

SEPARATE COMBINED NON-FINANCIAL REPORT

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Non-financial
report

ABOUT THIS NON-FINANCIAL REPORT

In accordance with section 315b et seq. and section 289b et seq. of the German Commercial Code (HGB), DEUTZ will publish a separate combined non-financial report ('non-financial report') for each financial year from 2017. The content of this report covers both the DEUTZ Group and the parent company DEUTZ AG and is issued as a separate report. Unless otherwise indicated, all disclosures pertain to the Group ('DEUTZ') as a whole. Disclosures that relate only to DEUTZ AG are labelled accordingly. The non-financial report summarises the key issues pertaining to the following areas of focus: environmental matters, treatment of employees, social responsibility and measures to combat corruption and bribery. Corporate social responsibility at DEUTZ AG is not subject to reporting requirements according to the materiality assessment. However, it is also reported on in this non-financial report so as to provide a more rounded picture of the Company. Human rights are not reported on as they are not relevant to the Company's situation and the resultant risks are not deemed to be material. Reference is made at the relevant points to further information contained in other parts of this annual report. References to disclosures outside the scope of the combined group management report or consolidated financial statements do not form part of the non-financial report.

This non-financial report has been produced with reference to the framework provided by the German Sustainability Code (DNK). It covers criteria 1, 3 and 6 of the DNK.

The non-financial report has been voluntarily submitted for a review with limited assurance pursuant to ISAE 3000 (Revised).

Using the net method, we identified no material risks in relation to our own business activity or to our business relationships, products and services pursuant to sections 289c (3) nos. 3 and 4 HGB. All other information on opportunities and risks are presented in the opportunity and risk report on page 59 et seq. of the combined management report.

BUSINESS MODEL

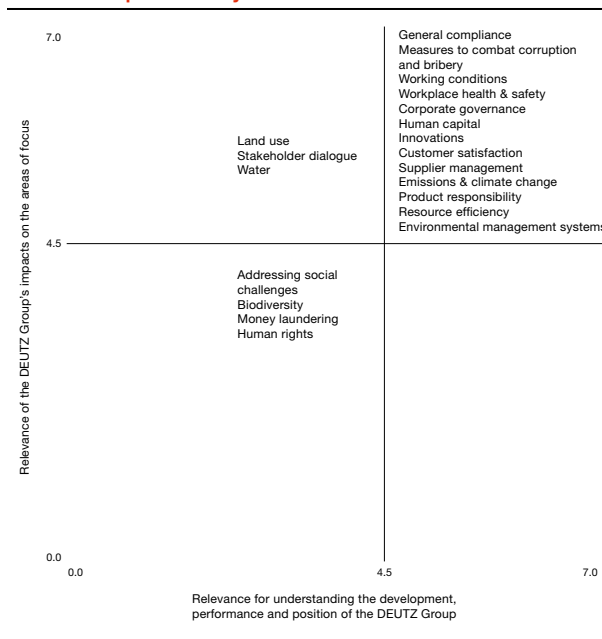
DEUTZ is one of the world's leading engine manufacturers. We are an independent producer of diesel and gas engines in the power output range of 19 kW to 620 kW for on-highway and off-highway applications. For further information on the business model, see page 32 et seq. in the combined management report of this annual report.

MATERIALITY ASSESSMENT

Last year, in preparation for the non-financial report, we set up an internal process to identify the key topics under the Corporate Social Responsibility Directive Implementation Act (CSR-RUG) pursuant to sections 315b et seq. and 289b et seq. HGB. First, we drew up a comprehensive list of potential key topics based on research into competitors, frameworks and sustainability ratings. This list was then analysed. We declared those topics to be material that were particularly relevant both in terms of their impact on the aforementioned areas of focus and in understanding DEUTZ's development, performance and position. To get to this stage, we first conducted a survey among internal contacts. The results of this survey were then discussed in a workshop before undergoing a final assessment by the Board of Management.

The materiality matrix encompasses the dimensions 'Relevance of the DEUTZ Group's impacts on the areas of focus' and 'Relevance for understanding the development, performance and position of the DEUTZ Group'.

DEUTZ Group: Materiality matrix



The following key issues were identified for each area of focus:

- Environmental matters: environmental management systems, resource efficiency, air and climate
- Treatment of employees: working conditions, health, safety and human capital
- Social responsibility: product responsibility
- Compliance: general compliance, measures to combat corruption and bribery, corporate governance
- Overarching topics: customer satisfaction, innovation, supplier management

In the following section, we report on the 13 key topics on the basis of the criteria specified under CSR-RUG.

The materiality assessment revealed that the subject of human rights has little relevance in terms of impacts on the areas of focus and in terms of understanding the development, performance and position of our Company because our compliance with applicable domestic and international laws and collectively agreed working conditions means that human rights infringements can essentially be ruled out. Furthermore, it emerged that there were no material risks with regard to our business activities, to our business relationships, products and services, and to the non-financial areas.

ENVIRONMENTAL MATTERS

Key environmental concerns for DEUTZ are environmental management systems, resource efficiency and climate. These are explained below:

Environmental matters form part of the integrated management system DEUTZ AG's integrated management system, which covers environmental protection, energy and quality, meets the requirements of the DIN EN ISO 14001, 50001 and 9001 (version 2015) standards that are currently applicable. This conformity was reviewed and confirmed by the external auditors from TÜV Rheinland Cert GmbH.

The continuous improvement process, which was introduced together with the integrated management system, helps DEUTZ AG to continually review the targets that it has set itself. This is done as part of the management review conducted by the Company's most senior level of management (Chairman of the Board of Management).

The senior management team is involved in the processes through the environmental management system. It assesses the measures as part of the management review and decides on further activities.

Continuous reduction of emissions The DEUTZ Group has set itself the target of reducing CO₂ emissions per manufactured engine by at least 2 per cent every year. Data is also collected on the pollutants dust, nitrogen oxide and benzene; here too we are striving to continually reduce the level of these emissions per unit of production.

Regular audits of energy use and environmental impact DEUTZ AG has set up a working group to review its compliance with important product-related laws and regulations. The group conducts investigations into the supply chain, part of which includes auditing suppliers. In addition, internal environmental and energy audits take place five or six times a year as set out in the integrated management handbook. These are carried out in accordance with a fixed schedule and help to ensure that the examined processes comply with statutory norms and customer specifications. Most of the work is done by an external service provider that specialises in environmental and energy matters. The aim is to provide an assurance of legal conformity and to reduce commercial risk.

Reducing energy consumption In early 2017, DEUTZ AG's energy management system was recertified under ISO 50001 without any nonconformities. We continue to work on further developing this system in a continuous improvement process at strategic and operational level.

Ongoing training for trainees/apprentices and production staff as well as optimisation of the measurement systems form the basis for identifying and successfully implementing measures to improve energy-related performance.

DEUTZ AG has adopted a variety of measures aimed at reducing primary and secondary energy consumption. It has achieved most energy savings by optimising its network of sites.

Despite a sharp rise in production volume, the amount of energy used throughout the DEUTZ Group was reduced in 2017, by nearly 50 per cent in the case of district heating. Electricity consumption rose slightly for production-related reasons. Consumption of LPG was also higher due to production-related reasons, as this is being used to test the new gas engine.

DEUTZ Group: Energy consumption in our plants¹⁾

MWh	2017	2016
Electricity	84,605	79,837
Natural gas	35,277	35,795
District heating	12,223	23,017
Heating oil ²⁾	3,653	4,440
Diesel fuel ³⁾	19,218	20,144
LPG ⁴⁾	421	310
Total	155,397	163,543

¹⁾ Plants in the DEUTZ Group, excluding joint ventures.

²⁾ At 10.5 kWh/litre (mean).

³⁾ At 9.85 kWh/litre (mean).

⁴⁾ At 12.8 kWh/kg (mean).

Minimising CO₂ emissions through engineering A number of different measures are in place to achieve the aim of reducing CO₂ emissions. At DEUTZ itself, emissions are primarily produced by the engine test bays used in development and production. The state-of-the-art, high-performance exhaust gas aftertreatment system used in the production test bays at the German sites ensures that DEUTZ remains within permitted limits and, in some cases, is well below them. DEUTZ AG is also introducing cold testing, a system in which comprehensive pre-start diagnostics are run on the engine functions. Some engines will therefore not have to undergo test runs for minutes at a time. This will conserve fuel and substantially reduce engine emissions. The test method, which offers compelling economic and ecological advantages, was purchased in the reporting year. The project will commence in the second half of 2018. Plans for the forthcoming optimisation of material flows for engine series with capacities of less than 4 litres include ramping up the proportion of cold tests of sub 4 litre engines at the Porz plant to more than 50 per cent by 2020. The cold testing has the potential to dramatically reduce factory-related emissions, which at DEUTZ AG are mainly released from the consumption of fossil fuels in test bays.

Reducing CO₂ emissions through sustainability The optimisation of our network of sites, which was completed last year, is also playing a key role in resource efficiency. The clearing of the Cologne-Deutz premises at the beginning of 2017, with the site being sold and a new shaft centre built in Cologne-Porz, has freed up around 160,000 square metres of industrial space in a central location in Cologne. The area can be used for housing, commercial premises, schools and parks. As the Company's utilisation of space is now much more efficient and old infrastructure has been disposed of, the energy efficiency of the network of sites has improved and the emissions they produce have been markedly reduced. And in mid-2017, the relocation of production from the Übersee plant on Lake Chiemsee to the Ulm plant was successfully completed – and it has had a positive impact in terms of both resource efficiency and emissions.

When designing its workspaces, DEUTZ AG takes sustainability aspects into account as soon as planning starts. In our new shaft centre at the Porz plant, the supply of coolant has been centralised and the flow of materials optimised from an economic and ecological perspective. This has reduced the throughput time of camshafts by around 75 per cent and of crankshafts by more than 50 per cent.

Reducing CO₂ emissions through technology and innovative products DEUTZ is further minimising emissions by introducing more stringent emissions standards for diesel engines and by optimising its products. In 2017, DEUTZ became the world's first engine manufacturer to be given a certificate for the Stage V emissions standard, which comes into effect in the EU in 2019. Numerous engine models in the 3.6 litre to 7.8 litre power output range have now been certified. The Company has therefore met what will be the world's strictest emissions standards ahead of time and is actively contributing to climate protection and improvements in air quality. DEUTZ engines offer high performance, a small installation space and, at the same time, reduced fuel consumption. This is to the benefit both of our customers and of the environment as CO₂ emissions are directly related to fuel consumption.

In recent years, Torqeedo has won multiple accolades for its innovative products and environmental credentials. For example, it received the Top Product 2016 award from US magazine Boating Industry for its Cruise 10.0 R outboard motor as a "green and quiet alternative for commercial and recreational users".

DEUTZ's Xchange product programme also plays its part in improving sustainability as having used engines professionally refurbished gives them an extended lease of life.

Significant reduction in CO₂ emissions The DEUTZ Group's primary environmental target is to reduce CO₂ emissions per engine manufactured by at least 2 per cent every year, and it did significantly better than this in 2017, cutting emissions by 18.5 per cent. This is mainly attributable to the optimisation of the number of sites in Germany, the construction of a state-of-the-art, energy-efficient shaft centre at the Cologne-Porz plant, the savings in diesel fuels in development and the greatly expanded production programme. The overall impact will soon be greatly enhanced by the introduction of cold testing, which reduces some of the test runs that engines have to undergo.

The reduction in nitrogen oxide, dust and benzene emissions was mainly achieved by cutting fuel consumption in production areas at the Cologne-Porz plant⁵⁾.

⁵⁾ Not checked by the external auditor.

DEUTZ Group: Annual CO₂e emissions in our plants¹⁾

Tonnes	2017	2016 ²⁾
CO ₂ e emissions (Scope 1)	13,239	13,748
CO ₂ e emissions (Scope 2)	38,012	39,325
CO ₂ e emissions (Scope 3)	9,217	7,722
CO₂e emissions (total)	60,469	60,795

Scope 1: CO₂e emissions from diesel, natural gas, LPG and heating oil caused by combustion in our own facilities.

Scope 2: CO₂e emissions relating to purchased energy (e.g. electricity, district heating).

Scope 3: CO₂e emissions from air miles and CO₂e emissions produced by the treatment of purchased water.

¹⁾ CO₂e = carbon dioxide equivalents.

CO₂e emissions in plants in the DEUTZ Group, excluding joint ventures. CO₂e figures are reported in accordance with the Greenhouse Gas Protocol and are determined by multiplying the energy consumed by the relevant emissions factor. Prior-year figures have been adjusted in line with the new calculation method.

²⁾ CO₂e figures for 2016 have not been checked by the external auditor.

DEUTZ Group: Emissions per engine in our plants^{1),2)}

Emissions per engine	2017	2016
CO ₂ e (kg)	353	433
Nitrogen oxide (kg)	0.18	0.22
Dust (g)	2.25	2.70
Benzene (mg)	76.8	84.8

¹⁾ CO₂e = carbon dioxide equivalents.

CO₂e emissions in plants in the DEUTZ Group, excluding joint ventures. The other data relates only to German plants. CO₂e figures are reported in accordance with the Greenhouse Gas Protocol. Prior-year figures have been adjusted in line with the new calculation method. The 'emissions per engine' figure is calculated by dividing total emissions by the number of engines made. CO₂e reporting includes all scopes.

²⁾ CO₂e figures for 2016 and all figures for dust, nitrogen oxide and benzene have not been checked by the external auditor.

TREATMENT OF EMPLOYEES

Because of the materiality of DEUTZ AG as the executive parent company, there is currently no overarching system that monitors the treatment of employees in the Group as a whole. Our reporting therefore focuses on the treatment of employees at DEUTZ AG. The subsidiaries are managed on an individual basis on account of different local circumstances. The local senior management teams regularly report on relevant matters to DEUTZ AG's management.

HUMAN CAPITAL

DEUTZ AG has formulated the following goals in this area:

- Provide foundation training for specific specialist positions
- Fill vacancies for specialist/management roles with qualified internal candidates
- Develop the workforce at all levels

Due to the specific labour market situation in Extremadura, DEUTZ Spain is planning to open its own business school in 2018 so that it can fundamentally improve the skills of its employees.

Strong focus on training and development Measures in place at DEUTZ AG include individual development plans, training in technical and IT professions, career guidance for young people, student programmes, support for part-time education (e.g. technical training and master's degrees), inhouse training courses and training courses run in collaboration with external providers.

DEUTZ AG has long been committed to providing vocational training in professions recognised by the Chambers of Industry and Commerce (IHK). In Germany, our apprentices can train in careers ranging from electronics, mechatronics and metalworking to warehouse logistics and business administration. Last year, 29 young men and women began a vocational apprenticeship at our Company; as at the end of 2017, a total of 51 trainees were employed at our Cologne site, 19 at the DEUTZ plant in Ulm and six at the components plant in Herschbach. Our training centre in Cologne also provides vocational training, on a part-time and full-time basis, for apprentices from 21 other companies.

In 2017, a total of 206 interns were employed at DEUTZ AG, of whom 35 wrote their bachelor or master's dissertations while at the Company. A total of 34 students spent a practical semester with us.

Our management trainees followed a special management training programme (six participants in 2017). Our professional development programme comprised 362 seminars (inhouse training and one-off external courses), attended by 1,897 participants. A further 29 specialist employees participated in skills training provided by the employers' liability insurance association. The existing collaboration with the training provider macils.management-centrum GmbH for the implementation of specific workshops was successfully continued.

Some employees also took part in a cross-mentoring programme for female management trainees. We offer career days for young people and encourage women to enter industrial/technical occupations.

In 2017, the HR management system at DEUTZ Spain underwent thorough analysis, with 300 employees taking part in SWOT workshops in order to examine the strengths and weaknesses of the current set-up. Workspaces were assessed and an employee appraisal system was developed. An HR programme for 2017 to 2021 was defined that highlights the cause-and-effect relationships of the various approaches in HR management. These were used to create an HR dashboard featuring a hierarchical system of KPIs that gauge the efficiency of the various measures.

DEUTZ Business School in Spain The more technology progresses towards Industry 4.0, the more highly skilled employees will have to be. Because of this and because of the specific labour market situation in Extremadura, approval was given in 2017 for a project that will culminate in the opening of the DEUTZ Business School® with its four areas of focus: strengthening dual vocational training, offering university courses in lean management, running language courses with official certification and providing ongoing training in the form of conferences and seminars.

At each site, approval processes ensure that the senior management team is closely involved in all proposed measures.

DEUTZ AG evaluates its service providers and trainers by conducting satisfaction surveys among the participants.

At DEUTZ Spain, procedures are in place for the structuring of internships (students undergoing practical training, dual vocational training and HR programme). In addition, the training process is monitored by both the company committee and the quality management system.

DEUTZ trainees and training score highly The achievements of trainees and the DEUTZ training centre in Cologne are regularly recognised, and 2017 was no exception. Indeed last year, DEUTZ's training was right up there with the very best in Germany, with the Association of German Chambers of Industry and Commerce (DIHK) presenting an award to a DEUTZ trainee in December 2017 in Berlin for achieving the best result in the metal technology specialist exam. And for the seventh year in a row, the DEUTZ training centre was recognised by the Chambers of Industry and Commerce for its outstanding achievements in vocational training. Further DEUTZ apprentices were awarded 'best performer' certificates at national, regional and federal state level.

DEUTZ AG takes on apprentices after they have completed their training and recruits graduates who worked at DEUTZ while they were studying. Technical and *meister* grade positions are generally filled by internal candidates. We have also improved skills training for employees, widened the reach of the 'employees train employees' scheme and extended the training courses offered by DEUTZ AG.

At DEUTZ AG, the ratio of trainees to total employees stood at 2.5 per cent in 2017. All apprentices and trainees who passed the final examination were given a permanent employment contract. Currently, around 5 per cent of apprentices at DEUTZ are female.

The high-potential programme at DEUTZ Spain has proven to be a success, with 75 per cent of participants having now been taken on. Its success prompted the launch of a second programme in September 2017.

WORKING CONDITIONS

Compliance with laws and agreements DEUTZ acts in accordance with the collective pay agreements, tax laws, social insurance guidelines and rules on variable remuneration that are currently applicable. Our corporate culture is built on respect for different cultural values and supports equal opportunities for all employees, regardless of gender, age, ethnicity, sexual orientation or disability. Our management culture helps managers and employees to work together efficiently and from a position of trust. DEUTZ strives for fair and appropriate remuneration for all employees.

DEUTZ Spain specified comparable targets for working conditions in its HR strategy plan 2017–2021 and was the first company in Spain to introduce a compliance system with consequences under criminal law. Certification to the UNE19601 standard ensures that the statutory working conditions are also being complied with.

Employee communications and consultation At all locations, the senior management team is closely involved in the implementation of measures. DEUTZ AG and DEUTZ Spain also follow the principle of codetermination, which gives workers a voice in company decisions. All employees in Germany are subject to the collective pay agreement of the metalworking and electrical engineering industry. Employees are represented by a works council at each site. There is also a General Works Council with responsibility for matters concerning multiple sites. An elected Senior Staff Committee represents the interests of senior managers at DEUTZ AG. Both the works council and senior managers appoint representatives to the Company's Supervisory Board. Employee rights are safeguarded by adherence to the Company's own corporate and management principles, collective bargaining agreements and the corresponding agreements with the employee representative bodies. The myDEUTZ staff magazine, noticeboards and ad-hoc announcements keep employees up to date with what is going on in the Company. Moreover, any employee can attend one of the local works meetings and have their voice heard if they feel this is necessary.

Appropriate measures are in place to reintegrate members of staff at DEUTZ AG who have been on long-term sick leave.

Childcare facilities Employees of DEUTZ AG in Cologne can have children under the age of three looked after at the 'DEUTZlinge' day care centre, which makes it easier for them to return to their day-to-day work after parental leave. We also offer tailored or flexible working hours for employees who provide care or assistance to an elderly or disabled family member. In addition, all employees covered by collective pay agreements receive a share of the Company's profits in accordance with a system agreed with the works council.

Promoting equality DEUTZ Corporation closely monitors best practice in the US and builds on this to generate improvements and recommendations. The subsidiary has implemented an affirmative action plan in line with the regulations of the U.S. Equal Employment Opportunity Commission (EEOC). This sets out how discrimination on the grounds of skin colour, gender and other factors can be avoided when recruiting and promoting staff and in the general working environment.

Codetermination in action On the basis of the applicable collective pay agreements and laws, the employee representatives at DEUTZ AG and DEUTZ Spain are closely involved in the processes and in any action taken that concerns the treatment of employees (recruitment, remuneration, reassignment, development, dismissal).

At DEUTZ Spain, there are job profiles and salary bands that comply with the collective pay agreements. A compliance system safeguards equal opportunities in the selection of personnel.

DEUTZ Corporation makes efforts to ensure that its pay is fair and appropriate. Regular audits are carried out to check that this is the case. Mechanisms have been put in place for employees to report workplace bullying and inappropriate behaviour. A handbook describes relevant countermeasures. An equal opportunities audit is carried out once a year and the results are reported to the regulatory authority (EEOC).

Key figures bear out the effectiveness of measures Average staff turnover at DEUTZ AG is very low, at 1 per cent.

In 2017, three children were looked after at the new day care centre at the Cologne-Porz site. In an employee survey, 89 per cent were in favour of company childcare provision.

More than 70 new fathers at DEUTZ AG made use of the option to take parental leave.

HEALTH AND SAFETY

Reducing accident frequency A groupwide accident frequency rate of less than 10 is a target specified by DEUTZ AG in the area of health and safety. Accident frequency is defined as the number of reportable accidents in relation to hours worked.

Various measures helping to achieve this target At DEUTZ AG, these include ergonomic improvements, flu vaccinations, medical check-ups, sports events, accident analyses, health and safety training, and campaigns run in conjunction with health insurance schemes. Managers in production, development and assembly also followed a multi-part training programme in health-oriented leadership.

At DEUTZ Spain, medical check-ups are offered and workspaces are ergonomically optimised. Noise, vibrations and levels of chemical pollutants are also measured and risk assessments carried out.

At DEUTZ Corporation, all aspects of workplace safety management (accident analysis, prevention, etc.) have been outsourced to an external service provider.

At all locations, the senior management team is closely involved in the implementation of health and safety measures through management reviews. Stakeholders such as external service providers and health insurance schemes are also involved.

Alignment with overarching standards In order to assess safety and the protection of its employees' health, DEUTZ AG and DEUTZ Spain have put in place a system for checking workspaces. IMS (Integrated Management System) has been introduced in Germany and OHSAS in Spain. The primary areas of focus are health, safety and the environment. The frequency with which these internal inspections take place depends on the extent and type of the risk presented by the machinery or workspace. Teams made up of experts from various disciplines carry out these workplace safety inspections in areas such as assembly and production. Any issues that are identified are documented in action plans that specify a timeframe for remedial measures to be taken.

To minimise safety risks, DEUTZ AG has introduced an internal approval process for hazardous substances and for the procurement of plant, machinery and equipment. The service providers that we engage are given detailed information about site-specific risks.

The accident frequency rate at the DEUTZ Group was 13.9¹⁾ in the year under review. Despite the improvement that can be seen in all plants, DEUTZ AG fell short of its target of an accident frequency rate of below 10 (2017: 15.1; 2016: 22.2²⁾).

¹⁾ Plants in the DEUTZ Group, excluding joint ventures.

²⁾ Prior-year figures not checked by the external auditor.

SOCIAL RESPONSIBILITY

Product responsibility is a cornerstone of our commitment to act as a good corporate citizen.

PRODUCT RESPONSIBILITY

Because of the materiality of DEUTZ AG as the executive parent and production company, there is currently no overarching system that monitors product responsibility in the Group as a whole. Our reporting therefore focuses on product responsibility at DEUTZ AG. The local senior management teams regularly report on relevant matters to DEUTZ AG's management.

Product-related KPIs at DEUTZ AG relate to the following metrics:

- Targets concerning durability
- Targets concerning delivery quality (zero-hour defects)
- Targets concerning field quality (field defects)
- Targets concerning the speed at which defects are fixed
- Delivery reliability of engines
- Full compliance with machinery directives such as RoHS and REACH
- Certification to EU Stage V, the latest exhaust emissions standard

DEUTZ AG carries out audits on the basis of ISO 9001, ISO 14001, ISO 50001, VDA 6.3, the German Occupational Safety Act and REACH. DEUTZ Spain carries out audits in line with ISO 9001 and IATF 16949 and Torqeedo to ISO 9001.

Foundation laid for high quality At DEUTZ AG, consistent high quality is maintained by means of certification to ISO 9001. A weekly quality report featuring KPIs keeps the senior management team up to date with the current status of target attainment. Where shortfalls are identified, an action plan is drawn up at quality meetings and subsequently implemented within the Company in order to meet the targets.

Product-related targets, with a particular focus on durability and field quality, are taken into account early on in the product development process when the product specifications are defined.

Initial successes documented DEUTZ AG plans to further raise the level of customer satisfaction by reducing zero-hour defects. It has also increased the speed at which field problems are resolved and successfully commenced certification of its product range in accordance with EU Stage V.

Every year, Torqeedo launches new products with the aim of continually improving its market position.

For information on Torqeedo's new products, patents and awards, see the Innovations section on page 76 et seq.

COMPLIANCE

General compliance, corporate governance and the fight against corruption and bribery play an important role in compliance. As measures to combat bribery and corruption form an integral part of the general compliance management system, these key issues are explained together.

GENERAL COMPLIANCE AND MEASURES TO COMBAT BRIBERY AND CORRUPTION

The prime objective of the groupwide compliance management system is to prevent violations of applicable laws and internal policies. To this end, employees are given help in familiarising themselves with the relevant laws and policies as well as guidance on how to apply them correctly. The Board of Management strives to act in accordance with ethical principles. It is unreservedly committed to compliance and declines to be involved in any transactions that are inconsistent with these values. It is also fully committed to compliance with competition law and does not tolerate any form of corruption.

Compliance organisation in place A Compliance Officer appointed by the Board of Management coordinates compliance activities within the Group. The individual business units and subsidiaries have their own compliance coordinators, who are responsible for compliance in their organisations and present structured written reports twice a year to the Compliance Officer. The Compliance Officer in turn reports to the Board of Management and Audit Committee. As well as information on compliance activities and changes to the legal situation or compliance organisation, the reports also detail possible future risks and countermeasures. The basic principles of the compliance organisation are described in rules of procedure. The duties of the relevant employees are set out in job descriptions.

Code of conduct forms the basis Compliance with these principles is set out in the code of conduct, which provides a mandatory framework for ensuring that behaviour towards business partners and employees is fair and in compliance with the law. The code of conduct forms the basis of a structured system of policy management that is continually updated. Other policies, such as the zero tolerance policy, the gifts and entertainment policy, the policy on the engagement of external distributors, the anti-money laundering policy and the insider trading policy, provide employees with binding rules on specific issues relevant to their day-to-day work.

Training is intended to ensure that employees are aware of the relevant laws and corporate policies, and that they comply with them at all times in their day-to-day work. Salaried staff in the head office sales, procurement, research and development and administration units, as well as in the subsidiaries, generally receive annual training sessions that are specifically tailored to their areas of activity. In the production plants, compliance training takes place in conjunction with the regular safety training.

Whistleblowing system introduced Employees can supply information or direct questions to line managers, compliance coordinators, the Compliance Officer or the managers responsible for the legal affairs or internal audit units. Furthermore, since the beginning of 2017, the DEUTZ AG website has featured a whistleblowing system that can also be accessed by non-employees. Any information supplied is rigorously followed up. Any necessary investigations are carried out by internal audit, with external support if required.

Regular meetings are held to develop, discuss and coordinate compliance initiatives. These activities focus on preventing corruption, tackling money laundering and complying with export regulations (including export controls). They also ensure safety in the workplace, IT & data security, corporate security and product safety. A further aim is to prevent breaches of environmental, antitrust and insider trading laws.

As and when needed, the Board of Management and the Compliance Officer take legal advice as part of their efforts to continuously improve the compliance management system. The internal audit department advises on all activities. The compliance management system is also reviewed by internal audit or by external consultants, and is monitored by the Audit Committee on behalf of the Supervisory Board.

Training stepped up Compliance activities at DEUTZ AG during the year under review again centred on the continuation and intensification of regular staff training, including for staff at subsidiaries outside Germany. The primary focus was on the code of conduct, money laundering, gifts, commission, export checks, antitrust/competition law and contract law. In 2017, around 1,100 employees took part in the various classroom-based training courses. In the production plants, compliance training takes place in conjunction with the annual safety training measures. Around 1,800 employees worldwide successfully completed the e-learning programme.

At DEUTZ Corporation USA, additional classroom-based training was provided on compliance with the International Traffic in Arms Regulations (ITAR). An e-learning programme specifically for the US was launched in 2017. From 2018, this will be mandatory for all DEUTZ Corporation employees.

OVERARCHING TOPICS

Customer satisfaction, innovations and supplier management are important overarching topics.

Because of the materiality of DEUTZ AG as the executive parent company, there is currently no system that monitors overarching topics in the Group as a whole. Our reporting therefore focuses on DEUTZ AG. The local senior management teams regularly report on relevant matters to DEUTZ AG's management.

CUSTOMER SATISFACTION

DEUTZ AG has adopted a zero-error strategy. Our main aim in pursuing this quality assurance programme is to ensure that we always meet our customers' expectations. The idea is to detect errors before they actually occur. And where errors do occur, we have to learn from them quickly in order not to make the same mistakes again. A further objective concerns delivery performance: A high standard of delivery performance means delivering engines and parts at the right time and in the right quantity and thus enhancing customer satisfaction. The aim is for customer satisfaction to be as high as possible, which is why it is regularly measured using various means.

Comprehensive measures under the zero-defect strategy DEUTZ AG is lowering its defect rate using a range of measures that, depending on their scope, are defined by the responsible departments or in conjunction with the Board of Management. The senior management team also plays its part by receiving regular reports and making important decisions. In all parts of the Company, action is being taken to improve quality. In 2016, we developed a concept to implement our quality assurance programme, designating certain employees as 'multipliers' and providing them with the necessary training to run workshops. This system was further refined in 2017. At two half-day sessions, managers and employees were given intensive training on topics such as customer satisfaction, quality of work and constructive approaches to dealing with errors.

A survey carried out in collaboration with the Laboratory for Machine Tools and Production Engineering (WZL) revealed that the culture of quality assurance among middle-management employees at DEUTZ AG was very strong on average in terms of external customer focus.

We regularly gauge the levels of satisfaction among DEUTZ AG customers in order to identify areas where we could improve. The customer feedback is used to create action plans that are designed to improve aspects such as customer communication, the availability of contact persons and the transparency of pricing.

The senior management team is closely involved in the implementation of measures.

Quality assurance begins with suppliers DEUTZ AG works together with its suppliers to systematically apply the advanced product quality planning (APQP) process, with the aim of safeguarding and continually improving the quality of delivered parts. This ensures that supplier parts are procured in accordance with the product development process and are of the required quality before volume production begins. Suppliers' delivery reliability and quality performance are also regularly evaluated.

An external service provider works with the Business Intelligence unit to analyse the results of the customer satisfaction survey. In addition, a monthly report on all quality- and customer-relevant KPIs as well as a weekly status report on the most important problems is sent to the unit heads and the Board of Management to ensure a rapid response time where targets are not being met.

Regular reviews At DEUTZ AG, a monthly report on defects reported by customers is presented to the Board of Management and the relevant departments, based on which rapid remedial measures are defined. The proportion of employees trained as part of the quality drive stands at 55 per cent and is increasing all the time. An annual management review examines the financial and non-financial quality KPIs. Here too, the measures taken on the basis of previous reviews are analysed to see how effective they have been. The 2016 survey revealed that customer satisfaction had increased overall compared with 2013, with an increase in scores recorded in most categories.

INNOVATIONS

Our aim is to position DEUTZ as a leading manufacturer of innovative drive systems.

Innovations at DEUTZ AG are primarily in one of the three following areas:

1) Alternative fuels: As well as looking at liquefied petroleum gas (LPG), we are focusing on natural gas, hydrogen and fuels generated from renewable sources.

2) Hybrid drive systems: A key pillar of our development work is the combination of internal combustion engines and electric motors (hybridisation).

3) Digitalisation: There is a particular focus on innovative digital solutions that offer our customers new services (connectivity, smart services for engines).

Centralised research and development At DEUTZ AG, most innovations originate from the central R&D department in Cologne-Porz. Our DEUTZ Corporation and Torqeedo subsidiaries are involved at an early stage in product planning so that they can actively contribute their market-specific requirements to the development and innovation process. DEUTZ Corporation focuses in particular on US emissions legislation (EPA, CARB). Torqeedo is most closely involved in the innovation process when it comes to hybridisation and electrification.

Within DEUTZ AG, the product management department is responsible for monitoring the market and for the product requirements that result from this. Members of the Board of Management are among those that attend its quarterly 'Product Boards', at which market trends and preliminary development work are discussed and other development activities are initiated and prioritised. New developments are brought on and assessed with the aid of the well-established product development process (PEP). Internal and external development work is carried out in order to achieve the Company's targets. In the case of external development work, we collaborate closely with development partners that include suppliers, universities and research institutes.

Torqeedo provides innovation boost In 2017, we acquired Torqeedo GmbH. The company serves as the nucleus for the E-DEUTZ strategy, under which we aim to develop hybrid and all-electric drives for off-highway applications. Torqeedo's expertise in electric-powered drive systems is providing a huge boost to innovation at DEUTZ.

Every year, Torqeedo brings new products to market that consolidate and extend its competitive edge in the market for electric drives for boats.

As previously mentioned, the DEUTZ AG senior management team is closely involved in innovation activities via the 'Product Boards'. At these meetings, which are attended by representatives from product planning, sales and service, the Board of Management discusses the status of preliminary development and approves suitable projects for the next stage of development. Subsidised projects are discussed by a committee below the level of the senior management team. An innovation process is currently being worked on in this area.

DEUTZ broadens its technology portfolio Last year, we presented a number of pioneering new developments that stemmed from our innovation activities. At Agritechnica, the world's biggest agricultural machinery fair, we unveiled our Stage V-certified engine range, our new in-line engines with capacities from 9 to 18 litres, and the E-DEUTZ strategy for hybrid and all-electric drives. We are also committed to investing in the digitalisation of our service products. As well as the DEUTZ Connect app, a tool for remote engine diagnostics, we have a new web shop that has brought the DEUTZ service network online.

DEUTZ AG uses a bonus-driven ideas management scheme to harness the creativity of its employees. Last year, the ideas that they submitted (an average of 24.1 per 100 employees) generated a benefit of more than €200 thousand.

Multitude of patents and awards We use patents, patent applications and utility models to safeguard our expertise against unauthorised use by third parties. In 2017, DEUTZ AG submitted 20 new patent applications, six of which were in Germany. DEUTZ AG now holds a total of 125 patents registered in Germany and 189 registered elsewhere.

Torqueedo has brought a multitude of new products to market in recent years. It has also received numerous awards for these, including the Pittman Innovation Award from Sail Magazine in the US for its Cruise FP Rudder Drive, and the NMMA Innovation Award 2017 from the US National Marine Manufacturers Association for its Cruise F.

SUPPLIER MANAGEMENT

DEUTZ AG's overarching supplier management system¹⁾ is designed to continually improve quality, lead times, commercial conditions and general communication with our suppliers. There is a clear focus on supplier development. As part of this quality improvement process, target defect rates are defined for each product group, communicated to the suppliers and regularly monitored, with remedial measures initiated where necessary. Our overarching objective is to have zero defects. All new suppliers need to be approved by DEUTZ based on self-declarations, feasibility studies, and supplementary documents and criteria. This process usually includes a site audit. The DEUTZ Group uses only certified original equipment suppliers (certified to ISO 9001:2015 as a minimum). Purchasing at the subsidiaries, particularly DEUTZ Corporation and DEUTZ Spain, is modelled on the supplier management system in use at DEUTZ AG.

¹⁾ The statements relate to direct suppliers that have a contractual relationship with DEUTZ.

Performance measurement tool DEUTZ AG manages its suppliers using a 'supplier cockpit'. We use this to monitor suppliers' performance from purchasing, delivery and quality perspectives and, in the case of development partners, with regard to their research and development capabilities and their ability to innovate. Before being included in the cockpit, suppliers must first be categorised accordingly. Their results for the individual KPIs and how these change over time are used to initiate remedial measures and improve performance.

For further information, please see the Compliance and Customer Satisfaction chapters on pages 74 and 75 et seq.

On a monthly basis, the senior management team at DEUTZ AG is provided with information about the procurement budget and other KPIs in the balanced scorecard. This monthly procurement management report contains key figures for the Board of Management, including key financials and KPIs related to quality. The underlying targets were confirmed by the Board of Management.

Supplier due diligence process being set up to ensure compliance DEUTZ AG assesses its suppliers using self-declarations and audits, including preventive audits where necessary. As previously mentioned, the Company also uses a 'supplier cockpit', a piece of supplier management software that can be used to categorise suppliers and track their performance. A supplier due diligence process is currently being set up to ensure compliance. The first global surveys are currently being evaluated. The TSD (Total Supplier Development) steering committee meets every two weeks to discuss data from the supplier cockpit and determine what action needs to be taken. A system of risk management for suppliers is also in place, covering risks such as insolvency, corruption, natural disasters and local developments.

Regular review of KPIs DEUTZ AG compares the current and target figures in regard to cost savings, supplier performance and quality KPIs. The degree of target attainment is also checked. In 2017, we visited and audited a large number of suppliers. The defect rate (ppm) for deliveries was lower than ever before last year.

CORPORATE SOCIAL RESPONSIBILITY¹⁾

Corporate social responsibility is a well-established tradition at DEUTZ. As a company with operations around the world, we of course shoulder our responsibilities as a corporate citizen. This includes responsibility for our decisions and our actions, for our products and services, for our customers and lenders, for the environment and for society. We have been involved in corporate citizenship projects for many years, not only in our home region in the area around Cologne but also throughout Germany and beyond.

Nurturing enthusiasm for technology The DEUTZ engine museum, which includes exhibits on the origins and history of global motorisation and shows original machines from the early days of the engine, opens to the public free of charge and continues to attract a good number of visitors. Our history began more than 150 years ago with the founding of N.A. Otto & Cie., the predecessor of today's DEUTZ AG. The Company's history department, which is run on a voluntary basis, and the Friends of DEUTZ's Engine Collection, whose patron is Professor Andreas Pinkwart, Minister for Economic Affairs in the State of North Rhine-Westphalia, again initiated joint projects with the Rhineland Regional Association, the Knowledge Foundation of the Sparkasse savings bank in Cologne/Bonn and the Luxembourg Science Center in 2017.

DEUTZ also promotes a continual dialogue of ideas in order to nurture enthusiasm for technology among the general public, particularly young people. As part of the redevelopment of the former DEUTZ site in Cologne-Mülheim, for example, the Company is helping to preserve historical features in partnership with investors and the City of Cologne.

Helping young people and the unemployed into work For more than 26 years, we have been working with IN VIA – an association under the auspices of the German Caritas organisation – and the German Federal Employment Agency to provide career preparation courses for young people with learning and social difficulties. In 2016/17, a total of 28 participants underwent basic metalwork training over a ten-month period at the DEUTZ training centre. In 2017, 74 per cent of those who completed this training then enrolled on a vocational apprenticeship scheme, which is a relatively high proportion.

Successful integration of disabled workers DEUTZ has also successfully worked with GWK, a not-for-profit organisation based in Cologne, for more than 40 years. Currently, over 110 people with disabilities work for us at various sites on tasks that include processing packaging and assembly orders, using machines to produce additional articles such as belt pulleys and oil level gauges, and handling printing orders. The many different work steps enable the deployment of employees with a variety of abilities who benefit from the continuity of the repetitive tasks.

Playing our part in the community We support community projects in the region with our 'DEUTZ fulfils your wish' Christmas initiative. In 2017, around 90 youngsters from Kalker Kindermittagstisch wrote down their wishes on 'wish notes' and hung them on the Christmas tree in the foyer at our head office in Cologne-Porz so that DEUTZ employees could make their wishes come true. Employees at the Cologne-Kalk and Cologne-Porz sites also organised a donations drive as part of this community project. Kalker Kindermittagstisch serves a hot meal to up to 120 children every day and supervises them while they do their homework.

In spring 2017, apprentices at our Ulm site got involved with 'Guter Hirte', a local organisation that looks after young single parents with small children, young people in need and child refugees without parents.

Dr Hiller becomes patron of the DEUTZ choir In January 2017, the new Chairman of DEUTZ AG's Board of Management, Dr Ing Frank Hiller, became patron of the DEUTZ choir. This sends a strong signal, both internally and externally, of the choir's significance for the Company.

The ensemble regularly creates positive publicity for the DEUTZ name through its concerts and other appearances, which range from performances for staff and customers and local concerts at the Cologne Philharmonic Hall and Cologne-Gürzenich events centre to tours to churches and concert halls in Germany and abroad. Last year, almost 10,000 people were able to enjoy the choir's singing.

¹⁾ Not checked by the external auditor.

The choir also supports good causes. In 2017, donations collected from concert-goers totalling €7,200 were distributed to, among other organisations, the 'Good deeds' charity of the Kölner Stadtanzeiger newspaper, the 'Kölnische Rundschau für das Hilfswerk (Rundschau-Altenhilfe: Die gute Tat e.V.)' of the Kölnische Rundschau newspaper and the Cologne hospice service for children and young people.

Personal involvement by senior management The members of the Board of Management and managers at DEUTZ AG are also fully aware of their responsibility to lead by example. They have been contributing personally to various charitable associations, trade associations, committees, trusts and other forums for many years.