THE TECHNOLOGY GROUP
FOR SECURITY AND MOBILITY

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Armin Papperger, CEO
Maintaining the two-pillar structure
Minimizing risks and counterbalancing economic cycles

Rheinmetall AG

Defence

Contributing <50% of Group sales and **negative** earnings in 2014

Automotive

Contributing >50% of Group sales and **100%** of Group earnings in 2014

**TWO ESSENTIAL HUMAN NEEDS**

**TWO FASCINATING HIGH-TECHNOLOGY SECTORS**

**TWO SEGMENTS WITH GROWTH OPPORTUNITIES**
“Rheinmetall 2015”
Automotive fully on track, in Defence time shift of full realization

- **Strong development** of Automotive in China and Mexico
- **Export license delays** affect international Defence orders and thus, the development of certain hubs, e.g. in Russia or Middle East

- **Strong performance** in Mechatronics (+12%*), **considerable growth** in Hardparts (+6%*)
- **Ramp-up of large system contracts** in Defence, but **weakness in components business** by receding demand and export license delays

- **Restructuring on track**, low-cost capacities in Automotive increased, high-cost sites downsized
- **Better focused Defence business** due to comprehensive restructuring; additionally adjustments in two subsidiaries and closing of Oslo site

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* 9M 2014 vs. 9M 2013 for continuing operations
Profitable growth
Successful strategy to develop the segment

Operational earnings  in EUR million
Operational margin  in % of sales

- Strong pipeline of innovations
- Effective portfolio adjustment by ATAG JV
- Significant growth in Chinese business
- Optimized location and employment structure
- High share of contracted business until 2017 (>95% excl. Aftermarket)

Automotive is on the right track to continue profitable growth

* Continuing operations, i.e. excluding ATAG JV
Long-term perspective
Tailwind by a continuously growing market

Global LV production  in million units

Source: IHS Automotive

* Without China and Japan
** Without Germany
Deterioration of earnings
A set of internal and external factors impacts Defence business

Operational earnings \textit{in EUR million}

- Potential warranties in a navy weapon contract
- Cost overruns and sales decline in Norwegian subsidiary
- Product mix effects by ramping up low-margin system orders
- Trough of the economic cycle of ammunition business (de-stocking)
- Delayed export licenses, particularly in high-margin business
- Withdrawal of export license to Russia by German government

Business and contract risks materialized – in addition, previously booked profits burden current earnings
External and internal impacts on earnings
Situation analyzed, countermeasures initiated

<table>
<thead>
<tr>
<th>External impacts</th>
<th>Internal impacts / Product mix (EUR 10 million)</th>
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<tr>
<td>Withdrawal of export license to Russia</td>
<td>Provisions for potential warranties in naval gun contract</td>
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<td>EUR 20 million</td>
<td>EUR 20 million</td>
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<td>Delayed export order licenses, esp. ammunition and Protection Systems</td>
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<td>EUR 20 million</td>
<td>Cost overruns in Norwegian subsidiary</td>
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<td>Sales decline due to weak markets</td>
<td>EUR 10 million</td>
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<td>EUR 20 million</td>
<td>EUR ~ 60 million</td>
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<td>EUR ~ 60 million</td>
<td>EUR ~ 40 million</td>
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Shape and adjust to markets
- **Claiming compensation** for withdrawal of export license to Russia
- **Establishing early consultations** with German export authorities to prevent delays or unexpected decisions
- **Extending the focus on uncritical markets** regarding export licenses
- **Reassessing investment strategy**

Adapt organization and processes
- **Downsizing capacities** in two international subsidiaries and closing one site
- **Continuing improvement of project management skills**
- **Replacing management**
National perspective
The “Magic Square” of German defence industry

Key technologies
Definition of key defence technologies in Germany by German government

Export license policy
Specification of reliable export license policy to enable sustainable corporate planning

National procurement
Clarification of national demand and procurement in order to set up programs

Consolidation
Consolidation of the industry on a national and/or on a European level, depending on ❶, ❷, ❸
The “Magic Square” of German defence industry

(1) Definition of key defence technologies in Germany

Definition of key defence technologies in Germany

1. Exogenous
2. Endogenous
3. Exogenous
4. Endogenous

— Fundamental for long-term German security policy

— Key question: Which competencies will the German government define as key national defence technologies?

— Currently ongoing high-level discussion about the first draft of German MoD
The “Magic Square” of German defence industry

(2) Definition of national demand for security products

— After a period of “peace dividend” and in the light of rising global conflicts, we now see a change in mind of public opinion and of decision makers

— Set-up of R&D and procurement programs for relevant key equipment of German forces
Definition of national demand for security products

First requests and drafts show rethinking of national procurement

- Budget request for further 131 Boxer vehicles recently approved
- Continuation of upgrade program for Fox tanks
- Equipping forces by further “Gladius” systems
- Replacement of military trucks fleet
- Request for new main battle tank and discussion about needed number of vehicles

What are the relevant key products for national security in 2020 and beyond?

- Fuchs
- Leopard
- Puma
- Trucks
- Gladius
The “Magic Square” of German defence industry

(3) Export license policy

— Currently continuation of previous practice of case-by-case decisions,…

— …but high uncertainty and costly delays in the process of issuing licenses

— Thus, reliable and sustainable guidelines for exports to third-party countries needed, especially for identified key technologies

— Supplemented by an improved early warning system
The „Magic Square“ of German defence industry

(4) National and European consolidation of the defence industry

Discussion opened by announcement of KMW/Nexter JV and intended divestments of Airbus Defence & Space

Other way for a successful consolidation:

- First step: national consolidation to realize synergies and to form “national champions”
- Second step: “national champions” establishing on European and on international level
National and European consolidation of the defence industry
First step: Priority of a national consolidation

National consolidation

— only makes sense, if complying with political and economic conditions (key technologies, procurement, export policy)

— could pave the way for an international consolidation by forming “national champions”

List of companies not complete and only for illustrating reasons

* Family-owned

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National and European consolidation of the defence industry

Second step: Consolidation of a fragmented European market

- European defence industry still broadly fragmented
- Large public shareholding in many European defence players complicate a possible consolidation
- Political discussions about the need of international consolidation induced by shrinking budgets in Europe

List of companies not complete and only for illustrating reasons

- Patria*
- Saab
- Chemring
- Oto Melara*
- Aselsan*
- BAE Systems
- Nammo*
- Thales*
- RUAG*
- DCNS*
- DCI*
- Nexter*
International perspective
Defence is a growing market due to globally increasing need for security

Global defence spending in USD billion

Source: IHS Janes, SIPRI (www.sipri.org), Rheinmetall team analysis

* Without Germany
Future markets and hub development
Main factors for intensifying our internationalization

- **Export restrictions** implying obstacles for R&D spending in Germany
- **Stagnating defence budgets** in traditional markets
- **Unequal political support** (= unbalanced global competition)
- **Dynamic growth in new markets** (Asia/Pacific, Middle East, Latin America)
- **Increasing demand for local content**, i.e. local production, manufacturing, assembly
- **Unbalanced relation** between domestic sales share and value creation
Future markets and hub development

Unbalanced relation between domestic sales share and value creation

Unbalanced relation: More than 90% of value creation and gross margin generated in Europe, while European revenues only represent roughly 60%
Future markets and hub development

Realizing growth potential by more value creation in international hubs

- USA
- Canada
- UK
- Netherlands
- Switzerland
- Russia
- Scandinavia
- Italy
- Algeria
- Saudi Arabia
- UAE
- India
- Indonesia
- Brazil
- South Africa
- Australia

Hub with substantial growth potential by value creation
Other hubs to be continuously developed
Future markets and hub development
Intensifying today’s hub structure by covering global markets

Total USD 1,636 billion

USA 35%
Rest of the World

Next 20
Iraq, Sweden, Greece, Kuwait, Thailand, Ukraine, Switzerland, Chile, Belgium, Angola, Argentina, South Africa, Portugal, Malaysia, Denmark, Venezuela, Egypt, Morocco, Azerbaijan, Finland

Next 14
Israel, Spain, Columbia, Taiwan, Netherlands, Algeria, Iran, Poland, Singapore, Oman, Indonesia, Pakistan, Mexico, Norway

Next 10
UK, Germany, India, Brazil, Italy, South Korea, Australia, UAE, Canada, Turkey

Next 5
China, Russia, Saudi Arabia, France, Japan

Source: SIPRI World Military Expenditure (www.sipri.org)
Mitigating compliance risks

Compliance is an essential element of Rheinmetall’s corporate culture

Due to current cases in India and Greece, we completely reshuffled our compliance system

Countermeasures initiated

- Supporting official investigations
- Additional external investigations authorized
- Internal compliance organization strongly enlarged and improved
- External ombudsman appointed
PERSPECTIVE 2015 AND BEYOND
Defence tomorrow

**Strategic orientation for Rheinmetall Defence**

- Improving operational performance to resolve earnings trough in the short term
- Minimizing project risks and corresponding one-offs by strengthening project management capabilities
- Reassessing investment strategy in combination with hub strategy
- Combining existing product portfolio with **new business concepts**, e.g. Ferrostaal JV
Earnings trough in Defence
Original margin target not to be achieved in the short to medium term

Operational earnings in EUR million
Operational margin in % of sales

Assumptions and drivers:
- Recovery of defence markets in NATO and “NATO-equivalent” countries
- Recovery of weapon and ammunition business
- Normalization of the export license process in Germany
Automotive tomorrow

Strategic orientation for Rheinmetall Automotive

- Growth with existing products in emerging markets, e.g. Mexico, China
- Growth with new products in existing markets, e.g. variable valve train
- Expanding Aftermarket business
- Safeguarding restructuring success
- Increasing the operational flexibility in economic up- and downturns
- Improving efficiency of R&D spending
Sustainable improvement in Automotive
Optimistic to succeed the original margin target in time

Assumptions and drivers:
- No considerable economic slowdown in global light vehicle production
- Strong growth of Mechatronics above market average

* Continuing operations, i.e. excluding ATAG JV
Definition of key defence technologies in Germany
First draft by German Ministry of Defence
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