked bonds, profit-sharing rights and/or income bonds (or combinations of these instruments).

The proposed new authorisation is intended to facilitate both an adjustment to current market practices and further flexibility. In total, issuances of bonds up to a cumulative principal of €500,000,000 shall be authorised, which entitle their holders to receive up to 60,430,890 no-par-value bearer shares of the Company.

Issuing convertible bonds, warrant-linked bonds, profit-sharing rights and/or income bonds (or combinations of these instruments) allows the Company to benefit from attractive conditions to raise debt capital, which – depending on the terms and conditions of the individual instruments – can be classified as equity or equity-like capital for rating and reporting purposes.

The conversion and/or option premiums earned as well as the equity classification strengthen the Company's capital base and thus open up attractive funding opportunities. In addition to granting conversion/option rights, possibilities to impose conversion/option exercise obligations and attach rights of the Company to sell shares to bond holders (or combinations of these instruments) are being envisaged as further opportunities to expand the scope for the structuring of such financing instruments. The authorisation furthermore offers the Company flexibility to issue bonds directly or through other Group companies. Bond issues may be denominated in euros or in any other legal tender of an OECD member state and may have a limited or indefinite maturity term.

Existing shareholders must generally be given pre-emption rights. In order to simplify the process, the authorisation shall also include the possibility to transfer bonds to banks or companies within the meaning of section 186 (5) sentence 1 AktG subject to an undertaking by the banks or companies to offer the shares to existing shareholders according to their pre-emption rights (indirect pre-emption right). However, an exclusion of such pre-emption rights shall be permitted under the following circumstances.

Where convertible bonds and/or warrant-linked bonds (or profit-sharing rights or income bonds with attached conversion/option rights, an attached conversion obligation, or an attached right of the Company to sell shares) are issued, the Board of Management is to be provided with an authorisation to disapply the pre-emption rights of existing shareholders subject to the consent of the Supervisory Board, provided these convertible bonds and/or warrant-linked bonds (or profit-sharing rights or income bonds with attached conversion/option rights, an attached conversion

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Sitz und Registergericht / Domicile and Register Court: Köln / Cologne

Nr. des Handelsregisters / Commercial Register No.: 42 HRB 281

Vorsitzender des Aufsichtsrates/Chairman of the Supervisory Board: Hans-Georg Härter

Vorstand / Board of Management:

Dr. Frank Hiller (Vorsitz / Chairman),

Dr. Margarete Haase, Dr. Andreas Strecker, Michael Wellenzohn

obligation, or an attached right of the Company to sell shares) are issued against cash payment and the issue price is not significantly lower than the theoretical market value of the convertible bonds/warrant-linked bonds (or profit-sharing rights or income bonds with attached conversion/option rights, an attached conversion obligation, or an attached right of the Company to sell shares) as determined using recognised financial calculation methods. The notional amount of the shares (to be issued upon conversion of the bonds issued in accordance with this authorisation) as a proportion of the Company's issued capital must not exceed the lower value of 10 per cent of the issued capital at the time when this authorisation comes into effect or 10 per cent of the issued capital at the point in time when this authorisation is utilised. Shares issued or sold in direct or indirect application of section 186 (3) sentence 4 AktG during the period of validity of this authorisation, up to the point in time when this authorisation is utilised, must be included in the calculation of the aforementioned 10 per cent limit. Shares to be issued or granted upon conversion of bonds issued during the period of validity of this authorisation on the basis of the utilisation of another authorisation with the disapplication of pre-emption rights in accordance with this provision must also be included in the calculation of the aforementioned 10 per cent limit.

The inclusion in the calculation of this limit ensures that convertible bonds and/or warrant-linked bonds (or profit-sharing rights or income bonds with attached conversion/option rights, an attached conversion obligation, or an attached right of the Company to sell shares) are not issued if this would lead to a disapplication of pre-emption rights for shares worth more than 10 per cent of the Company's issued capital in direct or indirect application of section 186 (3) sentence 4 AktG without a specific objective reason. This more far-reaching restriction is stipulated in the interest of shareholders who seek to maintain their proportionate ownership stake when corporate actions such as capital increases occur. In the event that pre-emption rights are disappplied, the issue price for the bonds must not be set significantly below the market price due to the direct or indirect applicability of section 186 (3) sentence 4 AktG. This provision is intended to protect existing shareholders against a dilution of their holdings. The prohibition of issuing a bond at a price significantly below the estimated market value – which is envisaged as part of the authorisation – would effectively reduce the value of a pre-emption right to near zero. In order to ensure that this bond issuance requirement is met, the price at which the bonds are issued must not be significantly lower than the theoretical market value of the convertible bonds/warrant-linked bonds (or profit-sharing rights or income bonds with attached conversion/option rights, an attached conversion obligation, or an attached right of the Company to sell shares) as determined using recognised financial calculation methods. Subject to the above, shareholders will be protected against a dilution of their shareholdings and will not suffer any economic disadvantage as a result of a disapplication of their pre-emption rights. Shareholders who want to maintain their percentage stake in the Company's issued capital or who want to acquire bonds in proportion to their shareholdings, can do so through additional purchases in the market.

In the event that profit-sharing rights or income bonds are intended to be issued without conversion/option rights or conversion/option exercise obligations, the Board of Management is authorised – subject to the consent of the Supervisory Board – to disapply the pre-emption rights of existing shareholders, provided the profit-sharing rights or income bonds are structured in a form similar to bonds, i.e. they do not confer any rights of membership in the Company, they grant no share of liquidation proceeds and the amount of the coupon is not calculated on the basis of net income, accumulated income or the dividend. In addition, the coupon and the issue price of the profit-sharing rights or income bonds must reflect the prevailing market terms for comparable instruments at the time of issue. If the specified preconditions are satisfied, shareholders will not suffer any disadvantage from the disapplication of pre-emption rights because the profit-sharing rights or income bonds do not confer any rights of membership in the Company, nor do they grant the holders any share in the proceeds of liquidation or in the profits of the Company. Although the coupon can be linked to the availability of net income, accumulated income or a dividend, the Board of Management would not be permitted to include any arrangement in which higher net income, higher accumulated income or a higher dividend would lead to a higher coupon. The issue of profit-sharing rights or income bonds therefore does not change or dilute shareholders' voting rights, investment in the Company or share of profits. In addition, in this case, the pre-emption rights have little value because of the arm's-length terms and conditions of issue that are mandatory for this type of disapplication of pre-emption rights.

The aforementioned provisions for a disapplication of pre-emption rights provide the Company with the flexibility it needs to benefit from favourable capital market conditions at short notice and enable it to take advantage of low interest rates

and/or strong demand by issuing the previously specified types of financial instruments at short notice and in a flexible manner. The decisive factor here is that unlike in the case of bond issuances with pre-emption rights, the issue price does not need to be determined until immediately before the placement, which avoids increased price risk during the subscription period and makes it possible to maximise the issue proceeds in the interest of all shareholders. The disapplication of pre-emption rights also eliminates the need for an advance subscription period for shareholders, which has a positive impact on the cost of the capital increase and the placement risk. An issue without pre-emption rights also offers the possibility to reduce not only the placement risk but also the safety margin which would otherwise be required and to reduce the cost of the capital increase by the corresponding amount for the benefit of the Company and its shareholders.

The Board of Management is furthermore authorised, subject to the consent of the Supervisory Board, to exclude fractional amounts from the pre-emption right. Fractional amounts can result from the issue volume and the determination of a reasonable subscription ratio. In such cases, disapplying pre-emption rights can simplify the issue process. Available fractional amounts that are excluded from shareholders' pre-emption rights are either sold in the market or otherwise used to the maximum benefit for the Company.

In addition, the Board of Management is to be authorised, subject to the consent of the Supervisory Board, to disapply the pre-emption rights of shareholders in order to compensate holders/creditors of conversion and/or option rights, or holders/creditors of bonds with attached conversion/option exercise obligations or an attached right of the Company to sell shares, for dilution effects by granting them pre-emption rights equivalent to the entitlement they would have if they exercised their conversion/option rights, fulfilled their conversion/option exercise obligation or took receipt of shares delivered by the Company under its right to sell. If the authorisation is utilised, this provision allows the Board of Management to avoid the need to reduce the option exercise/bond conversion price for the holders of existing bonds with conversion/option rights as specified in the applicable terms and conditions.

To improve flexibility, the applicable terms and conditions may also stipulate that the Company is entitled to settle amounts owed to holders of conversion/option rights in cash instead of delivering Company shares. The use of a combination of both types of performance of the Company's obligations should also be permitted. It may furthermore be stipulated that the number of shares received upon exercising the conversion/option rights or complying with conversion/option exercise obligations, or upon taking receipt of shares in accordance with the Company's right to sell, may be variable and/or that the conversion/option exercise price may be adjusted during the term of maturity within a certain price range (to be specified by the Board of Management) depending on the performance of the share price or on grounds of dilution protection provisions.

Even when the conversion ratio and/or the conversion/option exercise price are variable, the conversion/option exercise price to be determined must not be lower than 80 per cent of the Company's share price as quoted on XETRA (or a comparable successor system). The calculation is based on the average closing price of the last ten trading days before the day on which the Board of Management adopts the resolution for the issuance of the bonds in question; however, if subscription rights are traded, the calculation will be based on the days during which the rights are traded, excluding the last two trading days. If bonds have an attached conversion/option exercise obligation or an attached right of the Company to sell shares, the conversion/option exercise price can be either at or above the aforementioned minimum price or equivalent to the average volume-weighted trading price of the Company's stock based on a minimum of three trading days on XETRA (or a comparable successor system) immediately before the determination of the conversion/option exercise price, in accordance with the applicable terms and conditions. This applies even if this average trading price is below the aforementioned minimum price threshold (80 per cent).

Lastly, it is intended that there be an option for the Board of Management to disapply the pre-emption rights of shareholders to the bonds – subject to the consent of the Supervisory Board – if the bonds are issued against non-cash payments or contributions, especially in the context of company mergers or (direct or indirect) acquisitions of entities, parts of entities, equity investments in entities, or other assets, or entitlements to acquire assets, including the acquisition of outstanding debts against the Company or its group companies. The above applies with the proviso that

the value of the non-cash contribution must be appropriate in relation to the value of the bonds. For convertible bonds and/or warrant-linked bonds (or profit-sharing rights or income bonds with attached conversion/option rights, an attached conversion/option exercise obligation, or an attached right of the Company to sell shares), the theoretical market value as determined using recognised financial calculation methods applies. The issue of bonds for a non-cash contribution offers the possibility of using bonds as an acquisition currency in eligible individual cases involving acquisitions of entities, parts of entities or equity investments in entities. This creates flexibility to seize opportunities for acquisitions of entities, parts of entities or equity investments in entities using means other than authorised capital, in order to conserve liquidity. In specific cases, this type of approach may also offer advantages with regard to an optimisation of the financing structure.

Upon adoption of the authorisation, the total shares issued subject to a disapplication of pre-emption rights must not exceed 20 per cent of the issued capital – neither at the time this authorisation becomes effective, nor or at the time this authorisation is utilised, if the latter value is lower. Included in the calculation of this 20 per cent limit are (I) shares issued or sold during the period of validity of this authorisation based on the use of another authorisation in disapplication of the pre-emption rights or (II) shares issued upon conversion/exercise of convertible bonds or warrant-linked bonds issued during the period of validity of this authorisation based on the use of another authorisation in disapplication of the pre-emption rights. Under the provisions of the above authorisation, the possibility of disapplying shareholders' pre-emption rights is already highly restricted; this additional restriction – which goes beyond regular statutory limitations – is designed to reduce the impact on shareholders to a minimum.

The proposed conditional capital serves to satisfy conversion/option rights, conversion/option exercise obligations or rights of the issuer to sell shares that are attached to convertible bonds and/or warrant-linked bonds (or profit-sharing rights or income bonds with attached conversion/option rights, an attached conversion/option exercise obligation, or an attached right of the issuer to sell shares) issued for cash, unless treasury shares or other means are used to satisfy such rights and/or obligations. However, the proposed conditional capital does not serve to satisfy conversion/option rights, conversion/option exercise obligations or rights of the issuer to sell shares that are attached to convertible bonds and/or warrant-linked bonds (or profit-sharing rights or income bonds with attached conversion/option rights, an attached conversion/option exercise obligation, or an attached right of the issuer to sell shares) which were issued in exchange for a non-cash contribution.

Cologne, 6 March 2018

The Board of Management of DEUTZ AG

Dr. Frank Hiller

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Dr. Andreas Strecker