



Annual General Meeting

MTU Aero Engines Holding AG

Address by the Chief Executive Officer

Egon Behle

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in Munich

- Convenience translation -  
- **Check against delivery** -

Good morning ladies and gentlemen, shareholders of the company,

On behalf of the Board of Management of MTU Aero Engines Holding AG, it is my pleasure to welcome you to our 2008 Annual General Meeting.

Thank you all for taking the time to be here in Munich today, to hear how MTU's business has developed in 2007 and learn more about your company's future prospects. Before going any further, I would like to express my sincere thanks for your active, personal interest in MTU.

I wish to start by sharing some of my early impressions of MTU, gathered during my first four months as CEO. I will then continue with a summary of the company's performance in the financial year 2007 and report on how we have progressed in the first months of 2008. This will be followed by a short description of our latest projects and technology programs and, to close, I will take a look forward into the future and provide you with an assessment of the way the market and our business can be expected to develop.

But first of all, allow me to say a few words about my professional background. I have a degree in aerospace engineering and my working experience over the past 25 years includes five years in the aerospace sector, as sales director for Dornier on Lake Constance, five years in the machine tools industry, and 15 years in the automotive sector with Bosch and ZF Friedrichshafen. For the last five years I was CEO of ZF Lenksysteme GmbH, a company of a similar size to MTU in terms of revenues, where I was called upon to implement a turnaround process.

Ladies and gentlemen, it has been four months since I took over the post of CEO at MTU Aero Engines. During this time, I have formed a picture of the whole enterprise, visiting the MTU plants across the world from the United States to China and profiting from numerous occasions to talk with employees at all levels, from executive managers to office clerks. I have sought intensive dialog with our partners and customers, and with government representatives and industry associations. I have meanwhile also met with many of the investors and analysts who follow our company's activities, during visits to London, Frankfurt, New York and Boston. During these meetings and in interviews with the media I have spoken about MTU and its future prospects, also mentioning the challenges we currently face in view of the U.S. dollar's evolution and the general market situation.

What conclusions did I draw from these few weeks, and what action can you expect from me?

MTU's high reputation rests not only on its technological and economic strength, but also on its motivated, highly trained workforce. It is firmly embedded in a reliable network of stable partnerships. My ambition is to continue to build on this privileged market position. Our twin objectives are to be leaders in innovation and in cost management. Innovation is the factor that underpins our strength and ultimately determines our market success. Cost management will enable us to remain competitive over the long term and improve our potential for growth, given that customers not only demand excellent products but, moreover, expect to pay an acceptable price. At the same time, we want to generate sufficient profits to be able to invest in projects that will guarantee our future, while still paying out an adequate dividend to you, our shareholders. You can rest assured that I will do everything in my power to ensure that your company remains committed to excellence and innovation, and continues to produce successful, profitable growth.

At the very beginning of this year, I and the other members of the Board of Management sat down together to discuss the company's situation and our strategic objectives. I will report on our conclusions in more detail later on.

But first, allow me to present a review of the past year's business.

## **2007: A successful year for MTU**

2007 was a successful business year for MTU. The aviation industry has been going through a period of sustained growth, and MTU once again produced very successful results.

Indeed, we have been so successful that we were able to raise our earnings forecasts in the course of the year, and by the end of the year we had met and in some cases even exceeded our targets for all performance indicators.

Our revenues improved by 7 percent to around 2.6 billion euros.

EBITDA<sup>1</sup> rose by 24 percent to 393 million euros. This is significantly higher than the 2006 figure of 318 million euros, and also higher than our forecast.

Our underlying net income for 2007 has increased significantly too, improving by 22 percent to 148 million euros. This represents a sum of 2.83 euros per share in 2007, compared with 2.25 euros in 2006.

And finally our free cash flow amounted to 132 million euros, which is 12 million euros higher than our forecast.

## **2007: Sustained positive growth**

Now let me give you a short breakdown of these figures:

### Revenues

In terms of revenues, the commercial engine business produced particularly successful results for MTU. Revenues from this business improved by 11 percent compared with the previous year.

In the military engine business, our revenues grew by 2 percent.

Growth in commercial maintenance revenues, at 5 percent, was lower than we had expected. Our Hannover plant was unable to implement the process changes and logistics workflows, necessitated by the high level of orders received in the previous two years, as quickly as we had hoped. Further difficulties were encountered last summer when new software and logistics systems were introduced, making it necessary to undertake further changes and provide additional resources. The associated additional costs will continue to affect performance in the first two quarters of 2008. I will come back to this point later.

### EBITDA

MTU increased its profitability still further in 2007. EBITDA grew at an above-average rate of 24 percent, while return on sales rose by more than 2 percentage points to 15.3 percent. This places us well within our target EBITDA margin of 14 to 15 percent.

This result demonstrates the effectiveness of our program of measures to boost efficiency and profitability, through which we will be able to achieve annual savings of 50 million euros from 2008 onward. This may sound considerable, but it is not enough to counteract the various additional cost factors arising from the U.S. dollar exchange rate and the pressure on prices while still meeting our targets on a sustainable basis. I will return later to the measures we have already taken and those we intend to take.

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<sup>1</sup> EBITDA = Earnings before interest, tax, depreciation and amortization

The company's good operating results in 2007 were mainly attributable to the OEM business, where EBITDA increased by 40 percent. In the commercial MRO segment, operating profit remained 15 percent below the previous year's level, reflecting the particular challenges at the Hannover site that I mentioned a short while ago.

#### Free cash flow

MTU's free cash flow increased by 14 percent in 2007. The majority of this cash flow was used to finance our share buyback program and to cover the dividend payment.

For those of you who are interested, more detailed information on our business results in 2007 can be found in our Annual Report, copies of which have been laid out in the foyer.

#### **Dividend for 2007**

As I mentioned earlier, 2007 was a good business year for MTU. We would like you, our shareholders, to share in MTU's success. As item 2 on today's agenda, therefore, you are invited to accept our proposal of distributing the 47.2 million euros of our unappropriated profit in the form of a dividend payment. MTU treasury shares do not bear dividend rights, and are therefore excluded. Our proposal corresponds to a dividend payment of 93 cents per share and thus an increase of 13 percent on the dividend paid out last year.

#### **Share performance**

As customary for any listed company, a review of the past year's activities necessarily includes a commentary on the evolution of the company's share price. Looking back to the beginning of 2007, you might remember that the MTU share started out at a quoted value of 36.21 euros. Over the first six months of the year it performed significantly better than the already positive stock market average, consistently increasing in value up to August 1, when it reached an all-time high of 50.93 euros. The abrupt reversal of capital market trends from then onward also led to a turnaround in the development of the MTU share. Its closing price at year-end was 40.00 euros; in November it had fallen to as low as 31.69 euros.

Year on year, the price of the MTU share rose by 12.8 percent, thus outperforming the relevant sector indices – MDAX and the Dow Jones Aerospace & Defense Index.

Since the beginning of 2008, the MTU share has had to contend with the pessimistic mood of a stock market shaken by the subprime mortgage crisis and by general economic developments, as well as a steadily weakening U.S. dollar. Between January 1 and the end of last week, the value of the MTU share dropped by 32 percent. This indicates that the MTU share has been more volatile than the MDAX, which has fallen by 5 percent over the same period, or than the members of its peer group, which on average traded at 13 percent lower value. At the close of trade yesterday, the MTU share was quoted at 27.55 euros. This price level, dear members of the audience, is unsatisfactory, and we are unable to entirely follow the reasoning behind it: Out of the 19 current ratings published by financial analysts covering the MTU share, 17 rate it as either "buy" or "hold", giving an average target price of around 36 euros. MTU has made a promising start to 2008, and the interim results presented last week fully support our forecasts.

## 1st quarter 2008

Revenues of 630 million euros were generated in the first three months of 2008, remaining close to the previous year's level. After adjustments for the U.S. dollar exchange rate, revenues even increased by 10 percent.

MTU improved its adjusted EBITDA by 9 percent to 98.3 million euros in the first three months of 2008. The EBITDA margin increased by 1.5 percentage points to 15.6 percent. The improvement in the EBITDA margin is above all attributable to the positive evolution of the OEM business, where the successful implementation of various programs to improve efficiency, a high demand for spare parts, and the start of volume production in certain programs compensated for the unfavorable U.S. dollar exchange rate: The EBITDA margin in the OEM business amounted to 22.6 percent, while in the commercial MRO business it amounted to 5.5 percent.

MTU's first-quarter net income more than doubled to 44.2 million euros. The comparative 2007 figure includes a nonrecurring charge for the early redemption premium in connection with the high yield bond. Excluding this exceptional item, net income increased by 40 percent.

These results show that MTU is still a highly profitable company, despite the continuing unfavorable U.S. dollar exchange situation. And the first quarter's results substantiate our expectations for the financial year 2008 as a whole. We are confident that we will reach our targets.

## Evolution of the business units

That more or less sums up the major points concerning our general financial results. Now let's take a closer look at some of the events that have marked the year for the various business units.

### **Commercial engine business: Sound product mix provides basis for sustained business development**

Let's turn first to the milestones in the **commercial engine business** and – more importantly – what we hope to achieve in the current financial year:

- The GP7000 engine for the Airbus A380 reached a decisive milestone in 2007, when it was certified in conjunction with the A380. This paves the way for deliveries of volume production, for which output will be accelerated this year. Our aim is to secure our market share of around 50 percent on a long-term basis.
- And together with our partners Pratt & Whitney we have made significant progress on the next generation of engines for regional jets and for short- and medium-haul airliners: The first tests on the geared turbofan have been successfully completed, giving us a strong time lead over our competitors. We expect to be able to sign contracts with Pratt & Whitney in the coming weeks, according MTU an anticipated 15-percent share in the program. The launch customers for the geared turbofan are Mitsubishi Heavy Industries and Bombardier, both of whom intend to equip their respective new regional jets exclusively with a geared turbofan engine.
- Another important project with a bearing on the future is the PW800 family made by Pratt & Whitney Canada. These engines are destined for use in heavy business jets. MTU aims to secure a significant percentage share in this program. The final phase of negotiations is already underway here too.

- We also plan to play a significant role in the future engine for the Airbus A350XWB and are examining other opportunities to successfully market our know-how.
- The V2500 continues to be our perennial bestseller – in particular in its new version, SelectOne, for which a consistently high level of new orders is being received. In April, we were awarded contracts worth 117 million euros for new engines of this type.

### **Military business: Expansion of business in the United States assures MTU's competitiveness**

Now let's take a look at the **military sector**:

- In 2007, MTU further consolidated its position in the world's largest military market, that of the United States. We have increased our share in General Electric's F414 / F404 military jet engine program to a total of 6 percent, and plan to augment our stake in this program still further. Work on the program has already started successfully.

We intend to make further inroads into the U.S. market. There are opportunities for participating in the engine program for new heavy-lift helicopters, and I don't exclude the possibility of acquiring a share in other engine programs for combat jets.

- Meanwhile, we continue to uphold our commitments to serve the military market in Germany and Europe, where we are involved in export drives in connection with various engine programs. The Eurofighter and its EJ200 engine has scored some major successes. Austria's order for 15 aircraft was followed in 2007 by Saudi Arabia's decision to order 72 aircraft. And the prospects for winning over even more export customers are looking good. India and Switzerland, for instance, are showing a particular interest.
- The TP400-D6 engine for the Airbus A400M military transporter is making significant progress. The engine's first flight aboard the flying testbed, a converted C-130 Hercules, is scheduled for this June. Later in the summer, the A400M itself – powered by four TP400-D6s – is due to take off on its maiden flight. Up to now, we have delivered all of the engines required for these first flights within the contractual deadline. We are doing all that we can to ensure that the A400M program will ultimately turn out to be a success.

### **Commercial maintenance: Better-than-average market growth**

In the **commercial maintenance** business, we improved the value of contracts for engines for which maintenance agreements are in place by 53 percent in 2007. This refers to engines that can be reasonably expected to be sent to MTU for maintenance under the terms of existing agreements.

One of the factors responsible for this substantial increase was at the same time one of the major business highlights of 2007, namely the largest single order in the history of MTU Maintenance. American airline JetBlue has chosen to have its fleet of V2500 engines – this is the engine that powers the Airbus A320 – serviced in Hannover. Over the full lifetime of the contract, which is to run for 15 years, the total volume of orders will amount to 2.4 billion euros.

Last year, we also entered into a strategic partnership with the Indonesian airline Garuda for the maintenance of their CFM56 engines. The CFM56 powers the Boeing 737. This partnership is particularly important in view of the fact that Indonesia – like China and other Asian countries – is one of the nations with the strongest growth in air traffic.

In 2007 we also began work on the construction of a second large test rig in Hannover. It will be completed by the middle of this year, thus removing a source of capacity limitations.

Despite this progress, our commercial maintenance business has also had to sail against the wind in certain respects in the past year. One unfavorable factor was the U.S. dollar exchange rate. Another was the introduction of new software and logistics systems, which necessitated the reorganization of certain fundamental processes. Together, these two factors had a negative impact on the performance of our maintenance business. And it took longer than originally planned to recover momentum.

But you can rest assured that we are doing everything in our power to bring the commercial MRO business back on course. The preparatory work has been accomplished and the necessary measures are being implemented. The most important leverage points are structural reorganization and reorienting our engine lines on the basis of optimized material flows. These efforts are already having the desired effect at an operational level. For instance we have significantly improved our performance in terms of on-time deliveries. We estimate that the impact of these measures on our financial results will start to take effect from the second quarter onwards. Meanwhile, we are progressing in the right direction. The management team in Hannover is highly motivated and being closely supported by the Board of Management.

### **Claire – MTU's Clean AIR Engine technology program**

I would now like to say a few words about the technological side of our business.

As you are all no doubt aware, the topic of climate change has increasingly dominated the headlines for some time now. And the aviation industry has been singled out as the object of much criticism – on the basis of the predicted twofold increase in the volume of air traffic between now and 2020. To prevent the burden on the environment from increasing to the same degree, aircraft and their engines have to become quieter, more fuel-efficient and less polluting. As pioneers in the design of aircraft engines, our response is clear: We want to be among the first to develop new technologies that will promote the sustainable development of the aircraft industry, even bearing in mind that aviation is only responsible for 2 to 3 percent of global CO<sub>2</sub> emissions.

Through the Claire (**C**lean **A**ir **E**ngine) technology program, MTU has found a way to answer this challenge in close collaboration with the researchers of Bauhaus Luftfahrt. Over the coming decades, fuel consumption and CO<sub>2</sub> emissions are to be reduced in three stages by up to 30 percent. And, as if that wasn't enough, perceived engine noise levels are also to be cut in half.

And how do we intend to do this? By combining several key components that have already been developed and tested, or for which proof of principle has been demonstrated. These new, environment-friendly technologies fulfill all expectations concerning energy efficiency and economic viability. This is what sets us apart from many of our competitors: MTU not only has visions but also already possesses the real-life components needed to realize them.

The component technologies in question will be added together in three stages to produce a "geared turbofan with counter-rotating propfan and heat exchanger technology". We are developing the geared turbofan in collaboration with our American partners Pratt & Whitney. The decisions by Mitsubishi Heavy Industries and Bombardier to equip their future regional and business jet programs with this type of engine confirm our belief that we have chosen the right technological approach and correctly interpreted the market's needs.

So, ladies and gentlemen, as you can see, our technological leadership is one of the essential prerequisites for our enduring market success and continuing competitive strength. And in turn we intend to link this with cost leadership.

## **Employees**

The real key to sustainable success is without doubt our employees, without whose dedication and highly motivated performance MTU would not have been able to achieve the results of the past year. I would therefore like to thank each and every one of MTU's over 7,000 employees for their hard work and determined efforts to assure MTU's future. I invite you to give them the round of applause that – I am sure you agree – they so manifestly deserve. Thank you.

The challenges that MTU has to face as a result of operating in an international market make it increasingly important that our employees should be able to think and act in entrepreneurial terms. For this reason, we involve them in all major decision-making processes at an early stage – and enable them to share in the company's success through a variety of performance-related incentives. On the basis our results in 2007, profit-sharing and other bonuses totaling approximately 26 million euros were paid out to employees.

For the first time, employees were offered the option of using their bonus payments to acquire MTU shares. MTU employees are entitled to receive a 50-percent supplement on top of the invested sum. In other words, for every two shares purchased by an employee, MTU is offering one additional share. In this way we want to show our employees that their performance is not only of importance to themselves but also to the company. The shares for the employee stock option plan were bought back on the stock market beforehand.

## **Share buyback**

And now a direct word to you, our shareholders: At the last Annual General Meeting on April 27, 2007, you granted us the authorization to purchase treasury shares with a par value of up to 10 percent of the company's capital stock. So far, MTU has acquired around 5 million shares under its buyback program. Of these, 3 million have been called in, thus concluding the share buyback program as authorized by the 2007 Annual General Meeting.

We want to continue along this path and are planning to buy back further shares. Hence today's motion asking you to grant us your approval to implement a new share buyback program, replacing that of 2007 and with an authorization valid through to October 2009. We wish to purchase these shares either on the stock market or through a public call for offers addressed to all shareholders.

## **Aviation remains a growth industry**

And now let me say a few words about the latest developments in our sector of industry.

Last year's statistics show that air traffic is continuing to grow at a significant rate. The International Air Transport Association (IATA) reports that the volume of international air traffic increased by 7.4 percent in 2007. Taking the development of air traffic in the various domestic markets into account in addition to international flights, the average global growth rate amounted to 6.6 percent. Even freight traffic, which increased by 4.3 percent globally in 2007, or by 3.5 percent including domestic traffic, was higher in 2007 than the long-term average.

Aviation industry observers expect to see further growth in 2008, with an increase in passenger traffic of between 4 and 6 percent on average, and an increase in freight traffic of somewhere between 3 and 4 percent. There are signs, however, that the growth curve in the United States has flattened, and that, globally, growth will be weaker in 2008 than in 2007.

The long-term outlook is positive: If the forecasts are accurate, this increase would seem to be the manifestation of an upward trend that is likely to last for more than just a few years. MTU stands to benefit to a considerable degree from this upward trend.

## **Outlook for 2008: Continued profitable growth**

As things stand today, what performance can we – and you, ladies and gentlemen – expect from MTU in 2008?

I have already mentioned the uncertainty concerning the U.S. dollar and its future exchange rate against the euro. The impact this will have on our business performance is obvious, and in all probability it will severely reduce our growth potential expressed in our key currency, the euro. Meanwhile, the price of energy and raw materials is likely to rise still further, and competitive pressure will increase as the economic situation of the aviation industry continues to weaken.

MTU needs to, and will, respond to this situation. At the Board of Management strategy meeting I mentioned earlier, we discussed and passed resolutions on a number of appropriate measures. In the short term, we will be taking further major steps to reduce costs. Budgets have been frozen, and strict limits imposed on recruitment plans.

For the slightly longer term up to 2010, we have started to draw up a cost reduction program focusing on product costs, and are beginning to introduce optimization measures in our supply chain along with other ways of increasing efficiency. We are optimistic that we will be able to achieve further progress in this context, and regard the present economic conditions as a challenge that will spur MTU on to improve its competitiveness still further. Of course, we have no intention of cutting back on the necessary development expense for our new programs to assure future growth.

But now let's return to the concrete aspects of our outlook for 2008:

The company expects to generate revenues of 2.6 billion euros, roughly equivalent to those generated in 2007. This corresponds to a growth rate of around 6 percent after adjustments for the effect of the U.S. dollar exchange rate. We expect revenues in the commercial engine business to increase by around 6 percent, discounting the effect of the U.S. dollar, with sales of new engines probably growing at a stronger rate than spare parts sales as a result of the start of volume production of the GP7000 engine for the Airbus A380. In the commercial MRO segment, we would like to see revenues grow by 4 to 5 percent in dollar terms; this is higher than the average for the market. We intend to keep revenues in the military business at a stable level.

Our estimated EBITDA target for 2008 is 390 million euros. In other words, we expect our operating profit to equal that of 2007 despite a significantly higher level of capital expenditure and the continuing effect of the unfavorable U.S. dollar exchange rate. We are consequently aiming for a return on sales in the upper region of our target corridor of 14 to 15 percent, as in 2007.

Our net profit for the year ought to reach the 180-million-euro mark in 2008; this represents an increase of around 20 percent.

We are reckoning on a free cash flow of approximately 100 million euros. This reflects the active steps we are taking to assure the company's future, including acquiring additional shares in engine programs. Another major project on the agenda is the construction of our new site in Poland.

Ladies and gentlemen, I am confident that we will reach the targets we have set ourselves for 2008 – especially given that the first quarter's results substantiate our expectations for the financial year 2008 as a whole.

In conclusion, I can say that MTU can look back on a successful business year, has made a good start to a new business year full of important challenges, and is well equipped to reap further success in the future. This gives us every reason to look ahead with confidence. We will continue to deliver the best work possible to convince our shareholders, customers and partners that they can count on our ability to perform. On behalf of the Board of Management, I would like to thank you all for the trust you have placed in us. We hope you will remain well disposed towards us, and continue to support our efforts.

Together with my colleagues, I now look forward to discussing any points you might wish to raise, and hope that you will approve the motions we have set before you.

Thank you for your kind attention.