

MAHLE

Driven by performance



ANNUAL REPORT 2006



CREATIVITY FOR THE TECHNOLOGY OF TOMORROW

Creativity is the engine of innovations. It drives new development—in science, research and technology, as well as in art. Behind this lies the strong passion for achieving what is new, better, and unique with imagination, perfection, and the utmost personal commitment, to create a work that continually moves and fascinates.

MAHLE innovations. The inventiveness of our employees produces technical masterpieces. And these objects have inspired artists to create expressive works of art. The works shown here reflect the creativity of our technology—with the technologies of creativity.



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*Prof. Dr. Heinz K. Junker
Chairman of the Management Board*

Dear readers,

For MAHLE, 2006 was a year of consolidation and preparation for important expansion moves in the future. Nevertheless, internal organic impetus enabled us to increase our sales by just under 5% to more than EUR 4.3 billion in a difficult market environment. This is primarily due to our good international market presence and our innovative strength as a technological leader in our core businesses.

On a global scale, the automotive industry was able to further increase its production figures, but there was a shift in the respective importance and growth rates of the various regions of the world. Some of our traditional customers in Europe and America have to contend with considerable problems. Stagnating markets, particularly in Western Europe and North America, and simultaneous construction of new output capacities in countries where labor costs are low, lead to considerable excess capacities, triggering a price war and stretching many companies to their limits.

We cannot avoid the effects of this general market development, which affects all companies in the automotive industry's value chain, right down to the end customer. In order to accommodate the increased demands for price reductions on our products and services and, at the same time, continue the development in revenue we have achieved in recent years, we had to intensify our efforts and strive for even higher productivity increases at all MAHLE locations. We are currently on course to achieve this goal.

At the same time, we want to further strengthen our presence in the major growth markets of the automotive industry. We see great potential for long-term organic growth in this area. In addition to our new engine valve production plant in Wölfersheim, Germany, we commissioned new plants for liquid filtration in Timisoara, Romania, and Shanghai, China, in 2006. In the course of the year, other new plants were constructed in Guangzhou, China, for air filtration system production and in Yingkou, China, for the production of bearings and piston rings.

Great effort was required in order to continue the development in revenue recorded in the previous year. Improvements were achieved in both income from ordinary business activities and the net income for the year, which we regard as a satisfactory development in comparison with the industry as a whole. However, we had set ourselves higher goals for the end of the year. In particular, the unexpectedly sharp rise in the cost of materials put a strain on profit. Even with considerable efforts in the area of procurement and purchasing policy, these effects could not be controlled, as almost all raw materials used in our production plants are dictated by global market conditions. In addition, various exchange rate developments had an adverse effect on profit.

The situation at many of our domestic locations continues to appear problematic, despite intensive efforts. We will therefore have no option but to bring in more streamlined cost structures, adapted to potential order levels.

After all, our strategic objective must be to strive for cost leadership on a global scale and, at the same time, consolidate and expand our status as a global technological leader. With this in mind, we began to substantially reinforce our advanced development capacities in 2006. New engine technologies, such as downsizing, super charging, and exhaust gas recirculation, which all help to reduce consumption, CO₂, and exhaust gases, are being researched in both theory and practice. The engine know-how of MAHLE Powertrain (formerly Cosworth Technology) is proving to be very helpful. Our new research and development center in Shanghai, China, commenced operations in April. This strengthens our competence in the increasingly demanding and diversified Asian markets. Similarly, we have further renovated and expanded our development locations in Japan, in order to continually improve the local service for our large Japanese customers. Toward the end of the year, construction work was started on another new research and development center near São Paulo in Brazil. In future, this center will be responsible for carrying out all application developments for the South American market and other special Group tasks, as well as for the topic of flex fuel.

In general, we assume that the process of consolidation in the first supply stage of the automotive industry will intensify in the future. Therefore, it is vital for MAHLE to continuously press ahead toward the long-term strategically defined growth objectives. This can only be achieved with stable development in revenue, both now and in the future. It forms the basis for our future strategic objectives.

In the first quarter of 2007, by acquiring the engine parts group of the American company Dana Corporation, Toledo, Ohio, and additional production plants for engine valves, we took further steps to bring our worldwide market position in the areas of piston rings, bearings, valves, and in the free trade business for engine components in line with our strategic objectives. Furthermore, we expect to acquire the air intake module and air filtration business segment of Siemens VDO Automotive shortly. With additional sales potential of approximately EUR 1 billion, it now makes good sense to integrate 33 new production plants and approximately 8,000 new employees into the global MAHLE production network. Consequently, restructuring expenses and integration costs will put a strain on the development in revenue for 2007. However, if we want to remain the partner of choice for our global customer base, we must further expand our worldwide presence and offer premium-quality products and services using the best technology at attractive prices. We can only achieve these goals by successfully integrating the business segments described and with above-average dedication from all employees in the global MAHLE family. "Driven by performance" is part of our corporate identity and our brand essence. Performance is the driving force for a successful future.

On behalf of the Management Board, I would like to thank all employees for their dedication and commitment in the past business year and our business partners for their good cooperation.



Heinz K. Junker



PACEMAKER

FOR THE FUTURE

PERFORMANCE THAT MOVES US FORWARD





DRIVEN BY PERFORMANCE—WORLDWIDE

A rapid change is taking place in the automotive industry—markets and technologies are changing more quickly than ever before. As our customers' leading development partner, we are globally established, with a regional presence. We see ourselves as a pacemaker for innovations that secure the competitive edge for the future. "Driven by performance"—with passion for performance, precision, perfection, and comprehensive systems competence in the combustion engine and engine peripherals, we consistently promote the development of vehicle and engine technology. We have been setting standards for progress for over 80 years. Throughout the world, we contribute to making mobility more reliable, more comfortable, more environmentally friendly, and more reasonably priced.

TECHNOLOGICAL LEADER WORLDWIDE

The MAHLE Group ranks amongst the top three systems suppliers worldwide for piston systems, cylinder components, valve train systems, air management systems, and liquid management systems. Our components and systems are used in every second automobile produced worldwide. Our customers include all automobile and engine manufacturers.

Following acquisitions in the first few months of 2007, approximately 47,000 employees now work at 110 production plants and seven research and development centers.

Members of the Management Board and Management Committee



Prof. Dr. Heinz K. Junker

Dr. Hans Peter Coenen

Dr. Hans-Josef Enning

Michael Glowatzki

Peter Grunow

Dr. Bernhard Volkmann

We are further expanding our top international position and market leadership by means of organic growth and targeted acquisitions in our core businesses. By doing so, we are safeguarding the performance and independence of the Company for dynamic future development.

CUSTOMER-ORIENTED, GLOBAL, EFFICIENT: THE GROUP ORGANIZATION

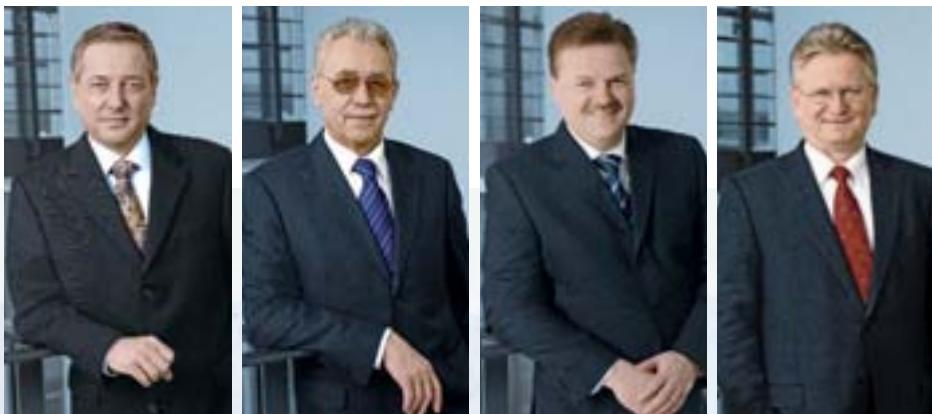
Our Group organization is consistently customer-oriented and globally focused. Our key account structure simplifies communication with the customer by representing all products and services. Five globally organized product lines cover the range of original equipment for the automotive industry.

In addition, independent organizational structures supply the free trade market for spare part products in OE quality and the market for small engine and large engine components, motorsports, engineering services, and industrial filtration.

MAHLE Group organization

Product lines			Profit centers
			Aftermarket
			Small Engine Components
			Large Engine Components
			Motorsports
			Engineering Services
			Industrial Filtration
Advanced development	Sales	Procurement	

Members of the Management Committee



Dr. Thomas Buchholz

Hans Gebert

Dr. Bernd Mahr

Dr. Rudolf Paulik



PRODUCT LINES

Piston Systems

Aluminum pistons for gasoline and diesel engines, articulated and steel pistons for commercial vehicle engines, piston assemblies and complete power cell modules.

Cylinder Components

Piston rings, piston pins, connecting rods, cylinder liners, bearings and bushings for combustion engines and other automotive applications, piston inserts.

Valve Train Systems

Machined cylinder heads and cylinder head assemblies. Machined engine blocks and complete engine assemblies, precision sintered parts, turbocharger parts. Complete valve train systems and their components.

Air Management Systems

Complete air intake systems, air filtration elements, valve cover modules, crankcase ventilation systems, design and acoustic covers, EGR modules, mechatronics components.

Liquid Management Systems

Oil filter modules, oil and fuel spin-on filters, fuel filter modules, fuel pressure regulators, inline fuel filters, carbon canister modules, heat exchangers for engines and transmissions, hydraulic oil filters, air driers.

PROFIT CENTERS

Aftermarket

Products for engine service and rebuilding from the complete MAHLE product range.

Small Engine Components

Cylinder assemblies, cylinder heads, pistons, and filters for small engines of handheld power equipment, motorcycles, and power sports vehicles.

Large Engine Components

Pistons and engine components for gas, diesel, heavy-oil, and multi-fuel engines for marine, applications and energy production.

Motorsports

Development and production of high-quality engine components for motorsports.

Engineering Services

Development of high-performance engines for road vehicles. Electronic control units and electronic diagnostics. Concepts to optimize consumption and exhaust gas, including the use of alternative fuels.

Industrial Filtration

Fluid filtration, fluid separation, oil mist separation, process filtration, and de-dusting in general, industries, ship maintenance, for large engines, in industrial vehicles, and in process technology.

GROWING DEVELOPMENT AND SYSTEMS COMPETENCE

In the global competitive environment, we use our increasing competence and performance to ensure that we can respond to future challenges with innovative solutions. In doing so, we think beyond the existing systems boundaries. Our strategic objective is to expand our position as technological leaders and, at the same time, to lead the way in terms of product and production costs on a global scale.

We are systematically expanding our competence in our core business of the combustion engine and engine peripherals. The engine know-how of MAHLE Powertrain (formerly Cosworth Technology) is making a decisive contribution to these activities. As a global development partner, we offer our customers new, integrated, and cost-optimized solutions. Our product and process know-how is available globally through networked, inter-disciplinary knowledge management in all regions and locations.

By expanding our research and development activities, we are strengthening the technological basis for dynamic development in the future. MAHLE now has seven research and development centers in Stuttgart, Northampton, Detroit (Farmington Hills and Novi), São Paulo, Tokyo and Shanghai. Approximately 2,300 development engineers and technicians worldwide are involved in fundamental research and ongoing development of the combustion engine. They work intensively on forward-looking new concepts, products, and systems, which lead to ecologically and economically sound solutions.

DOING BETTER—BENCHMARK FOR THE FUTURE

Yesterday's progress is today's starting point for completely new developments, which we initiate and accelerate. With passion for engines. With fuel in our blood. And with technical know-how. Good is not enough; our aim is to do better: pioneering technological excellence with a high degree of efficiency and consistent quality worldwide, down to the last detail. Allowing our customers to fully exploit the potentials.

Nothing demonstrates our technological leadership in more impressive style than the successes achieved in international motorsports: Vehicles with MAHLE engine components reliably hit the top spots time and again—in Formula 1 (FIA), the 24 Hours of Le Mans, the World Rally Championship (WRC), the German Touring Masters (DTM), the World Touring Car Championship (WTCC), the Formula 3 Euroseries, the Formula 3 Cup, and in North America at the American Le Mans Series, (ALMS). At the Dakar Rally, the NASCAR Nextel Cup, NASCAR Craftsman Truck, NASCAR Busch, Grand American Rolex, World of Outlaw Sprint Car, and the USAR Pro Cup. Our know-how gained from motorsports is often subsequently used in the development of new series-produced automobiles.

The global objectives of today and tomorrow are what move us. With our entire systems competence, we help to make engines even more efficient: optimized for reduced fuel consumption and emissions, for more performance, for a longer service life. We are thus expanding our position as technological leaders by means of continual growth.



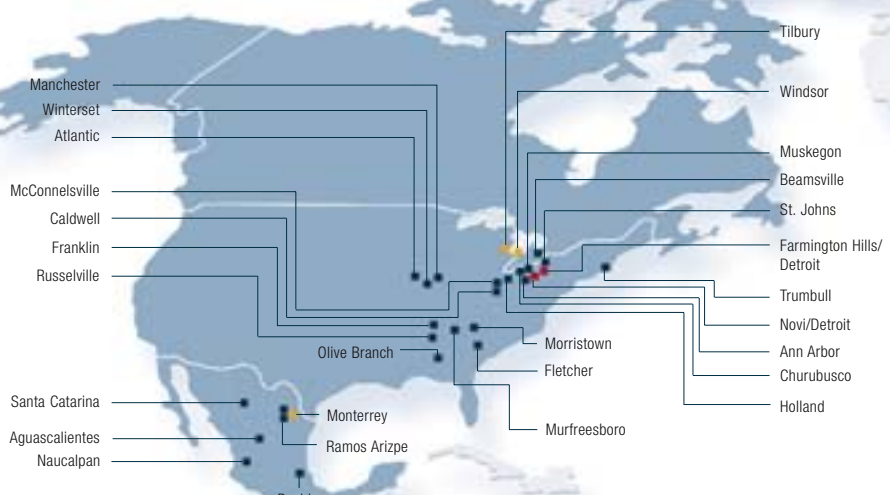
GERMANY

- Albershausen
- MAHLE Motorkomponenten GmbH
- Alzenau
- MAHLE GmbH
- Barsinghausen
- Kolbenring Barsinghausen GmbH
- Eislingen/Fils
- MAHLE Motorkomponenten GmbH
- Fellbach
- MAHLE GmbH
- Flintbek
- MAHLE AKO GmbH
- Gaildorf
- MAHLE Ventiltrieb GmbH
- Hamburg
- MAHLE NFV GmbH
- Leibertingen
- MAHLE Motorteile GmbH
- Lorch
- MAHLE Filtersysteme GmbH
- Markgröningen
- MAHLE GmbH
- Öhringen
- MAHLE Filtersysteme GmbH
- Plettenberg
- MAHLE Brockhaus GmbH
- Roßwein
- MAHLE Brockhaus GmbH
- Rottweil
- MAHLE GmbH
- Schorndorf
- MAHLE Aftermarket GmbH
- Stuttgart
- MAHLE Aftermarket GmbH
- MAHLE Filtersysteme GmbH
- MAHLE GmbH
- MAHLE International GmbH
- MAHLE Motorkomponenten GmbH
- MAHLE Motorteile GmbH
- MAHLE Ventiltrieb GmbH
- Wölfersheim
- MAHLE Ventiltrieb GmbH
- Wustermark
- MAHLE Ventiltrieb Brandenburg GmbH
- Zell im Wiesental
- MAHLE Ventiltrieb GmbH



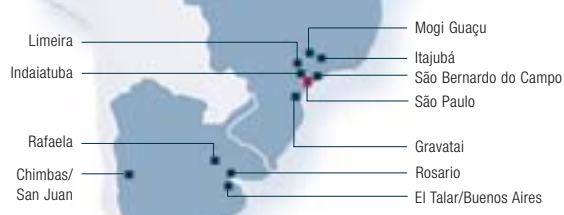
NORTH AMERICA

- Beamsville, CA
- MAHLE Clevite Canada, ULC
- Tilbury, CA
- MAHLE Filter Systems Canada, ULC
- Windsor, CA
- MAHLE Filter Systems Canada, ULC
- Aguascalientes, MX
- Sealed Power Autoparts, S.A. de C.V.
- Monterrey, MX
- MAHLE Sistemas de Filtración de México, S.A. de C.V.
- Naucalpan, MX
- Sealed Power Autoparts, S.A. de C.V.
- Puebla, MX
- MAHLE Sistemas de Filtración de México S.A. de C.V.
- Ramos Arizpe, MX
- MAHLE Componentes de Motor de México, S. de R.L. de C.V.
- MAHLE de México S. de R.L. de C.V.
- Sealed Power Autoparts, S.A. de C.V.
- Santa Catarina, MX
- Sealed Power Autoparts, S.A. de C.V.
- Ann Arbor (MI), US
- MAHLE Clevite, Inc.
- Atlantic (IA), US
- MAHLE Engine Components USA, Inc.
- Caldwell (OH), US
- MAHLE Engine Components USA, Inc.
- Churubusco (IN), US
- MAHLE Clevite, Inc.
- Farmington Hills/Detroit (MI), US
- MAHLE, Inc.
- MAHLE Technology, Inc.
- Fletcher (NC), US
- MAHLE Motorsports, Inc.
- Franklin (KY), US
- MAHLE Engine Components USA, Inc.
- Holland (MI), US
- MAHLE, Inc.
- Manchester (MO), US
- MAHLE Engine Components USA, Inc.
- McConnelsville (OH), US
- MAHLE Engine Components USA, Inc.
- Morristown (TN), US
- MAHLE, Inc.
- MAHLE Industries, Incorporated
- Murfreesboro (TN), US
- MAHLE Filter Systems North America, Inc.
- Muskegon (MI), US
- MAHLE Clevite, Inc.
- MAHLE Engine Components USA, Inc.
- Novi/Detroit (MI), US
- MAHLE Powertrain, LLC
- Olive Branch (MS), US
- MAHLE Clevite, Inc.
- Russelville (AR), US
- MAHLE Engine Components USA, Inc.
- St. Johns (MI), US
- MAHLE Engine Components USA, Inc.
- Trumbull (CT), US
- MAHLE, Inc.
- Winterset (IA), US
- MAHLE Filter Systems North America, Inc.



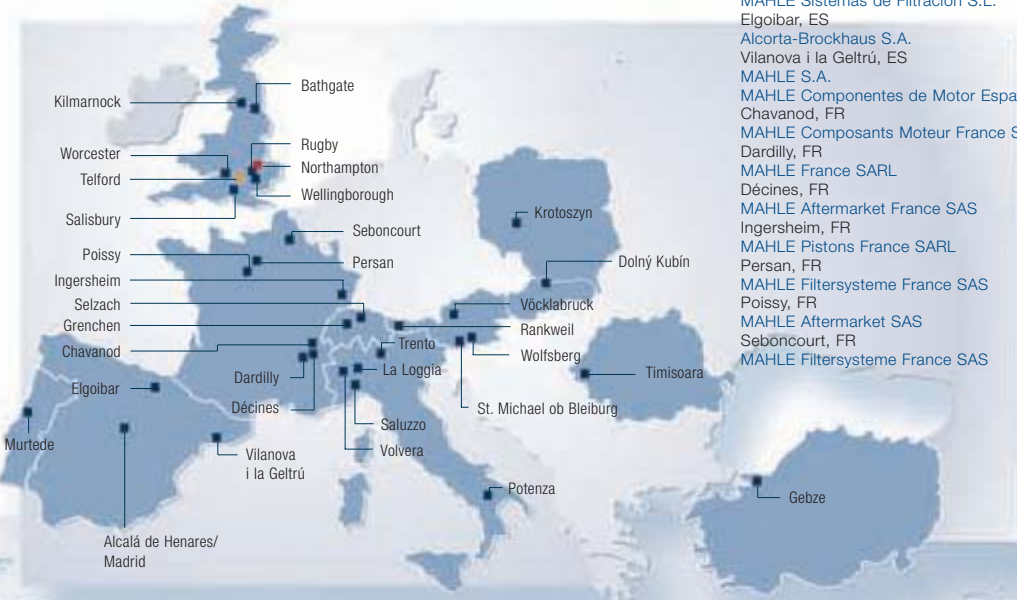
SOUTH AMERICA

- El Talar/Buenos Aires, AR
- MAHLE S.A. de Argentina
- Rafaela, AR
- Edival S.A.
- Rosario, AR
- MAHLE S.A. de Argentina
- Chimbas/San Juan, AR
- MAHLE S.A. de Argentina
- Gravataí, BR
- MAHLE Metal Leve S.A.
- MAHLE Indústria é Comércio Ltda.
- Indaiatuba, BR
- MAHLE Metal Leve Miba Sinterizados Ltda.
- Itajubá, BR
- MAHLE Componentes de Motores do Brasil Ltda.
- MAHLE Metal Leve S.A.
- Limeira, BR
- MAHLE Metal Leve S.A.
- Mogi Guaçu, BR
- MAHLE Metal Leve S.A.
- São Bernardo do Campo, BR
- MAHLE Metal Leve S.A.
- São Paulo, BR
- MAHLE Metal Leve S.A.



EUROPE

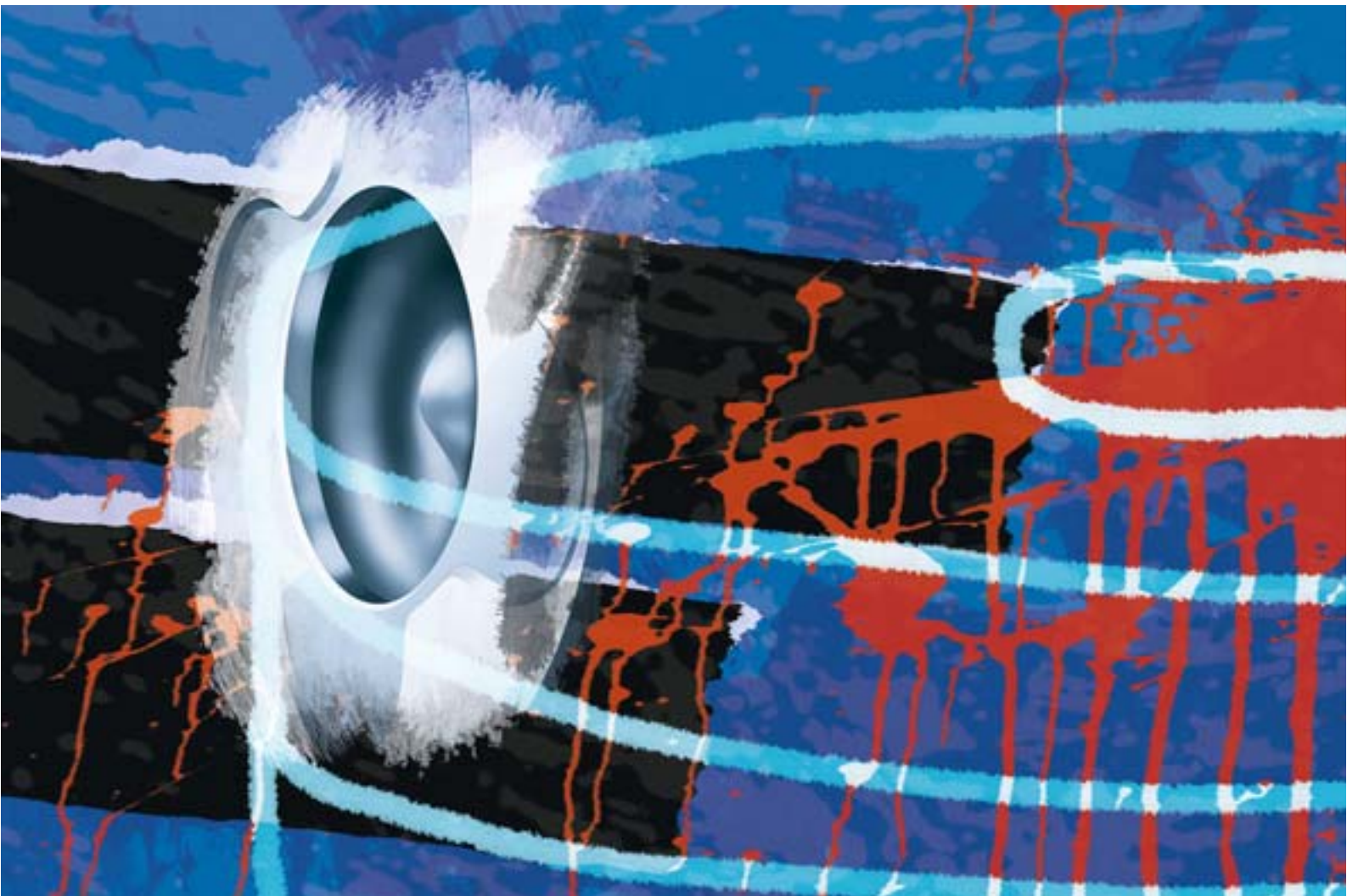
- Rankweil, AT
- MAHLE König Kommanditgesellschaft GmbH & Co
- St. Michael ob Bleiburg, AT
- MAHLE Filtersysteme Austria GmbH
- Vöcklabruck, AT
- MAHLE Vöcklabruck GmbH
- Wolfsberg, AT
- MAHLE Filtersysteme Austria GmbH
- Grenchen, CH
- MAHLE Motorkomponenten Schweiz AG
- Selzach, CH
- MAHLE Motorkomponenten Schweiz AG
- Alcalá de Henares/Madrid, ES
- MAHLE Sistemas de Filtración S.L.
- Elgoibar, ES
- Alcorta-Brockhaus S.A.
- Vilanova i la Geltrú, ES
- MAHLE S.A.
- MAHLE Componentes de Motor España S.L.
- Chavanod, FR
- MAHLE Composants Moteur France SAS
- Dardilly, FR
- MAHLE France SARL
- Décines, FR
- MAHLE Aftermarket France SAS
- Ingersheim, FR
- MAHLE Pistons France SARL
- Persan, FR
- MAHLE Filtersysteme France SAS
- Poissy, FR
- MAHLE Aftermarket SAS
- Seboncourt, FR
- MAHLE Filtersysteme France SAS
- Bathgate, GB
- MAHLE Engine Systems UK Ltd.
- Kilmarnock, GB
- MAHLE Engine Systems UK Ltd.
- Northampton, GB
- MAHLE Powertrain Ltd.
- Rugby, GB
- MAHLE Engine Systems UK Ltd.
- Salisbury, GB
- MAHLE Filter Systems UK Ltd.
- Telford, GB
- MAHLE Filter Systems UK Ltd.
- Wellingborough, GB
- MAHLE Powertrain Ltd.
- Worcester, GB
- MAHLE Powertrain Ltd.
- La Loggia, IT
- MAHLE Componenti Motori Italia S.p.A.
- MAHLE Valve Train Italia S.r.l.
- Potenza, IT
- MAHLE Componenti Motori Italia S.p.A.
- Saluzzo, IT
- MAHLE Componenti Motori Italia S.p.A.
- Trento, IT
- Glacier Vandervell Italy S.r.l
- Volvera, IT
- MAHLE Valve Train Italia S.r.l.
- Krotoszyn, PL
- MAHLE Polska Spolka z o.o.
- Murtede, PT
- MAHLE Componentes de Motores S.A.
- Timisoara, RO
- MAHLE Componente de Motor SRL
- Gebze, TR
- MAHLE Farplas Filtre Sistemleri A.S.
- Dolný Kubín, SK
- MAHLE Engine Components Slovakia s.r.o.



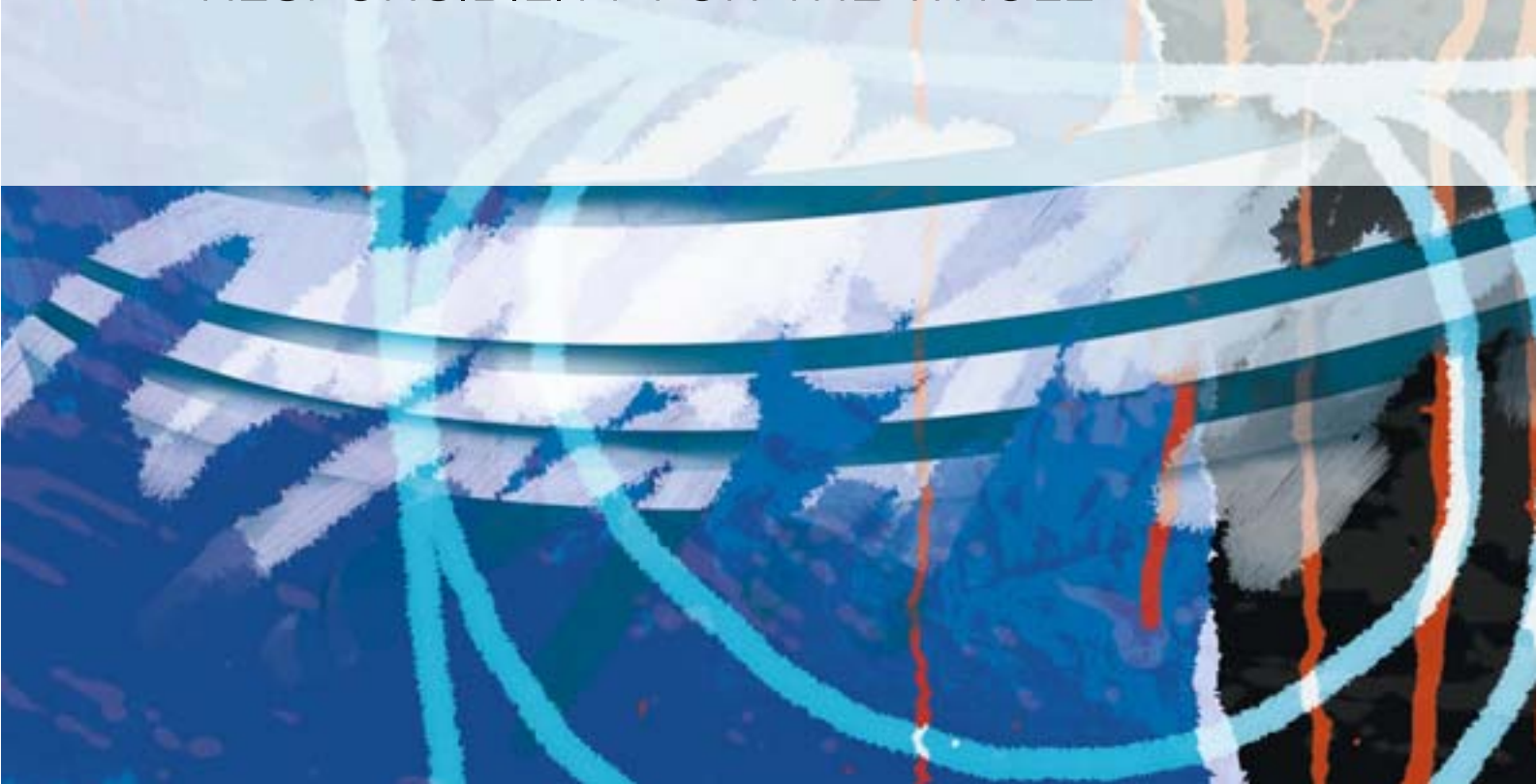
ASIA/PACIFIC

- Laverton North/Melbourne, AU
- MAHLE Engine Components Australia Pty Ltd.
- Changchun, CN
- MAHLE Donghyun Filter Systems (Tianjin) Co., Ltd.
- Chongqing, CN
- MAHLE Engine Components (Chongqing) Co., Ltd.
- Guangzhou, CN
- MAHLE Guangzhou Filter Systems Co., Ltd.
- Macheng, CN
- MAHLE Tri-Ring Valve Train (Hubei) Co., Ltd.
- Nanjing, CN
- MAHLE Engine Components (Nanjing) Co., Ltd.
- Shanghai, CN
- MAHLE Shanghai Filter Systems Co., Ltd.
- MAHLE Technologies Holding (China) Co., Ltd.
- MAHLE Trading (Shanghai) Co., Ltd.
- Tianjin, CN
- MAHLE Donghyun Filter Systems (Tianjin) Co., Ltd.
- Yingkou, CN
- MAHLE Bearings (Yingkou) Co., Ltd.
- MAHLE Engine Components (Yingkou) Co., Ltd.
- Gurgaon, IN
- Purolator India Ltd.
- Parwanoo, IN
- Purolator India Ltd.
- Pithampur, IN
- MAHLE Migma Private Limited
- Pune, IN
- MAHLE Filter Systems (India) Pvt. Ltd.
- Ishikawa, JP
- MAHLE Engine Components Japan Corporation
- Kawagoe, JP
- MAHLE Filter Systems Japan Corporation
- MAHLE Japan Ltd.
- Mooka, JP
- MAHLE Filter Systems Japan Corporation
- Nishimurayama, JP
- MAHLE Engine Components Japan Corporation
- Okegawa, JP
- MAHLE Engine Components Japan Corporation
- MAHLE Trading Japan Co., Ltd.
- Sakuragawa, JP
- MAHLE Filter Systems Japan Corporation
- Tokyo, JP
- MAHLE Engine Components Japan Corporation
- MAHLE Filter Systems Japan Corporation
- MAHLE Japan Ltd.
- Tsuruoka, JP
- MAHLE Engine Components Japan Corporation
- MAHLE Japan Ltd.
- Hwasung, KR
- MAHLE Donghyun Filter Systems Co., Ltd.
- Nam-Gu/Ulsan, KR
- MAHLE Donghyun Filter Systems Co., Ltd.
- Cavite, PH
- MAHLE Filter Systems Philippines Corporation
- Bangkok, TH
- MAHLE Engine Components (Thailand) Co., Ltd.
- Samutprakarn, TH
- MAHLE Siam Filter Systems Co., Ltd.

■ Locations
 ■ R&D centers
 ■ Siemens VDO Automotive (exp. from 2nd quarter 2007)
 as of April 2007



THINKING AHEAD
RESPONSIBILITY FOR THE WHOLE







WORLDWIDE RESPONSIBILITY FOR SOCIAL VALUES

MAHLE is a globally leading automotive supplier and therefore carries responsibility for society and the forces that affect it. We take this social and cultural obligation seriously and have been looking beyond the boundaries of the Company for many years. Throughout the world, we pursue the goal of providing benefit through our words and deeds and acting in such a way as to preserve and build on long-term values for people, cultures, and the environment. We link our success in the various regions of the world with the principle of sustainability. After all, we can only tackle future problems and create a society worth living in if we achieve a sensible balance between economic, ecological, social, and cultural needs.

PROVIDING BENEFIT – THE MAHLE FOUNDATION

Taking responsibility for public welfare is an active part of our corporate culture. In 1964, the Company founders Hermann and Ernst Mahle transferred their ownership of the Company to the MAHLE Foundation for public benefit, which has held almost all the Company's shares in trust since that time. MAHLE GmbH makes a dividend available to the MAHLE Foundation from the annual Group profit. We regard this as an important contribution toward playing a responsible, hands-on role in our community. The MAHLE Foundation serves charitable causes—by promoting health care, youth development and welfare, schooling, general adult education and vocational education, as well as organic farming. Since 1975, one of the key projects sponsored by the MAHLE Foundation has been the Filderklinik in Filderstadt-Bonlanden near Stuttgart, Germany. It combines modern, scientific orthodox medicine with holistic, anthroposophical medicine. Since 2004 alone, the MAHLE Foundation has donated EUR 8.5 million to date to support the extension and restructuring of the clinic. The details of this clinic extension and restructuring and the large number of other projects sponsored are presented in the MAHLE Foundation's own annual report. In addition, policy decisions were made in 2006 to provide increased support in the future for medical and social projects for activities in Brazil and other countries outside Germany. MAHLE GmbH provided the MAHLE Foundation with a substantial one-off sum to start up these activities.

RESPONSIBILITY BEYOND OUR BOUNDARIES

The Group is also involved in many countries and projects beyond the work of the MAHLE Foundation. Below are some examples of MAHLE's involvement in the various regions of the world.

Brazil: In 2006, we successfully continued the focal task of sponsoring socially underprivileged young people. These educational and health sponsorship projects rely primarily—as in all countries—on the voluntary commitment of our employees. In the future, the social aid programs already being run by MAHLE Metal Leve S.A. and MAHLE Componentes de Motores do Brasil Ltda. will be supplemented and augmented by cooperation with the MAHLE Foundation.

Germany: In 2006, MAHLE contributed to the “Jugendbegleiter” (“Youth Support”) program, for example, which supports young people in choosing careers and entering the job market. In 2007, the number of places for initial vocational training will also be increased in order to provide career prospects for even more young people. Numerous employees helped to give 20 young people from Brazil an unforgettable experience, sponsored by MAHLE during the soccer World Cup in connection with UNESCO International Youth Day. These disadvantaged young people are participants of our “Formare Program” in Brazil—a program that supports these young people during a very important stage of their lives and offers them additional opportunities.

Great Britain: MAHLE Powertrain Ltd. supported the British air ambulance service by providing a team to take part in the annual “Dragon Boat Race”. MAHLE Filter Systems UK Ltd. sponsored the “Elim Newlife Foundation”, a foundation involved in Prizren in Kosovo, whose activities include the provision of humanitarian and medical aid and support for the reintegration and training of returning refugees. MAHLE provided computers for education and MAHLE employees traveled to Kosovo to provide assistance on the ground in their free time.

North America: MAHLE supports the “United Way” organization, both through donations directly from the company as well as through employee payroll deductions. United Way sponsors regional charities, coordinates emergency services, mediates between collaborating organizations, and provides financial aid. In 2006, many MAHLE employees gave up a portion of their income and started a number of activities to raise donations for charitable organizations like United Way. In terms of the number of participants and amount of donations, MAHLE is a fantastic example to other companies in the USA. 33 projects were sponsored in 2006, from a retirement home to a soup kitchen.

Poland: In the 2006/2007 school year, MAHLE is helping to provide meals and clothing for children from less fortunate families. MAHLE provided financial aid toward medical care for severely handicapped children and the purchasing of orthopedic devices. In collaboration with the “Blood Foundation”, MAHLE also helped to finance bone marrow tests, for example. Help was also provided to disadvantaged children at the elementary school in Krotoszyn in cooperation with the “Children’s Friend Association”.

Portugal: In 2006, MAHLE supported activities to combat poverty and social exclusion through the “Integration into the regional social network” project, acting as a “friendly neighbor” by sharing responsibility for the local community.



Promoting health care is one of the main focuses of the MAHLE Foundation





CONTINUING TO DEVELOP
WITH NEW TECHNOLOGIES



SYSTEMATIC SOLUTIONS FOR THE FUTURE

In the area of combustion engines, the trend toward higher specific outputs and loads is continuing. This trend has various underlying causes; however, it is primarily due to the tightening of emission regulations and the need to sustainably reduce fuel consumption and CO₂ emissions.

In order to meet the increasing demands of the future, we are not only working on technologies to optimize the combustion process (direct injection, HCCI—homogeneous compression ignition, and downsizing concepts), but also act as a partner to our customers in the ongoing development of all essential engine components. Because of our systems know-how, we are increasingly approached about topics such as super charging, engine thermodynamics, and exhaust gas recirculation. To further optimize engine efficiency, we are intensively researching the reduction of friction losses. Different fuels, such as CNG (compressed natural gas), biodiesel, and flex fuel, along with new lubricating oil formulations, lead to new development activities aimed at media compatibility and wear resistance.

SYSTEMS COMPETENCE AND EFFICIENT PROCESSES

In the field of engine-related products, optimum solutions can only be achieved by carefully tuning the individual systems components. For a number of years, MAHLE has therefore increasingly focused on more intense analysis of entire systems rather than individual components. An all-inclusive analysis of the interactions is becoming increasingly important for optimizing running behavior as well as friction, wear and lubrication—particularly when it comes to the design of the components of the power cell unit (piston, piston rings, piston pin, cylinder liner, and connecting rod with bearings). We achieve this by adapting simulation tools, for example. Taking the design interactions for all relevant components—e.g., piston, piston pin, and connecting rod—into account, improved simulation approaches allow us to develop weight-optimized solutions, which could not be implemented if the individual components were analyzed separately.



Air impulse valve for dethrottling gasoline engines



Air impulse valve for increasing exhaust gas recirculation rates

In addition, we are now successfully using computer simulations for analyzing wear behavior. This is a newly developed simulation method, which takes the surface geometry and roughness of piston rings and cylinder liners into consideration.

By developing innovative coating concepts for our materials, we optimize the wear resistance of surfaces to meet higher requirements—for instance, in terms of reduced lubrication, oil dilution, and operating temperatures. In the development process, we use modern wear testing methods in the laboratory. Innovative examples include our PVD coatings for piston rings and piston pins as well as lead-free bearing coatings.

ENHANCED LOAD-BEARING CAPACITY AND OPERATIONAL SAFETY

In the area of materials, our high temperature-resistant aluminum alloys for gasoline and diesel pistons have become successfully established on the market. With optimized piston cooling, we offer a means to further increase the load-bearing capacity of pistons. Over six million of our passenger car diesel pistons with cooled ring carriers are now in use—this unique cooling technology is increasingly employed in new projects for future high-performance diesel engines in passenger cars.

EVEN BETTER UTILIZATION OF POTENTIALS

New material development: A powder metal material infused with copper for valve seat inserts was prepared for series production in 2006 for CNG-type passenger car engines. With a wear- and heat-resistant matrix and a wear-resistant intermetallic phase, this material offers significant advantages under extreme operating conditions.

Production and process technology: In 2006, we were able to introduce a number of improvements. For example, a roller-burnishing process with improved manufacturing quality was developed for pressure rolling the high-performance fillet radius on the flanges of cylinder liners.

New telemetry system: The newly introduced system allows component temperatures in the operating engine in the range above 450°C to be determined reproducibly with great precision. These temperatures occur in the combustion chamber of the MONOTHERM® steel pistons, which are subject to high loads. The potential of the MONOTHERM® piston, which has been in series produc-



Transmission for the MAHLE SAE engine



Valve lift switch or shut-off of roller-type cam followers in the valve train for cylinder deactivation



tion for several years, has by no means been fully exploited. We anticipate that the ongoing development of this piston type will offer us an excellent opportunity to meet the requirements of new emission regulations, such as EU5 or US10.

In the area of cylinder components, we have further expanded our systems approach for the development of assemblies. We gained important knowledge about the systems properties of piston rings and cylinder liners for heavy commercial vehicle engines. In order to lower the weight of the power cell components, we extended the simulation to all relevant components, including the connecting rod. In the future, the ongoing development of coating systems for a variety of components subject to wear will become increasingly important for our customers.

In connection with fully variable valve train adjustment concepts, we are testing switchable roller-type cam followers. The CamInCam® camshaft systems have now been put into series production. They enable variable valve timing, even with a single camshaft in the engine. An additional valve lift setting feature will be the next modular step in this direction. Our fast-switching air impulse valve can be used as a system for the dethrottling of gasoline engines. This allows dethrottling without interfering with the valve train. Advantages can also be created in terms of cold start characteristics and internal exhaust gas recirculation, as well as support for supercharging systems. We are intensively researching the future low-pressure exhaust gas recirculation design, so that high exhaust gas recirculation rates can be achieved with an innovative product, even under unfavorable pressure conditions.

AIR MANAGEMENT SYSTEMS: CUTTING-EDGE INNOVATIONS

In order to reduce oil consumption and comply with more stringent emissions legislation, the Air Management Systems product line is setting standards with novel oil mist separators integrated into the crankcase ventilation system. Cost-effective passive impactors, which can be integrated into the cylinder head covers, are used in this design. Our first active electric disk separator worldwide met with great interest among our customers, particularly in view of the extreme requirements in the commercial vehicle sector. In 2006, we successfully started series production of plastic cylinder head covers with integrated oil mist separation and pressure regulation.

Another milestone in the development of intake modules is the commencement of series production of a new three-stage resonance-charged intake module. The two integrated, electrically operated valve actuators using innovative molded-in assembly technology are MAHLE's first electrical actuators developed and produced in house—making a crucial contribution to our systems competence and increasing added value. Other new customer projects for MAHLE mechatronics components are already in the series production development phase.

INTEGRATED, ECONOMICAL MODULAR SOLUTIONS

MAHLE has been developing highly integrated modular solutions in the Liquid Management Systems product line for many years. Significant progress in design and construction was made through weight-optimized and cost-effective modules with added functionality. Innovative all-plastic oil filter modules, in which the integration of the oil/water heat exchanger is particularly important for the entire module, already account for a significant market share. The elimination of several machining steps in comparison with aluminum high-pressure die casting housings and increased vertical inte-

gration during internal production increase the added value and process reliability of these assemblies. Series startups of all-plastic oil filter modules are planned in various regions in the near future.

Another innovative product brought into series production is the MAHLE oil pan top, which integrates oil filtration and engine oil cooling and is inserted between the crankcase and the oil pan. This opens up new design possibilities for the lubricating oil circuit and the positioning of components affecting the oil circuit, and thus allows flexible solutions that utilize the package constraint even more efficiently.

NETWORK OF ENGINEERING SERVICES

MAHLE Powertrain provides support in the search for intelligent, environmentally friendly solutions that conserve raw materials and energy, including complete engine development and component production. Innovations such as complex electronic control units and fully variable valve train systems are important contributions. Another key advancement is our fundamental research in the field of mechanical friction losses using a newly installed high-precision, high-resolution test bench for motored and live engines.

The analysis of different supercharging systems, accompanied by direct injection and downsizing of components, promises considerable potential for reducing fuel consumption and CO₂ emissions.

In order to verify new ideas and innovative technologies on the live engine, we use 78 engine test benches installed worldwide, supplemented by eight chassis dynamometers, allowing us to conduct detailed analyses of the component behavior by means of special gaging methods developed in house. Thanks to the international network of MAHLE research and development centers and the teamwork among experts from the different product lines, we are able to solve new problems comprehensively, competently, and highly efficiently.



Modern test benches provide precise measurements for the optimization of the entire system



Analytical and simulation tools for shorter development times



Systems responsibility from the initial concept to series production





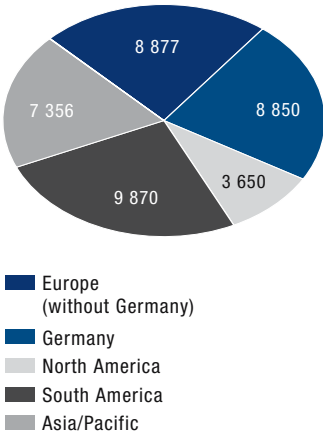
WINNING
THROUGH TEAMWORK





PROMOTING INTERNATIONALIZATION, PURSUING SHARED GOALS

**38,603 employees worldwide
as of Dec. 31, 2006**



In recent years, the MAHLE Group has developed continuously as a result of the commitment of its employees. Today, we are established globally, with our executives, comprehensive processes and systems, and excellent specialists in all functional divisions. We see globalization and development in our markets as an opportunity and a challenge, which should be transformed consistently into success with positive impetus and a great deal of energy. As of 2007, as a result of new acquisitions, approximately 47,000 employees in 24 countries on four continents epitomize our international orientation. With this structure, we support customers across the various time zones by providing competent local contacts and leading technological know-how. The high proportion of employees in Asia and South America and the expansion of our local engineering competence strengthen our presence in these growth regions. In spring 2006, another research and development center was opened in Shanghai, China, and the Chinese engineers trained in Germany and Japan are today collaborating successfully with colleagues throughout the world. With regionally established structures and local production facilities, we can reach the strong growth areas of the global economy directly, without neglecting the established, and still very important, traditional automotive regions in Europe and North America.

WORLDWIDE DIALOG WITH THE EMPLOYEES

Modern, sustainable organizational structures form the basis for successful work. To verify the efficiency of our Group structures, we conducted an Internet-based employee survey in our worldwide sales organization and among its internal interface partners, which recorded a pleasingly high participation rate. Immediately afterwards, working groups in each region of the world analyzed the results and formulated suggestions for optimization. International employee surveys form an important instrument and are now an integral part of our human resources work. Employee surveys enable us to continuously improve working conditions and organizational aspects, in order to increase and safeguard employee motivation for the medium and long term.

EXECUTIVE MEETINGS PROVIDE IMPETUS

For several years, we have made specific use of International Executive Meetings to communicate our strategic goals, undertake operational planning, and form networks. Through these meetings, concrete projects can be promoted. Subjects include, for example, inventory optimization programs or the strategic positioning of production plants. In addition, specific discussions of advanced development projects and strategic purchasing policy were the focus of attention. During the year under report, these meetings also focused on more general topics, such as executive development, the formulation of our MAHLE Mission, and discussion of the core brand values.

In the MAHLE Mission, we have put into writing—in 16 key statements—our basic values for a mobile future. This shared commitment to paramount values is a point of orientation and anchoring for all divisions of the Company. It can be called upon time and again by the whole organization as

a reference point. In addition to this, we develop effective working methods, remuneration and working hours models, which should guarantee maximum motivation and dedication to performance. This is noticeable to our customers and business partners as they collaborate with us throughout the world.

WORLDWIDE COMMUNICATION PLATFORMS

We have further expanded our global information networks, which support the work of our employees. For example, they are used to control the product development process in development networks spanning several countries. Our open communications policy is also implemented via Internet- and Intranet-based tools, and our employee magazine "MAHLE global" is now available to all employees worldwide in eight languages on the MAHLE Intranet, in all its regional editions.

What applies within the company is also reflected externally: from the modern Internet presence and our customer magazine "MAHLE Performance" for the original equipment market to "MAHLE News" for the aftermarket. For us, transparency, openness and accessibility for employees, customers, and the interested public are values that we embody and that characterize us.



Worldwide cooperation in globally networked expert teams

Looking to the future with committed specialists and executives





Challenging and promoting employees, building qualifications, networking knowledge

TRAINING AND LIFELONG LEARNING

We place a high value on promoting lifelong learning. In annual employee dialogs, supervisors and employees exchange information, determine qualification requirements, and prepare to deal with future tasks and changes. We support lifelong learning by offering a range of qualification activities specifically designed to meet the needs of our executives and employees. New concepts and on-the-job-learning methods with computer-assisted learning platforms are also used to convey necessary specialized knowledge. Several groups of our international trainees in Germany and abroad are implementing this learning method with great success. Through our Key University Program and our own Company network, we offer students in various fields of study the opportunity to complete national and international internships.

The dual training system is not only a suitable model for Germany. The significant expansion of our vocational education activities, e.g., in Mexico, illustrates this. In Germany, we are increasing the number of apprenticeship places by around eight percent in 2007. A total of 120 new apprenticeship agreements are being concluded for dual vocational training and training in universities of cooperative education "Berufsakademien". In 2006, around 400 young people completed their vocational training with MAHLE in Germany and laid the foundation for their future career. At the same time, we guarantee our ability to recruit qualified junior specialists for our technically advanced production processes.

ATTRACTING AND DEVELOPING JUNIOR EMPLOYEES AND EXECUTIVES WORLDWIDE

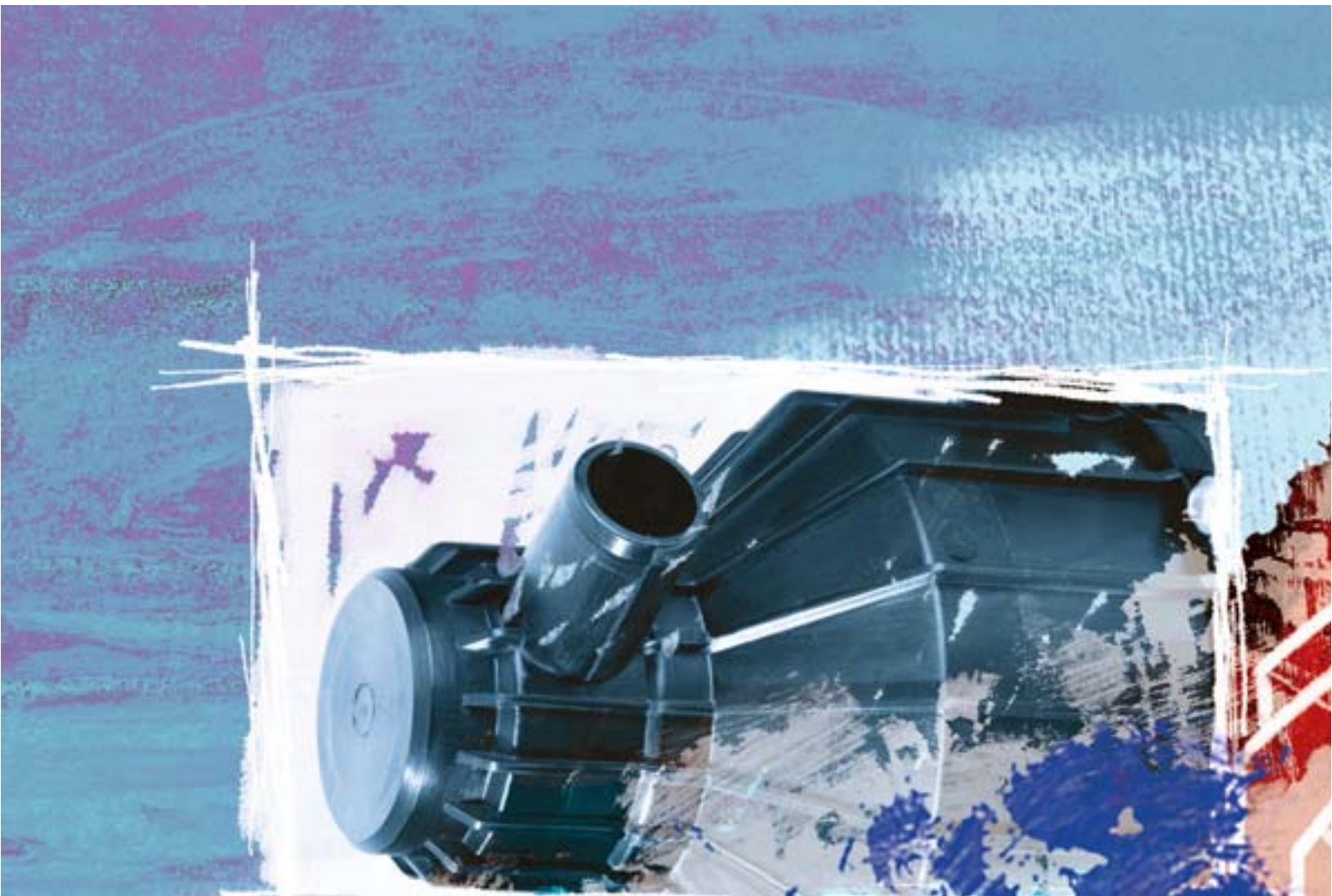
We are strongly committed to promoting and safeguarding the recruitment of junior employees with college and university educations. We are intensifying contact with major colleges and universities on the basis of our personnel marketing concepts. We are regularly involved with career fairs and organize several series of events for student groups in house and at fairs, e.g., at international motor shows. In addition, we support Formula Student (SAE)—the international construction competition among colleges and universities for prospective engineers—both in its competitions and with engines specially developed at MAHLE for these sporting and competitive events. In 2007, four colleges and universities from Germany and the USA will take part in these SAE competitions with MAHLE engines. Alongside direct entry into a specialist role, our International Trainee Program forms an ideal platform for attracting junior employees. We specifically develop our management trainees by means of support programs, which normally include international placements.

In 2006, we also started the International Development Program at Group level. It brings together high-potential employees from middle management who are willing to travel abroad to continue their professional development. The objectives of the program are to learn together, strengthen intercultural understanding, and work on real projects as part of an international team. Also in 2006, a worldwide internal job board for specialists and executives was introduced on the Intranet. It provides new opportunities for professional development across national borders and product lines. We are comprehensively expanding the specialist and leadership competence, based on the MAHLE Leadership Model, by means of long-term collaboration in qualification networks on a national and regional basis in all continents.

COOPERATION AS A BASIS FOR SUCCESSFUL COLLABORATION

The willingness to cooperate in a spirit of trust with the employee representatives is one factor that guarantees the constructive and successful ongoing development of the Group across the globe. It forms a basis for fair compromise even where there are differing interests. Economic conditions and cost increases resulted in a need for extensive cost reductions, which could not be achieved by productivity improvement measures alone. In most cases, thanks to the good and efficient cooperation of the internal partners, we were able to make the necessary adjustments by means of reasonable solutions that illustrated a sense of responsibility for the whole Company. As part of our corporate culture, this ability to strike a balance—together with technological innovative strength—safeguards the future of the Group and, ultimately, helps to preserve jobs. After all, in the long term, only competitive jobs are secure jobs.

The Management Committee would like to express its thanks to all employees for their proven willingness to perform, their readiness to cooperate across national borders and specialist areas, and the successes they have achieved. Successes that make us proud and allow us to look positively toward the future.



TAKING QUALITY TO THE NEXT LEVEL







QUALITY MANAGEMENT FOR BETTER PRODUCTS AND PROCESSES

The demands on the quality of our products and processes are growing with the changing technologies, markets, and requirements of our international customers. MAHLE quality management uses Group-wide standards to ensure consistent quality over the whole process chain—from prevention in product and process development to analysis of causes.

HIGHER QUALITY THROUGH PREVENTION

We make use of comprehensive preventive instruments and quality assurance measures in the development of new products and processes. Targeted prevention means that potential risks and reoccurrence of problems in ongoing production can be avoided to a large extent. In order to optimize the existing approach, which is geared toward established customer requirements, we formulated an improved quality management system with Group-wide prevention standards in 2005. After the system had been in use for a year, the results were assessed in 2006 and, on this basis, further optimizations were developed and integrated into the MAHLE quality management system. As a result, MAHLE was able to offer even higher standards throughout the world by the end of 2006.



High quality standards through leading-edge testing technologies and continuous improvement of processes within the team

HIGHER QUALITY THROUGH CONTINUOUS IMPROVEMENT

We also optimize our continuous improvement processes time and again. An international working group assessed the existing instruments for continuous improvement. The best practices compiled in 2006 were identified and then made available worldwide. The following instruments were selected for expansion to a worldwide Group standard: improvement projects, workshops, and suggestions for improvement.

We undertake improvement projects over a set—usually fairly long—period of time within a project structure. Everyone involved in the project pursues a goal clearly defined by the management. A project plan, including milestones for monitoring the progress of the project, is drawn up. An improvement project is considered to have been successfully completed if the effectiveness of the measures introduced can be demonstrated.

Workshops are held by the employees within a business unit, e.g., Production, Development, or Logistics. In their initial phase, the workshops are supported by a moderator. The employees form a team that holds improvement workshops at regular intervals. The objective of these workshops is also set by management, and the progress toward the goal is reassessed at each workshop. The team is responsible for introducing the necessary measures. If required, the management or other business units are brought in to provide support. In this way, we are able to frequently achieve significant progress in the area of quality.

Employees' suggestions for improvement are an absolutely essential part of this concept. Whereas improvement projects and improvement workshops focus on set objectives, employees can contribute in an entirely personal way to the continuous improvement of the Company by submitting their own suggestions.

Together with the Corporate Quality Management, the quality managers of the product lines assess the results produced worldwide by the three instruments for continuous improvement in order to identify the best practices. The methods and tools for the best practices can be accessed via a quality management platform on the internal MAHLE network. The methods and tools are then selected and used on site by the quality managers of the plants and profit centers.



ENVIRONMENTAL MANAGEMENT AND SAFETY AT WORK IMPROVED

MAHLE is also one of the leaders in the automotive supplier industry in the area of environmental protection. We believe that reconciling technical progress and the future of society with our environment is one of our most important tasks. For this reason, our environmental protection and safety at work strategy is oriented globally at all locations.

ENVIRONMENTAL MANAGEMENT: 90% OF MAHLE LOCATIONS ENVIRONMENTALLY CERTIFIED

By becoming involved with environmental management in 1996, MAHLE laid the foundation for continuous environmental protection standards, which have been developed on an ongoing basis since that time. In 2006, ten years on, 90% of all MAHLE locations have been successfully certified in accordance with DIN EN ISO 14001 and/or EMAS II. This represents an increase of 10% in comparison with 2005, which was achieved as a result of further locations being successfully certified in Japan, India, and China. Bearing in mind the increasingly strict environmental regulations worldwide, we undertake all measures and appropriate investments at an early stage, and will continue to do so, in order to maintain parameters at or below thresholds for production-related processes. We are achieving consistent progress with our international certification rate and our commitment to environmental protection. Further locations are being prepared for certification—our goal for the immediate future is to be 100% committed to the environment.

SAFETY AT WORK AND HEALTH CARE

We are making further improvements to our internationally high standards in safety at work, accident prevention and health care by means of training and both internal and external audits. In 2006, we were able to further reduce the accident rate at the MAHLE locations in Germany. MAHLE now falls 20% below the average for German industry as a whole. In Great Britain, MAHLE Filter Systems UK Ltd. received the coveted Five Star Health and Safety Audit Award of the British Safety Council in February 2006 for its health and safety management system. Five stars represent the highest possible award, and the underlying safety criteria are among the most comprehensive worldwide.

USE OF RAW MATERIALS SIGNIFICANTLY REDUCED

In our plant in Öhringen, Germany, a package of measures enabled us to save valuable resources—178 tons in total—in 2005 and 2006. For example, the waste produced during startup of injection-



Integrated environmental management for our global locations

molding machines was decreased, the number of defective plastic parts was systematically reduced, and sprues of injection-molded parts were reground directly at the machine and added to the fresh resin. After customer approval, we were also able to use more than 200 tons of recycled resin in place of new resin.

ENERGY MANAGEMENT SYSTEM ESTABLISHED FOR GERMAN PLANTS

In view of the rising energy costs and the general unpredictability of German energy policy, MAHLE launched a systematic concept, consistent across the Group, for an in-house energy management system generating potential savings of 10% per year.

MODERN ENVIRONMENTAL TECHNOLOGY FOR NEW MONOTHERM® STEEL PISTON PRODUCTION LINES

In our plant in Rottweil, Germany, two production lines for MONOTHERM® steel pistons were fitted with a closed fully automated system for chip disposal and emulsion recirculation. This allowed us to significantly reduce coolant consumption and cooling costs. In addition, a new heat exchanger with external air cooling decreased the energy consumption required to cool the emulsion.

REDUCED ENERGY CONSUMPTION AT MAHLE, INC., MORRISTOWN, USA

In the MAHLE plant in Morristown, USA, gas consumption was dramatically reduced, costs were saved, and a substantial environmental benefit was achieved by periodically shutting off an industrial boiler heated by natural gas. The boiler supplied hot water to the cafeteria, shower rooms, and washrooms and heated the heat exchangers for hot air blowers. By installing four electric boilers for the supply of hot water and a smaller, lower-consumption water pump for the hot air blower for use in the summer, the natural gas boiler could be shut off for almost five months from March to October 2006, subject to weather conditions. The result: a saving of 198,240 cubic meters of natural gas and a cost saving of around USD 57,000. In addition, the total pollution emissions were reduced by more than 256 kilograms.

RECYCLING RATE FOR BATTERIES INCREASED TO 64%

Within a period of two and a half years, the battery recycling rate at MAHLE, Inc., Morristown, USA, was increased from 24% to 64%. The proportion by weight of recycled alkali batteries grew by almost 79% during this period.

MODERN WASTE WATER TECHNOLOGY FOR CHINA

The rapid growth in the Chinese market places a special obligation on MAHLE to protect the environment. By constructing a modern waste water treatment plant with the latest filter technology and neutralization at our plant in Yingkou, we made an important contribution to water pollution control and the establishment of improved environmental standards in China.





GROWTH: OUR DIMENSIONS FOR THE FUTURE

Growth means strength. For our customers. We're growing dynamically. Worldwide. With leading technological competence and strategic acquisitions, we are sharpening our competitive edge. The improved performance is an important step on the way to becoming the global market leader.

INCREASED GROWTH: ENGINE PARTS GROUP OF THE DANA CORPORATION

Dana Corporation, engine parts group

- 25 production plants in 11 countries
- Around 5,000 employees
- Sales of USD 659 million in 2006

By acquiring the engine parts business of the American automotive supplier Dana Corporation with its headquarters in Toledo, Ohio, in the first quarter of 2007, we expanded our worldwide market position, particularly in the areas of piston rings and engine bearings, as well as in the free trade business for engine components. The main products are piston rings, engine bearings, cylinder liners, and camshafts, which are also sold in the independent aftermarket under the brand names Perfect Circle®, Clevite®, and Glacier Vandervell™.

The acquisition comprises all units of the Dana engine components group worldwide, including the Clevite® trading organization, with production plants in the USA, Canada, Mexico, Argentina, Brazil, Germany, France, Great Britain, Italy, Slovakia, and Spain. The additional agreements concluded as part of the transaction include an agreement granting MAHLE the exclusive right to distribute the products sold under the brand name Victor Reinz® in the free trade business in the USA and Canada.

The next step for us is to integrate the added potential into the existing MAHLE network and exploit all synergy effects throughout the value chain, from purchasing, production, and product development through to sales, marketing, and administration.







INCREASED GROWTH: AIR INTAKE MODULES AND AIR FILTRATION BUSINESS DIVISION OF SIEMENS VDO AUTOMOTIVE

With the expected acquisition of the business segment intake modules and air filtration for combustion engines of Siemens VDO Automotive, we will expand our technological portfolio and significantly strengthen our global presence in this product segment. This strategically important step allows us to supplement our technology and win new customers, particularly in the American and Asian markets.

Siemens VDO Automotive, intake modules and air filtration business segment

- 6 locations in Canada, Mexico, Great Britain, and China
- Around 1,000 employees
- Sales of around EUR 300 million in 2005/2006

At the same time, this helps us to optimize and focus our global network for production and development in this business segment. Together with organic growth and the existing MAHLE activities, we will be able to improve our sales in this business segment to considerably more than EUR 1 billion, which will further increase the significance of air management and air filtration systems within the MAHLE Group.

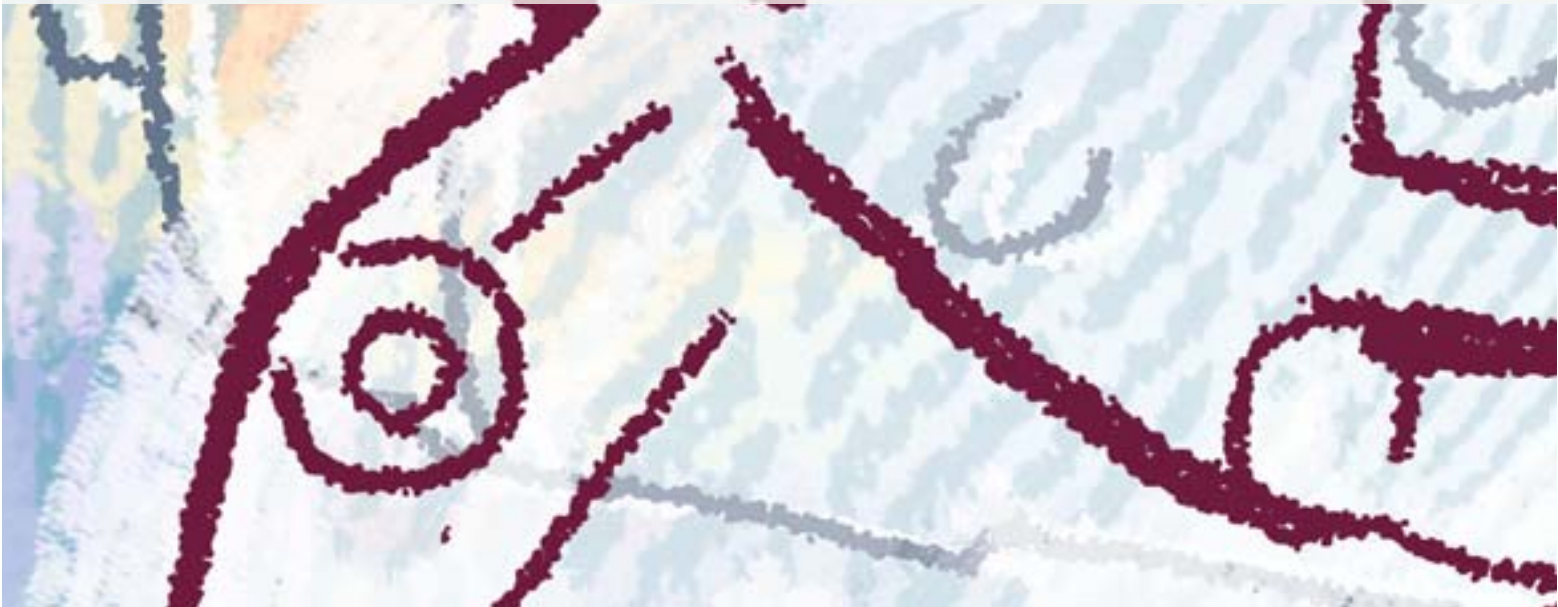
INCREASED GROWTH: GLOBAL EXPANSION OF THE ENGINE VALVES PRODUCT GROUP

Even stronger in Asia and South America: In January 2007, we expanded our valve train activities by means of a majority joint venture and the opening of the new plant MAHLE Tri-Ring Valve Train (Hubei) Co., Ltd. in Macheng, China. MAHLE Tri-Ring Valve Train is already the MAHLE Group's eighth production plant in China. We took a further step toward strengthening the Valve Train Systems product line by acquiring the valves company Edival S.A., Rafaela, Argentina. The company has all the necessary technical processes to manufacture passenger car, commercial vehicle, and motorsport valves, as well as valves for small engines, and generates the majority of its sales through exports to the NAFTA region and Europe. More than 30 million engine valves are produced annually at the two new locations.

**MAHLE Tri-Ring Valve Train (Hubei) Co., Ltd., Macheng, China
Edival S.A., Rafaela, Argentina**

- 1 location in China
- 1 location in Argentina
- Around 2,400 employees
- Sales of around USD 55 million in 2006







GRASPING
THE SITUATION CLEARLY



STATUS REPORT

GLOBAL ECONOMY EXPANDS UNAFFECTED BY HIGHER ENERGY PRICES

With an increase of 3.9% in the gross domestic product (GDP) in 2006, the global economy continued the positive development it has sustained for three years. Low real interest rates and higher employment in many national economies significantly strengthened consumer confidence and consumer spending worldwide. International trade, which expanded by 8.9%, also provided valuable support to the global economy. While energy prices and raw materials led to a price push that could not be passed on completely to the producer and consumer markets, rather moderate wage rises lessened the increase in the price level. However, the increased crude oil prices contributed to the intensification of global imbalances in the trade balance. While the oil-producing countries generated the majority of the surpluses worldwide, the rise in the cost of energy for oil-importing countries reduced the trade balance significantly.

In the euro zone, the growth of the gross domestic product significantly exceeded the previous year's rise, with 2.7% in 2006. The economic recovery in Germany provided impetus to the economies of the other member states. Exports, which underwent a further 8.7% increase, were the driving force of the economy. However, private consumption also expanded more strongly than in the previous years, with growth of 2.1%. This increase was primarily attributable to the stabilization of development on the job market. The unemployment rate reached 7.9%, its lowest value since 2001.

In the United States, private consumer spending weakened, exerting a limiting effect on the gross domestic product. In addition, the economic development weakened to 3.3%, as increases in energy prices and the interest rate level were also accompanied by a cooling of the residential real estate market. Having risen further to USD 890 billion—primarily as a result of oil imports—the trade balance deficit continues to pose a risk for the economic development of the USA.

Through regional primary production, the economy in the countries of Latin America benefited from the high raw material prices and the increase in domestic demand. In addition, the economic upturn was boosted by interest rate reductions as well as lower rates of inflation. In contrast, the upward revaluation of the real had a relatively moderate effect on the economic development of Brazil.

In China, the growth of the gross domestic product in the year under report amounted to 10.6%, once again exceeding the high increases of the previous years. Gross investments into fixed assets were the driving force once again, with a rise of 18%. However, increases in exports and private consumption also made a noticeable contribution to the upturn. As a result of the high trade balance surplus, the currency reserves of the Chinese yuan grew significantly once again and the upward pressure on the yuan, which is still not freely convertible, remained high.

Despite the heavy strain resulting from the increase in oil prices, India's gross domestic product rose by 8.3%. This increase was supported by exports, primarily of industrial goods, which recorded a rise of over 20% in only the third year.

The Japanese economy expanded for the fifth consecutive year, with growth of 2.8% in the gross domestic product. Supported by the devaluation of the Japanese yen, exports increased significantly. As a result of increased consumer prices, the Japanese central bank was able to end its “zero interest rate policy” after more than five years and establish an interest rate of approximately 2% for bond rates.

GLOBAL AUTOMOTIVE INDUSTRY ON COURSE FOR FURTHER EXPANSION

In 2006, the automotive industry was also able to benefit from the dynamic development of the global economy. The worldwide production of passenger cars and light commercial vehicles increased by 4.1% to 66.3 million units, primarily as a result of the higher demand in the BRIC countries (Brazil, Russia, India, and China). The manufacturers of passenger cars were able to achieve a volume increase of 6.6% to 42.9 million units, while light commercial vehicles remained at the previous year's level with 23.5 million units.

In Europe, the production of passenger cars and light commercial vehicles increased by 2.6% to 20.7 million units. Passenger car production rose by 2.1%, corresponding to 350 thousand units, to 16.9 million vehicles. At the same time, the manufacturing of light commercial vehicles was expanded by around 200 thousand units to 3.9 million vehicles. The growth of European production was caused by the rise of 16% in the output capacities of the Central and Eastern European plants. The new Toyota/PSA plant in the Czech Republic, as well as the increasing production in Slovakia, Russia, Romania, and Ukraine, contributed in particular to this rise. In contrast, the number of passenger cars and light commercial vehicles manufactured in Western Europe decreased by just under 0.2 million units to 15.8 million vehicles. Only Italy (15%) and Germany (1.5%), the two notable growth markets in this region, compensated for the declines in Great Britain (-8.4%), France (-7.2%), and Sweden (-6.9%). The market share of vehicles with diesel engines in Europe increased further. The proportion of diesel vehicles rose from 46% in the previous year to more than 47% in 2006.

Worldwide automobile production

Number in 1 000s

	2005	2005	2006	2006
	Passenger cars & light comls.	Commercial vehicles (incl. buses)	Passenger cars & light comls.	Commercial vehicles (incl. buses)
America	18 478	755	18 297	813
NAFTA	15 746	593	15 265	648
South America	2 732	162	3 032	165
Asia/Pacific	23 476	1 132	25 589	1 307
Japan	10 440	360	10 970	406
China	5 142	500	6 590	575
Europe	20 213	596	20 731	625
Germany	5 583	169	5 667	175
Other countries	1 534	0	1 718	0
Total	63 701	2 483	66 335	2 745

Source: Global Insight, March 2007



In North America, relatively high fuel prices, smaller price reductions, and the failure of Ford, General Motors, and Chrysler to align their product ranges with the market had a substantial impact during the second half of the past year. As a result of production cuts to reduce the extensive stocks, the production of passenger cars and light commercial vehicles remained 0.5 million units below the previous year's level at 15.3 million units. Pickup trucks and sport utility vehicles, which have particularly high fuel consumption, are suffering the full impact of this decline. The proportion of these vehicles decreased from 58% in 2005 to 54% in 2006. The Asian manufacturers made a disproportionately strong contribution to the increase in passenger car production and the rising demand for smaller vehicles with lower consumption.

In South America, falling interest rates and a solid domestic economy more than compensated for the effects of the upward revaluation of the Brazilian real. In view of the continuing rise in demand, the production of passenger cars and light commercial vehicles grew by 11% to 3 million units.

In Asia, the production of passenger cars and light commercial vehicles increased by 9% to 25.6 million units. This development was primarily driven by the continuing boom in the Chinese automotive market, in which the production of passenger cars and light commercial vehicles rose by a further 28.1% to 6.6 million units. The Chinese automotive industry thereby displaced Germany from its position as the third largest automobile manufacturing country worldwide. In contrast, a significantly smaller increase in production was recorded by Japan with 0.5 million, India with 0.3 million, and Korea with 0.1 million additional units.

The production of medium-weight and heavy commercial vehicles also developed more positively than expected at the beginning of the year, increasing by 10.5% to around 2.7 million units worldwide in 2006. In Western Europe, the production figures for commercial vehicles rose by 4.5% overall to 475 thousand units, primarily as a result of the growth of 17.9% in France. The production volume in Germany, Europe's largest commercial vehicle manufacturing country increased by 3.7% to 175 thousand units. Sweden and Spain recorded declines as high as -1.2% and -1.1% respectively in commercial vehicle production. In the Central and Eastern European countries, the 5.6% increase in the production of medium-weight and heavy commercial vehicles to 150 thousand units was primarily caused by the rise in production in Russia and Belarus.

In the NAFTA region, the commercial vehicle production volume grew by 9.3% to 648 thousand units. Heavy commercial vehicles over 15 tons made a disproportionately large contribution of 11.7% to this volume. The main cause of this production increase of 40 thousand units in the past year was the fact that some purchases were brought forward because of the tightening of the EPA 07 exhaust gas legislation in 2007, which will lead to a noticeable cost push.

Commercial vehicle production by manufacturers in South America slightly exceeded the previous year's value, with 165 thousand units. In particular, this was caused by the increased production in Columbia and Venezuela, as well as the large manufacturers' new strategy of using Brazil as a production base for exports to developing and emerging markets.

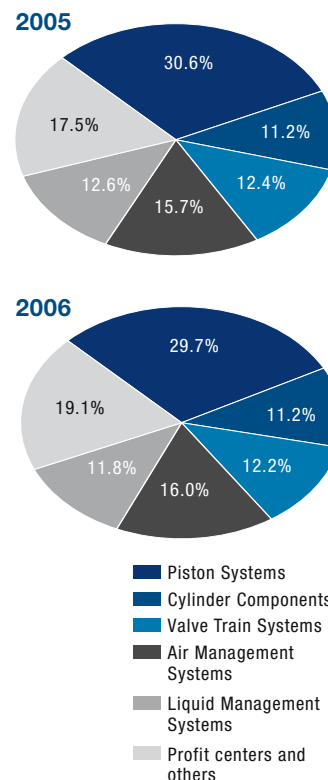
In Asia, the production of medium-weight and heavy commercial vehicles rose by 15.5% to 1,307 thousand units. This development was triggered by high demand, which was induced by the booming economy in most of the developing and emerging markets of Asia. The highest increase in comparison with the previous year was achieved in China, with an increase of 75 thousand to 575 thousand units, followed by India with an increase of 50 thousand to 280 thousand units. In Japan, commercial vehicle production increased by 46 thousand to 406 thousand units.

BUSINESS AND REVENUE DEVELOPMENT IN LINE WITH EXPECTATIONS

Overall, the sales of the MAHLE Group developed in line with the growth level of the global automotive industry, with growth of approximately EUR 200 million (4.7%) in comparison with the previous year. Changes in the international currency exchange rate structures led to an increase of EUR 25.7 million (0.6%) in reported sales. Positive effects from the Polish zloty, the Korean won, and, in particular, the Brazilian real were largely eroded by a devaluation of the Japanese yen and the US dollar. On the other hand, additions of companies in 2006 resulting from acquisitions brought sales amounting to EUR 28.5 million (0.7%) into the consolidation group. The major company acquisitions were made in the industrial filtration business segment. Allowing for currency and consolidation effects, the sales increase amounted to 3.5% and was thus on a similar scale to the quantity increases recorded by the market as a whole. This shows that the considerable price reductions on our products could be compensated for by gains of market share and increasing systems supplies. The strongest growth was recorded by the Cylinder Components and Air Management Systems product lines and the Aftermarket, Large Engine Components, and Industrial Filtration profit centers.

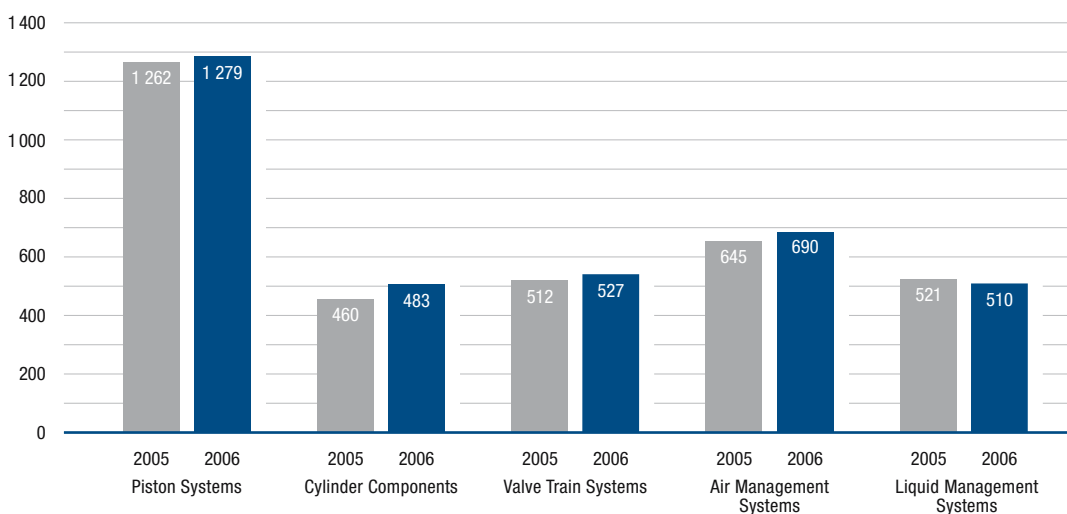
The operating profit of the MAHLE Group also increased in line with the rise in sales. Considerable improvements in profit generated by increased sales volumes, the shutdown of unprofitable business divisions, and improvements in productivity were offset by the strain on profit resulting from reductions in sales prices, significant increases in material prices, pay scale increases, and foreign currency changes. The unexpectedly heavy strain prevented a more significant improvement in profit in comparison with the previous year.

Share of Group sales achieved by the product lines and profit centers



DEVELOPMENT OF THE PRODUCT LINES

Consolidated sales (share of Group sales) in million EUR





PISTON SYSTEMS PRODUCT LINE

Sales

In the 2006 business year, the Piston Systems product line achieved sales of EUR 1,400 million. The organic growth amounted to 3%. Supported by the satisfactory economic situation in the worldwide automotive industry, the product line recorded sustained high demand for piston/connecting rod assemblies in the passenger car segment, thus becoming more firmly established in its strategic positioning as a systems supplier. The sales increase in the commercial vehicle sector in comparison with the previous year was primarily due to the rising demand for single-piece forged MONOTHERM®

steel pistons, which replaced articulated and aluminum pistons on the market to some extent. In addition, intra-Group deliveries – particularly to the Aftermarket profit center – increased significantly in comparison with the previous year.

In Europe, invoiced sales slightly exceeded the previous year's level, although a shift in sales occurred as a result of the discontinuation and new startup of piston types, as well as changes in technology. In terms of products, significant market success was recorded in the commercial vehicle sector by MONOTHERM® pistons. Sales of pistons for passenger cars fell slightly below

the previous year's level, as passenger car gasoline piston activities remained stable and slight declines were recorded in passenger car diesel pistons.

Sales in North America experienced slightly positive development in comparison with the previous year. In our commercial vehicle piston activities, the sales increase of 13.1% in comparison with the previous year was positively affected by the tightening of emission regulations from 2007 and the fact that purchases were brought forward accordingly. In the passenger car sector, sales continued to shift from pure passenger car pistons to passenger car piston/connecting rod assemblies. In the 2006 business year, sales of piston/connecting rod assemblies to North American customers rose by approximately 46% in comparison with the previous year.

In South America, our plants recorded a significant recovery in unit sales in comparison with the previous year as a consequence of the favorable economic conditions and the rise in local automobile production (2.6 million units, an increase of 3% compared with the previous year). Customer demand for pistons for both passenger cars and commercial vehicle engines intensified. In the past business year, the region also benefited from the resumption of direct supply to our North American customers as part of the optimization of logistical processes.

The sales achieved by the Asia/Pacific region in the 2006 business year approximately equaled those of the previous year. Volume impetus resulting from good overall economic development in Thailand and new startups in our Chinese companies in Nanjing and Yingkou compensated for declines in sales in Australia. Our Japanese company achieved sales around the previous year's level.

Operating profit

Although sales exceeded the previous year's high level, it was not possible to re-establish the operating profit. The good fixed cost coverage resulting from capacity utilization, accompanied by the positive development of sales, was more than offset by the intensified price pressure from our customers and the continually rising personnel, equipment, and energy costs. Furthermore, the

Development of product line

Business year	2005	2006
Consolidated sales*		
Product line	1 357	1 400
Share of Group sales	1 262	1 279
Capital expenditure on fixed assets*	87	75
Production plants	23	23
Headcount (as of Dec. 31)	12 674	12 546

* million EUR



Passenger car piston/connecting rod assembly

considerable increase in the prices of raw materials, particularly aluminum, steel, nickel, and copper, had a substantial negative impact on the operating profit. Overall, the productivity increases were not sufficient to compensate for these negative effects on profit.

Capital expenditure

With capital expenditure on fixed assets of EUR 75 million, the investments made by the Piston Systems product line amounted to 5.4% of its sales, exceeding depreciation once again. Investments focused on rationalization and additional quality improvement measures, as well as innovations in our process technology, and for special customer projects. In the 2006 business year, investments in the commercial vehicle sector for the recent expansion of capacities for MONOTHERM® steel pistons and the optimization of our foundries were given priority.

In Europe, we invested in expanding and optimizing our raw production equipment and in building up capacities for MONOTHERM® steel pistons. In addition, the machining capacities for pistons for passenger cars were expanded and automated. In North America, the expansion of capacities for the production of MONOTHERM® steel pistons was also a focal area of investment. Additionally, the process for putting together piston/connecting rod assemblies was optimized. In South America, the partial renovation of output capacities for piston machining, the implementation of customer projects, and automation measures formed the main areas of investment. The Asia/Pacific region expanded its fleet of machinery for melting and casting processes in Japan and Thailand. In addition, the Nishikawa plant in Japan was closed and production was relocated to Tsuruoka. In China, investments focused on our company in Nanjing, to allow for the scheduled ramp-up of output capacities while maintaining a constant level of quality.

Human resources

In the Piston Systems product line, the number of employees declined slightly in comparison with the previous year; as of December 31, 2006, the headcount was 12,546. Compared with the previous year, the staffing level decreased overall in Europe. While structural adjustments were necessary at some locations, other locations—Poland in particular—recorded an increase in the staffing level connected with the development of volumes. North America also employed fewer people than in the previous year. This is attributable on the one hand to the restrained business development in the area of pistons for passenger cars and, on the other hand, to regrouping measures within the Group. In South America, more employees were taken on, in line with the healthy order levels, in order to meet the growing demand. The staffing level increased in the Asia/Pacific region, primarily in our plant in Nanjing, as a result of the new projects. However, the number of employees in the Asia/Pacific region grew only slightly overall.



Part of a commercial vehicle power cell unit with cylinder liner, piston, and rings



MONOTHERM® steel piston for commercial vehicles



Example of pistons for passenger cars and attachments for modern gasoline and diesel engines



CYLINDER COMPONENTS PRODUCT LINE

Sales

As in the previous years, the Cylinder Components product line achieved a further business expansion in the year under report. A sales increase of 8% was generated exclusively by organic growth, with all products contributing to this growth. The continuation of the healthy economic situation in the commercial vehicle sector in 2006 had a particularly positive impact.

Development of product line

Business year	2005	2006
Consolidated sales*		
Product line	691	746
Share of Group sales	460	483
Capital expenditure		
on fixed assets*	54	47
Production plants	17	16
Headcount (as of Dec. 31)	9 224	9 480

* million EUR

Increases in sales of engine bearings were achieved primarily in the commercial vehicle sector in the USA. New customer projects for the supply of fully machined connecting rods led to sales increases in the passenger car connecting rod operating line in North America. Growth was achieved in piston ring activities, particularly in Europe, as a result of increased sales of piston rings for passenger car diesel engines and the new startup of a new generation of engines in the commercial vehicle sector. The healthy economic situation in the automotive industry also continued in South America, leading to an increase in sales of piston rings. Piston pin activities were positively affected by the South American automotive industry and the good economic situation in the commercial vehicle sector worldwide. Unit sales of cylinder liners increased, particularly in connection with commercial vehicle applications in Europe and in North America.

Part of the sales growth is due to currency exchange rate effects. The heavy rise of the Brazilian real led to an increase in reported sales in the Brazilian domestic market. In contrast, the weaker U.S. dollar adversely affected reported sales in the North American market.

Operating profit

Operating profit

After the previous year's profit was negatively affected by currency exchange rate effects and increases in raw material prices, an improvement in profit was recorded in the year under report. This was primarily achieved as a result of restructuring and rationalization measures as well as high



utilization of capacities at all plants. To some extent, the negative conditions created by the relationships between currencies and the costs of raw materials deteriorated further. For example, the heavy increase in the price of copper placed a considerable strain on profit, particularly in the production of bearings. In this form, the negative impact cannot be absorbed in the medium term without customer involvement. Restructuring costs also had an adverse effect, but will result in improvements in profit for the future.

Capital expenditure

In the past business year, heavy investments were made once again, although they fell below the previous year's value. The main area of focus was expanding capacities for the startup of new products. In the piston rings segment, capacities for commercial vehicle and passenger car diesel applications were expanded. Investments in cylinder liners concerned projects in the commercial vehicle sector as well as preparation for new passenger car projects in Europe. Capacities for finish machining of connecting rods for passenger car engines were expanded at our location in Mexico for new customer projects in the USA. These capacities were reused to a large extent by the Piston Systems product line for the assembling of power cell units.

In Brazil, additional capacities for manufacturing pre-products in raw part manufacturing were created for the bearings product group. In the piston pins segment, investments focused on rationalization measures connected with the conversion to improved production processes in raw part manufacturing.

In 2006, we continued with the construction of production facilities for piston rings in China and expanded capacities for these activities. Since the first half of the year, our Yingkou location in northern China has produced piston rings in addition to bearings.

Human resources

In order to achieve the rise in sales recorded in the year under report, the number of employees was increased. In particular, staffing additions were implemented at the locations in Poland and Brazil for cylinder liners, in Portugal for piston rings, and in Mexico for connecting rod manufacturing. A further increase was generated by the construction of the piston ring production facilities in China.

In Germany and at other European locations, the number of employees was maintained at the previous year's level. Because of rationalization measures and productivity improvements, the additional volumes did not require any staffing additions.



Piston rings



Bearings



VALVE TRAIN SYSTEMS PRODUCT LINE

Sales

In the Valve Train Systems product line, sales were slightly above the previous year's level. As a result of changes in the product mix, shifts occurred within the product groups. For example, in the valve seat inserts and valve seat guides segment, the trend toward increased customer demand for sintered rather than cast products continued. The lower price level of the sintered parts led to

a decline in sales, despite a significant rise in unit sales. As in previous years, unit sales of other sintered parts in the European and South American markets increased further. Sales of turbocharger parts were only slightly above the previous year's level, but were characterized by considerable price reductions.

In the composite camshafts segment, the further ramp-up of existing series led to corresponding growth in sales. Our cast camshaft activities generated significantly higher sales, particularly in the North American market. End-of-series products

in the valve actuator segment could not be replaced because of price pressure from competitors in countries where labor costs are low. The start of series production of roller tappets for commercial vehicles led to sales increases in the European market.

MAHLE Powertrain Ltd. in England assembled significantly more complete engines than in the previous year, intended for the Asian market, among others. Unit sales of machined cylinder heads decreased slightly in comparison with the previous year.

Sales growth in the valves segment was achieved as a result of new series production parts in the European market. In particular, the strong market presence with hollow valves was established more firmly in the past business year. A decline was recorded in sales of valve timing parts, which resulted from a change in one customer's engine design.

Operating profit

Operating profit could not be maintained at the previous year's level. A further significant increase in raw material prices and energy costs, accompanied by intensified price pressure from our customers, had a substantial impact in this area. The increases in material prices of alloy elements had extremely far-reaching consequences for sintered products in particular. Likewise, inefficiencies in production inevitably occurred through pre-production processes in view of the imminent relocation of various production activities. The strained capacity situation for chilled cast iron camshafts resulted in cost increases. The significant rise in demand from customers and the significant sales growth accompanying this rise could only be achieved by means of far-reaching special measures in personnel and logistics. The expenditure required for these measures was reflected in the lower overall margins.

Development of product line

Business year	2005	2006
Consolidated sales*		
Product line	516	531
Share of Group sales	512	527
Capital expenditure on fixed assets*	41	27
Production plants	17	16
Headcount (as of Dec. 31)	4 303	4 566

* million EUR



Valves, valve seat inserts, and valve seat guides



MAHLE lightweight valve

The cylinder heads product segment recorded an improvement in profit as a result of increased capacity utilization of engine assembly facilities. However, advance payments in connection with new startups for finish machining of cylinder heads and unplanned expenditure for increased pension benefits put a strain on profit.

Improvements were also made in comparison with the previous year in valve production. Measures to shut down a complete location and relocate processing equipment were successfully completed in the course of the past business year. The high additional expenditure resulting from temporary parallel production at two locations was reduced significantly. The optimized processes of the new production layout in Wölfersheim, Germany, took effect for the first time.

Capital expenditure

Investments in the business year focused primarily on rationalization projects and the expansion of capacities. In Switzerland, a new plant was built in order to concentrate the local sintering activities at one location. An additional line was installed in Leibertingen, Germany, for the production of composite camshafts. In Brazil, the foundry was extended in order to supply the market in accordance with the increased demand for camshafts made from chilled cast iron. At the location in India, additional production capacities were built for the machining of camshafts. In addition, capital expenditure was used to expand sample and prototype construction of camshafts. In the cylinder heads product segment, investments were made in mechanical machining so that unscheduled orders could be accepted at short notice. At our Polish location, the product line invested in the production of valve castings and valve seat guides. Investments were also used to construct valve machining facilities in China in connection with an existing order.

Human resources

The number of employees increased in comparison with the previous year. At the two South American locations in particular, the extremely high utilization of the capacities of the camshaft and sintered part production facilities resulted in new recruitment. Additional personnel were also taken on in India, in line with the growth of unit sales. In Europe, a slight rise in the staffing level was recorded, as MAHLE Powertrain Ltd. in England increased its workforce in line with the rise in sales. The number of employees at the German location remained constant. Further employees were taken on at the production plant for composite camshafts in Leibertingen, in accordance with the increase in sales. In contrast, the number of employees at the valve production plant in Wölfersheim was considerably lower than in the previous year as a result of the restructuring measures implemented there. Overall, efforts are being made to introduce stringent human resource management for the entire product line in the future, as the worldwide customer structure expects significantly higher productivity increases than in the past.



MAHLE CamInCam® camshaft, allows variable timing with one camshaft



AIR MANAGEMENT SYSTEMS PRODUCT LINE

Sales

Overall, business development in the Air Management Systems product line was satisfactory. Sales increased in comparison with the previous year in all regions of the world. Even allowing for changes in exchange rates, the regions exceeded the previous year's sales values. In particular, the positive exchange rate effects for sales in the Korean won almost offset the considerable negative impact of the Japanese yen in Asia.

Development of product line

Business year	2005	2006
Consolidated sales*		
Product line	691	743
Share of Group sales	645	690
Capital expenditure on fixed assets*	35	35
Production plants	17	18
Headcount (as of Dec. 31)	3 446	3 896

* million EUR

In Europe, sales were characterized by the unit sales figures for intake modules and air filter elements produced in Austria. Together with high tool sales, these sales more than offset the discontinuation of a range of intake modules in Germany. In France, air filter and air filter element activities remained below expectations. However, this was partly compensated for by higher tool sales. Sales growth was achieved in North America as a result of the further expansion of cylinder head cover activities, particularly for new engine types for Japanese customers. South America was included in the product line's consolidation group for the first time.

As a result of the expansion of cylinder head cover activities in particular, the sales increase was higher than expected. In Japan, sales declines in the passenger car sector, allowing for foreign currency exchange rate effects, could not be offset by the higher unit sales in commercial vehicle activities. In contrast, sales of intake modules and air filters in Korea, allowing for foreign currency exchange rate effects, substantially exceeded the previous year's sales. At the Chinese location in Tianjin, air filter and air filter element activities developed more positively than planned. Production of air intake modules for Chinese customers was also started. In India, our activities exhibited noticeably positive trends, exceeding the plan estimate.

Overall, further increases in unit sales were achieved with all product groups in the product line. Production of air filters commenced at the majority joint venture in Turkey, founded in 2005 to supply the Turkish market. The new location in Guangzhou, China, which was founded to supply mainly Japanese customers, commenced production of air filters in the last quarter of the year. The location in Shanghai, China, was included in the product line's consolidation group for the first time.



Intake module



Heated blow-by pipe



Valve actuator for intake modules

Operating profit

The product line's operating profit was below expectations, primarily as a result of the weaker development in revenue in Asia and North America in comparison with the previous year. In Europe, adverse effects arising from the increased price pressure from our customers and the lower product sales in France were offset by rises in productivity. Restructuring measures were initiated for adjustment purposes. The weakening of results in comparison with the previous year in Asia was characterized by demands for price reductions, weaker results from our Japanese activities, and minimal market success of our main customers in Japan. This resulted primarily from the lower production figures recorded by some passenger car customers. The North American units also generated unsatisfactory profit in the face of heavy price pressure, as well as increases in material prices for resins and procured plastic components in the USA. Measures were taken to reduce costs and optimize processes, and some production activities were relocated to Mexico.

Capital expenditure

In the year under report, the expansion of activities in Korea and China was one of the main focuses of the product line's capital expenditure on fixed assets. Capital expenditure in Korea was connected with the construction of a new filter plant in Nam-Gu/Ulsan, which offers logistical advantages on account of its proximity to major customers. Investments in China focused primarily on the construction of the new production plant in Guangzhou, along with the necessary production facilities for air filters, intake modules, and cylinder head covers, and the expansion of the plant in Tianjin for the production of intake modules. In addition to these investments, capital expenditure focused, in particular, on expanding capacities at the plants in Austria and Mexico.

Human resources

The growth in headcount in comparison with the previous year was characterized by the establishment of additional business activities for the Air Management Systems product line in Brazil, China, and Turkey, with a total of 215 employees. Growth in Asia, particularly in Korea, also led to the rise in the number of employees in the past business year. At the Western European production plants, staffing additions were only implemented in Austria. The proportion of employees in Europe out of the total headcount declined further, partly as a result of the development of sales.



Oil mist separator with film heater



Cylinder head cover



LIQUID MANAGEMENT SYSTEMS PRODUCT LINE

Sales

The Liquid Management Systems product line was able to achieve sales growth of 3% in the past business year. While sales stagnated in Europe, the activated carbon canister activities in North America expanded considerably, primarily as a result of the acquisition of manufacturing equipment.

Development of product line

Business year	2005	2006
Consolidated sales*		
Product line	607	624
Share of Group sales	521	510
Capital expenditure on fixed assets*	34	42
Production plants	16	15
Headcount (as of Dec. 31)	3 679	3 711

* million EUR

Declining sales in France and Germany were offset by corresponding increases at the production plant in Austria. While OEM/OES sales rose slightly, intra-Group sales in the aftermarket stagnated as a result of the Group's general measures to reduce inventories. Stagnating sales of fuel filters were offset by increasing sales of oil filter modules and activated carbon canisters.

In South America, a new distribution of production volumes between the two filtration product lines led to declining sales for Liquid Management Systems. In Japan, sales decreased slightly as a result of currency exchange rate effects and the intensified price competition in certain product segments, while sales increases were achieved in Thailand.

In China, a new distribution of production between the Air Management Systems and Liquid Management Systems product lines also generated lower sales in comparison with the previous year. In contrast, sales in India rose considerably.



Activated carbon canister for U.S. applications



Oil filter module

The new production plants constructed in the growth regions were successfully integrated into the existing production network. In Timisoara, Romania, the production of activated carbon canisters commenced. In addition, the production of oil filters began in Shanghai, China, in a newly opened production plant. In North America, the newly acquired manufacturing equipment was integrated into the production plant in Murfreesboro, USA, to expand the production of activated carbon canisters.

Operating profit

The profit of the Liquid Management Systems product line did not reach the previous year's level and fell below expectations. In Europe, the startup of production in Romania and restructuring measures initiated in France put a substantial strain on profit. In North America, profit did not reach the previous year's level as a result of the integration and startup of the new production lines and the accompanying startup costs. In South America and Asia, the situation in terms of profits was adversely affected by exchange rate effects and increased price competition. The negative effects of price reductions and increases in material costs are counteracted by intensive cost reduction and rationalization measures. However, the productivity increases achieved were not sufficient to compensate for the full extent of the negative effects on profit in 2006.

Capital expenditure

Investments focused on the acquisition-driven expansion of activated carbon canister production in North America, the expansion of infrastructure for the new location in Romania, and construction, of the new location in Shanghai, China, for the production of screw-on filters, as well as the optimization of production at the locations in Austria, Japan, and Brazil. The majority of the investments, went toward equipment for manufacturing new products in the startup phase.

Human resources

As of the end of 2006, the staffing level in the Liquid Management Systems product line was slightly above that of the previous year. In Europe, the new location in Romania led to a rise in the number of employees. In North America, the staffing level was increased in line with the expansion of output capacities. In Thailand, the number of employees also rose as a result of the increased demand. For the new business year 2007, particular attention will be focused on increasing productivity and optimizing the deployment of personnel in order to achieve the product line's long-term objectives.



*Integration of oil filter and
oil/water heat exchanger into
oil pan structure*



AFTERMARKET PROFIT CENTER

Sales

In the past business year, the Aftermarket profit center increased its sales by 16.5% in comparison with the previous year. The development was substantially affected by the regrouping of individual aftermarket activities from the OEM product lines into the Asia/Pacific regional section of the Aftermarket profit center. In addition, sales were improved by currency exchange rate effects from activities in South America.

Business development in Europe was characterized by a considerable expansion of sales in Eastern Europe. The filter products segment recorded disproportionately strong development, with MAHLE continuing the positive trend exhibited in these markets in recent years. The decline in sales of engine components in North Africa and Western Europe, which was due to a price collapse, was largely compensated for by increased exports to Latin America and the Middle East. The growth on these markets is primarily attributable to the strong demand for commercial vehicle pistons and cylinder liners. The local Aftermarket locations in Western Europe experienced varied development. While sales developed at the previous year's level on the French market, significant increases were achieved for some products in Great Britain and Spain.

In North America, sales also developed positively, primarily as a result of the filter product activities for European vehicle applications. The development of the Aftermarket locations in South America was affected by a significant containment of demand in Brazil, which was caused by the upward revaluation of the local currency in relation to the U.S. dollar and the euro. This led to increased imports and a competitive disadvantage for domestic suppliers. While exports to the other countries of Latin America developed positively, exports to other world regions did not reach the high sales level of the previous year. By establishing a new branch in Argentina, MAHLE strengthened its sales activities and took account of the growing importance of the largest market in South America after Brazil.



*Spare parts supplied
in original equipment
quality*

The focus in the Asia/Pacific region was the creation of uniform sales structures and the grouping of Aftermarket activities in China, with the foundation of MAHLE Trading (Shanghai) Co., Ltd., China. MAHLE Trading Japan Co., Ltd., Japan, was included in the annual financial statements of the MAHLE Group for the first time.

Operating profit

Declining sales on the Brazilian market, expenditure for setting up the sales organization in Asia, and increased personnel and equipment costs adversely affected operating profit in comparison with the previous year. These factors were partially offset by an increase in exports to the remaining regions of Latin America, further growth filter products, and pistons for commercial vehicles.

Capital expenditure

Investments focused on the construction of the new distribution center at the Krotoszyn location in Poland. This location has strengthened MAHLE's market position in Poland. The next step will be to supply the neighboring markets of Ukraine and the Baltic states from 2007.

Human resources

The increase in the number of employees in the Aftermarket profit center is due to the inclusion of the sales organization in Asia, the construction of the storage locations in Poland and Argentina, and the integration of the filter activities in Brazil. In the future, attention will be focused on very thorough employee development in the Aftermarket division, as more streamlined business processes are essential in order to ensure the competitiveness of this business segment.

SMALL ENGINE COMPONENTS PROFIT CENTER

Sales

In the core business of small engine components for lawn and garden equipment and leisure vehicles, a slight sales increase was achieved in comparison with the previous year. In particular, positive development was recorded in sales of piston and cylinder assemblies in the North American market for hand-held lawn and garden equipment and leisure vehicles. However, as a result of weak market development in Germany, the total sales of the profit center declined in comparison with the previous year.

Operating profit

Operating profit was improved in comparison with the previous year. However, both the USA and Germany made only negative contributions to profit, which meant that the profit center remained below expectations despite the overall improved development.

Capital expenditure

In the 2006 business year, the profit center's investment ratio was significantly higher than in the previous year. In order to meet the increased market requirements, investments were made in new machining centers and honing equipment in the USA. In Germany, a highly automated casting line for small engine cylinders was commissioned at the end of the business year.

Human resources

The Small Engine Components profit center had a total headcount of 996 employees worldwide as of December 31, 2006. This corresponds to a decline of approximately 8% compared with 2005. The decline in staffing levels resulted from rationalization measures and the discontinuation of production of cast products for engine blocks at the end of 2005.



*2-stroke assembly
for hand-held
power equipment*

LARGE ENGINE COMPONENTS PROFIT CENTER

Sales

With a continuation of the extremely positive market development, the Large Engine Components profit center was able to significantly increase its sales in all applications in comparison with the previous year. In particular, above-average growth was achieved in the segment comprising stationary and boat engines with cylinder diameters of more than 270 mm.

Operating profit

Alongside the positive development of sales, the operating profit also improved in comparison with the previous year. The return on sales increased as well. The general rise in material prices was offset to a large extent by improved fixed cost coverage and further improvements in productivity.



Capital expenditure

In the 2006 business year, investments focused on expanding capacities in line with the high volume increase. As a result, the investment ratio for the business year exceeded the previous year's value. In relation to sales, however, the investment ratio remained at a moderate level.



Composite pistons with diameters from 165 to 580 mm

Human resources

Because of the heavy increase in quantities, the staffing level in the Large Engine Components profit center was higher than in the previous year. As part of the continuation of the location securing program throughout Germany, MAHLE employees were transferred from the Small Engine Components profit center and other MAHLE locations. As a result of the continuing rationalization measures and productivity increases, however, the staffing additions were proportionately lower than the increase in sales.

MOTORSPORTS PROFIT CENTER

As in recent years, the major motorsport series and events, such as the Formula 1 World Championship, the 24 Hours of Le Mans, the American Le Mans Series (ALMS), the Rally World Championships, the German Touring Masters (DTM), the WTCC, and the Nascar Nextel Cup, were won with MAHLE pistons and engine components.

Sales

Sales in our core business of Formula 1 did not reach the previous year's level. This was due to the far-reaching changes in the regulations: The 10-cylinder engines were changed to 8-cylinder engines. In addition, one engine must be used for two racing weekends. In contrast, sales in the rest of the motorsport sector and in series activities remained largely constant.



Driving force in Formula 1

Operating profit

The decline in sales in Formula 1 activities led to a decline in operating profit in comparison with the previous year, as a result of a reduction in fixed cost coverage, because the output and development capacities had to be maintained in order to meet the high quality and technical requirements. In addition, the delayed startup of a machining line for small-lot high-performance pistons put a strain on profit.

Capital expenditure

In 2006, investments focused on the construction of the small-lot machining line. Additional investments were used to modernize and increase the flexibility of the processing equipment in order to meet the market requirements in the innovative motorsports business.

Human resources

The staffing level remained largely constant in comparison with the previous year. The employees made redundant as a result of the decline of the Formula 1 activities were able to find employment in the new small-lot production facilities. As it is particularly important for employees in the Motorsports profit center to be highly qualified and flexible, a large number of qualification activities were undertaken once again in the 2006 business year.

ENGINEERING SERVICES PROFIT CENTER

Sales

With sales of EUR 28.6 million, the Engineering Services profit center decreased in comparison with 2005, and therefore failed to reach the targets set.

There were two particularly crucial reasons for this: On the one hand, many OEMs faced extremely stiff competition for orders in 2006, as a result of cutbacks in research and development budgets. On the other hand, MAHLE Powertrain—newly integrated into the MAHLE Group—had to establish a reputation on the market and earn trust through close cooperation with customers. We are continuing to actively drive forward this process, which requires a sustainable approach.

In the second half of the year, sales developed positively. This was largely due to intra-Group orders and an increasing order intake, especially from customers in the Far East. We hope to further reinforce this trend in 2007.

Operating profit

Operating profit improved significantly in comparison with the previous year as a result of various cost reduction measures, but remained below our expectations.

Capital expenditure

Investments were made, e.g., in new calculation software and the modernization of our test bench equipment, in order to further improve our range of services and increase working efficiency.

Human resources

As a result of the initiated structural adjustments, the number of employees was reduced by approximately 15% to 370. This primarily affected indirect areas, while the staffing level in engineering remained largely unchanged in order.



MAHLE Powertrain single-cylinder research engine



INDUSTRIAL FILTRATION PROFIT CENTER

Sales

With sales of EUR 85.7 million, the Industrial Filtration profit center achieved growth of 29% in comparison with the previous year. A significant proportion of this was due to the first consolidation of two acquisition projects, which are active in the field of ship maintenance, large engines, and fuel preparation, and therefore expand the product range in the separator and backwash filter segments. The established hydraulic filter and de-dusting activities benefited from the improved order levels in plant construction and mechanical engineering and the continuing strong growth in the wind energy technology market.

While domestic business developed as planned, above-average growth rates were achieved in some foreign markets. Innovations such as the new filter series for cleansers or intake filter modules for mobile applications quickly met with a high level of customer acceptance and also made a significant contribution to the sales increase.

Operating profit

The expansion of the product range and the sustained stable growth in the established areas of activity contributed to improving profits in comparison with the previous year.

Capital expenditure

Investments focused on consistently expanding our range in the separator product groups and supplementing our backwash filter activities by acquiring MAHLE NFV GmbH in Hamburg, Germany, and MAHLE AKO GmbH in Flintbek, Germany. Other areas of focus were the construction of a new production facility in Romania and the implementation of rationalization measures in the production plant in Germany. Investments in tools to reduce costs and new investments in new series for cleanser filtration formed the focus of the profit center's investment measures.

Human resources

The staffing level was increased further, particularly in the sales and development departments. By reinforcing product management with additional application engineers and expanding the sales organization in important foreign markets, we once again intensified customer support and care. The headcount was 24% higher than in the previous year as a result of the first consolidation of MAHLE NFV GmbH and MAHLE AKO GmbH. A total of 427 people were employed worldwide.

DEVELOPMENT OF ALL PROFIT CENTERS

Business year	2005	2006
Consolidated sales*		
All profit centers	889	1 005
Share of Group sales	723	825
Capital expenditure		
on fixed assets*	37	38
Production plants	7	10
Headcount (as of Dec. 31)	4 093	4 404

* million EUR

Profit centers: Aftermarket, Small Engine Components, Large Engine Components, Motorsports, Engineering Services, and Industrial Filtration



Coalescer filter
for fuel treatment

DIFFICULT MARKET ENVIRONMENT IN THE PROCUREMENT MARKETS

In the 2006 business year, the procurement markets were subject to various factors adversely affecting profit, which made material requirements planning increasingly difficult for the MAHLE Group.

On the one hand, the reduced number of alternatives on the procurement side, which resulted from the gradual concentration of suppliers, was offset by counteractive measures. On the other hand, material shortages were accompanied by price increases for large proportions of the raw materials used within the MAHLE Group. As the prices, particularly those of listed raw materials such as aluminum, copper and nickel, could only be shared with our customers to a limited extent, the MAHLE Group's profit was affected considerably. However, this negative development did not affect only directly sourced materials, but also refined or processed pre-products such as sintered powder, semi-finished products, alloys, purchased parts, and resins.

In addition, energy costs increased considerably in large parts of the world. As multi-year sourcing agreements with fixed prices could only be concluded in certain subdivisions, the strain on the energy markets also had an extensive impact on the MAHLE Group's situation in terms of profits. Countermeasures used in other procurement markets, such as international or global pooling of requirements, are only possible to a very limited extent or with long lead times in the energy market, primarily on account of the supplier structure. Other optimization measures such as reducing consumption or avoiding peak loads during high tariff periods, were already initiated at all locations at an early stage, independently of the current developments in energy prices. In addition, the use of alternative energy sources was explored.

In 2006, MAHLE further expanded its efforts to coordinate procurement activities globally and combine purchasing volumes in order to counteract the market developments described above. MAHLE has established sections of its worldwide purchasing function in the major countries with competitive conditions. However, creating and expanding a large supplier structure is expensive; our high internal requirements in terms of process safety and quality call for a multi-step, time-intensive procedure for building up a pool of suppliers.

Besides the market-oriented measures outlined above, we took further consistent steps in the ongoing development of our own organization and methodology. The concept of material group purchasers with global and regional responsibility, established several years ago within the MAHLE Group, was differentiated further in 2006. Cross-regional procurement by designated responsible purchasers was also intensified.



As an additional measure to increase efficiency, the existing supplier Internet platform was expanded further. The number of purchases made over the Internet was increased considerably and further optimizations were made in terms of the technical exchange of data.

The purchase planning methodology was supplemented by a strategic planning component, which allows purchasing to be linked meaningfully with multi-year product line planning. In this system, the requirements and procurement planning for purchasing is derived from unit sales or production figures and the associated strategy pursued by the product lines. Also included in this step of the methodology is the forward sourcing approach, which was used for the first time in 2006. The aim of this approach is to identify future requirements and demand by means of market research undertaken at an early stage, thereby creating significantly more time and scope for selecting suppliers.

In order to guarantee optimum quality, MAHLE's international production locations—where the latest automated manufacturing and testing technologies are deployed—and suppliers are bound to strict quality standards. All MAHLE locations are certified in accordance with international quality standards, such as ISO TS 16949 for the automotive industry. The same applies to Corporate Purchasing. MAHLE regularly receives commendations and quality awards from well-known manufacturers. This is also an incentive for MAHLE's Purchasing department to continually improve its quality standards. Our Purchasing department is honoring this commitment by establishing its own quality management function.

INNOVATOR WITH HEAVY INVESTMENT IN RESEARCH AND DEVELOPMENT

An innovative product range with high customer benefit is vital to ensure that the MAHLE Group maintains a good market position and stands out from the competition. Innovation, like performance, is a fundamental characteristic of MAHLE's brand essence. In order to safeguard and strengthen this position, a high level of investment was devoted to research and development. The focus was placed on product innovations leading to lower fuel consumption and emissions. To safeguard the market leadership and systems competence in the area of combustion engines and engine peripherals, MAHLE is working on a number of new products, as well as new production technologies and processes. To ensure that optimum results are achieved, MAHLE's know-how is developed in customer-oriented technology centers in all regions of the world, but coordinated and amalgamated globally. This allows us to exploit and combine the strengths of local and global activities for our customers. For example, major innovations—resulting primarily from the collaboration between the individual research and development centers and the innovative engineering service provider MAHLE Powertrain—were developed to reduce pollution emissions and fuel consumption.

Besides the innovations in product engineering, intensive research and development activities are also being undertaken in order to improve process engineering. Innovative production processes guarantee the highest possible quality and customer satisfaction. Furthermore, these investments in research and development also help MAHLE to offer module and systems solutions on a more economic basis.

In an organizational sense, the customer-oriented approach in research and development is also reflected in the geographical distribution. MAHLE is represented in all major regions with technological know-how and competent employees. Approximately 2,300 development engineers and technicians at seven different locations guarantee fast, sustainable solutions to the problems arising from customer enquiries by means of their knowledge, internal networking, and customer focus.

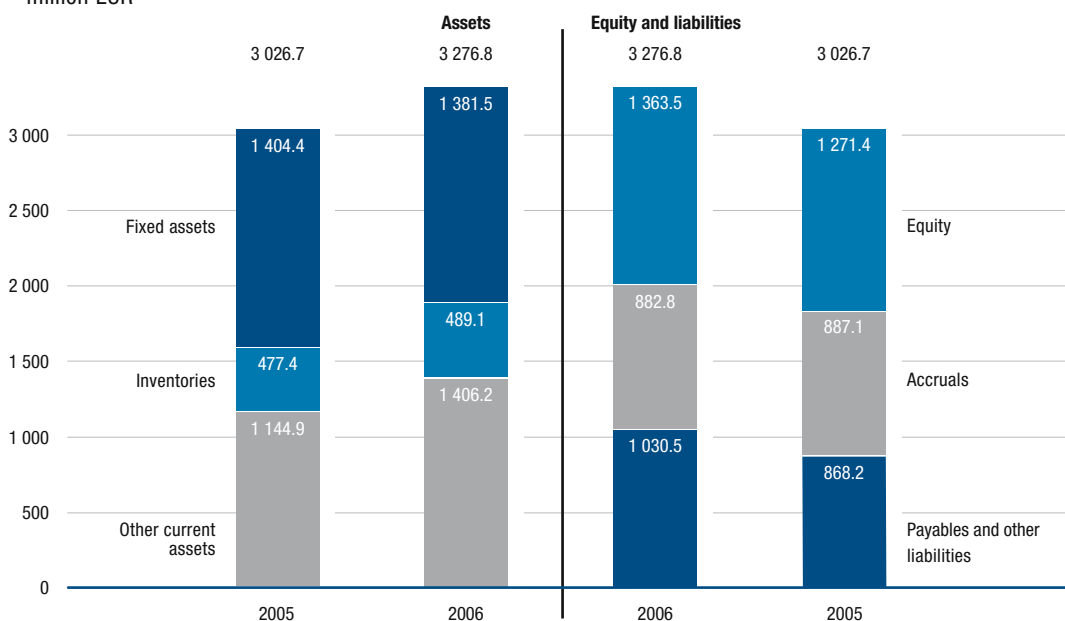
Overall, the research and development activities made a substantial contribution to enabling MAHLE to further strengthen its competitive position and lay important groundwork for future products and business success.

CONTINUAL IMPROVEMENT OF BALANCE SHEET STRUCTURE

The expansion of business activities is also reflected in the increased balance sheet total. The structure of the main elements of the assets and liabilities developed as follows in comparison with the previous year:

Balance sheet structure of the MAHLE Group

* million EUR



The increase of EUR +250.1 million in the balance sheet total is characterized on the asset side by slight growth in inventories (EUR +11.7 million), but primarily by trade receivables (EUR +68.2 million) and a significant increase in available cash (EUR +209.3 million). In contrast, declines were recorded in fixed assets (EUR -22.9 million) and other assets (EUR -18.0 million).



The reduction of fixed assets (EUR -22.9 million) results primarily from a decline in intangible assets (EUR -18.0 million), which was caused by depreciation. Despite investments remaining significantly above depreciation, tangible fixed assets fell slightly, as the conversion of currencies—particularly in Group companies reporting in U.S. dollars or Japanese yen—led to a decrease in book value. A slight decrease in financial assets (EUR -1.1 million) also contributed to the reduction of fixed assets. The slight increase of 2.5% in inventories is evidence, particularly in view of the business expansion of 4.7%, of the results of the MAHLE Group's activities to optimize warehousing and supplier management.


In contrast, the increase in trade receivables exceeds the amount of business expansion, as some of our customers are making payments later than in the previous year for reasons relating to their own economic situation. The increase in available cash, which is accompanied by the rise in liabilities to banks (EUR +143.1 million), is connected with acquisitions planned for the first few months of 2007. As a result of the disproportionately strong growth of current assets, the proportion of fixed assets in the balance sheet total decreased from 46.4% to 42.2%.

On the liabilities side, in addition to liabilities to banks, the Group's equity also increased significantly (EUR +92.1 million), while the equity ratio deteriorated from 42.0% to 41.6% as a result of the disproportionately strong increase in total assets and liabilities. As the year-end prices of the Japanese yen and U.S. dollar in particular, were subject to a more or less significant devaluation in comparison with the previous year, the conversion of foreign currency items in the Group balance sheet produced an equity reduction of EUR 58.4 million with no effect on profit. Excluding this negative foreign currency exchange rate effect and the acquisition-oriented structure of the available cash, the equity ratio would have reached approximately 48%.

The liability items provisions for pensions (EUR +10.7 million), other accruals (EUR +7.6 million), and other liabilities (EUR -39.5 million) contributed either insignificantly or negatively to Group financing. In contrast, the disproportionately strong increase in trade payables (EUR +66.0 million), which arose as a result of local extraordinary items, supported the financing of the increase in total assets and liabilities. As fixed assets have grown by a smaller amount than equity in recent years, fixed assets are now almost completely covered by the Group's equity.

OPERATIONAL FINANCIAL REQUIREMENTS COVERED BY GROUP FUNDS

In 2006, the cash inflows generated in the operative business of the MAHLE Group increased significantly and once again completely covered the operational financial requirements. The operating profit achieved on an ongoing basis contributed to this situation, as did the significantly smaller increase in the capital employed. Of the non-operating cash flows, net cash outflows for interest and taxes recorded a considerably lower value than in the previous year. In addition, the changes in intangible assets, financial assets, other assets, and other liabilities led to a minor release of funds.




In order to create a financing framework for potential acquisitions, existing credit lines with banks were utilized to a significantly higher degree than was the case at the end of 2005. As the additional funds provided by banks were used completely for short-term investments, the MAHLE Group's net financial situation changed only marginally as a result of this transaction. Whether, and to what extent, additional bank loans will be necessary in order to finance business and company acquisitions depends on the volume of potential acquisition projects.

IMPROVEMENT IN EARNING POWER

Adapting the profit and loss statement regarded as an international standard, the MAHLE Group applied the cost of sales method in the presentation of the income statement for the first time in 2006. To create a period-to-period comparison, the previous year's figures were presented in a form identical to that in which the 2006 financial statements were drawn up.

The net income for the year increased by EUR 32.8 million (+20.6%) in comparison with the previous year. The improvement was partly due to the positive development of operating profit and partly to effects from the financial result and non-operating profit area. The following factors, in particular, had a substantial impact on the development in revenue of the MAHLE Group in the 2006 business year:

- Sales grew in comparison with the previous year in the form described above, but suffered a loss in earning power. The price reductions demanded by our customers led to lower sales and, as a direct result, a significant strain on profit.
 - Market-induced increases in material prices could not be passed on to our customers to a sufficient degree. Once again, these costs adversely affected margins and profit overall.
 - Personnel costs also increased, putting a strain on margins and profit.
 - Overall, transactions in foreign currencies and the conversion of profits earned in foreign currencies led to a small negative change in profit in comparison with the previous year.
 - The progress made in productivity was not able to completely compensate for these factors. As a large proportion of the overall effects had an impact on sales and the cost of sales, MAHLE was faced with an unsatisfactory decline in the gross margin from 23.3% in 2005 to 22.9% in 2006.
 - Of the non-operating items in the income statement, three facts in particular were of significant interest. Firstly, there was a lower requirement for special amortization of goodwill and, secondly, the financial result was no longer negatively affected—as in the previous year—by values resulting from the change in the discount interest rate on pension accruals. Finally, structural measures and local extraordinary items led to a reduction of EUR 12.9 million in the tax expense.
- 



On the one hand, MAHLE was able to participate fully in the market development, but, on the other hand, profit was adversely affected, primarily by reductions in sales prices, as well as increased costs—of materials and personnel in particular—and translation losses, which meant that only a moderate increase was recorded in operating profit. The non-operating contributions of the interest result and tax expense thus contributed more significantly to the overall improvement in profit.

RISK MANAGEMENT

In the MAHLE Group, the implementation of systematic risk management is a fundamental goal. Globally established internal auditing is carried out by independent internal employees as well as by external professional service providers. The analysis focuses on the following points:

- In order to identify future opportunities and risks at an early stage, systematic early detection of market developments is undertaken within the MAHLE Group. Information from these analyses is used in the selection and ongoing development of locations and in business and production processes. In analyses of this kind, a major area of focus is the targeted evaluation of early indicators from the business environment.
- Identifying and controlling operative risks is also an important task for the MAHLE Group, which is undertaken systematically. The management of the individual plants monitors essential aspects of production safety and quality assurance. Likewise, the operative risks are monitored at Group level, with the support of a globally oriented quality and information system.
- Financial and currency risks are identified in a uniform way throughout the Group and controlled globally by means of the active involvement of experts in the various regions. Speculative transactions or the use of financial instruments without a connection to the underlying transaction are not employed within the MAHLE Group. Hedging transactions are entered into in accordance with Group-wide principles and subject to strict monitoring. Systematic, Group-wide liquidity management allows coordinated reduction of financing risks. This system continues to contribute to the communication of information relevant to decision-making with a high level of transparency in relation to residual risks.
- Market risks on both the sales and procurement sides are actively dealt with in the MAHLE Group. As regards sales risks, efforts are made to hedge against regional market and customer risks as effectively as possible through global orientation and a broad customer structure. Price and availability risks on the purchasing side are counteracted by means of global purchasing activities, systematic analyses of creditworthiness, and testing of the use of substitute raw materials and alternative production processes.

- The turnover of employees in key positions is counteracted to a significant extent by the strong focus on employee development and specific qualification measures. This is accompanied by an employee- and goal-oriented leadership style, incentive-based remuneration and flexible working hours systems, teamwork, and a high level of decision-making autonomy. These measures increase our employees' motivation and are intended to achieve a staff turnover rate in the MAHLE Group that falls considerably below the industry average.
- Fundamental risks are covered by insurance. Business-specific risks resulting from e.g., product liability or plant failure, are reduced by means of the highest quality requirements and extensive control and inspection processes.
- In order to decrease potential risks connected with information technology, adequate precautionary measures are taken at appropriate times. In addition, proven processes exist to safeguard and protect the Group IT infrastructure in the event of emergency and crisis situations.

For the 2006 business year, the auditors have analyzed the internal accounting-based control system as part of the audit of the consolidated financial statements and have raised no objections. The rules of the German Corporate Governance Code have also been implemented insofar as they apply to the MAHLE Group.

OUTLOOK

In recent years, MAHLE has set up a global network of research and development centers in order to safeguard and expand its technological competence, and continued this approach in 2006 by establishing a new center in China. It is expected that these investments in technological presence will lead to significant participation in business development, particularly in regions where MAHLE has the highest potential market share. These growth prospects are supported in the current business year by an overall positive economic environment. The conditions for further expansion of the global economy are favorable overall: Worldwide economic growth of approximately 3% is expected for 2007. In the euro zone, further increases in growth rates can potentially be achieved. Similarly, we anticipate a continuation of the considerable growth rates of 2006 in Asia and South America. In contrast, the prospects for North America are difficult to estimate and will depend largely on the effect of the restrictive monetary policy still expected from the U.S. Federal Reserve.

We believe that the development of the automotive industry, for the passenger car and light commercial vehicles market segment, is on course for continual growth—both globally and in all regions of the world. Nevertheless, it remains to be seen how the increased fuel prices and renewed discussion concerning CO₂ emissions will affect the ratio of passenger cars to light commercial vehicles. Varying regional trends, with a temporary global pause in growth, are evident only in the commercial vehicles sector.

From today's perspective, the likelihood that forecast vehicle production figures will be achieved is essentially dependent on the further development of crude oil prices, which we expect to stabilize in 2007.



Worldwide automobile production

Number in 1 000s

	2006	2006	2007	2007
	Passenger cars & light coms.	Commercial vehicles (incl. buses)	Passenger cars & light coms.	Commercial vehicles (incl. buses)
America	18 297	813	18 436	623
NAFTA	15 265	648	15 225	463
South America	3 032	165	3 211	169
Asia/Pacific	25 589	1 307	27 493	1 324
Japan	10 970	406	11 051	380
China	6 590	575	7 518	626
Europe	20 731	625	20 988	599
Germany	5 667	175	5 578	165
Other countries	1 718	0	1 795	0
Total	66 335	2 745	68 712	2 555

Source: Global Insight, March 2007

Besides the general trends in the global economy and automotive industry and their impact on business development, as well as continuous internal efforts to increase productivity and gain market share organically by means of innovative products and cost-effective production structures, the 2007 business year will be characterized by the acquisition of additional business divisions. Firstly, the entire engine parts group of the Dana Corporation, comprising locations in eleven countries with around 5,000 employees, has been acquired. In 2006, this business segment generated sales of USD 659 million. The main products are piston rings, engine bearings, cylinder liners, and camshafts. For MAHLE, this acquisition represents a considerable strengthening of its worldwide market position, particularly in the areas of piston rings and bearings and in the free trade business for engine components. As engine components have not been among the Dana Corporation's core business segments for some time, MAHLE will be faced with the important task of integrating the Dana locations into its existing production network—by means of suitable restructuring measures—in order to facilitate the necessary synergy effects for the future.


Secondly, we expect the takeover of the air intake modules and air filtration business segment of Siemens VDO Automotive. For MAHLE, this acquisition represents an important step in the expansion of its strategic market position, as it will allow us not only to consolidate and expand customer relationships but also significantly improve the regional balance of the Air Management Systems product line. The activities generate sales of approximately EUR 300 million, with around 1,000 employees. The majority of these activities are now located in North America, while other major locations are in Europe and Asia. The latter region shows additional future sales potential of considerably more than EUR 100 million in this business segment.



In the 2007 business year, MAHLE Tri-Ring Valve Train (Hubei) Co., Ltd. in Macheng, China, and Edival S.A. in Rafaela, Argentina, were also included in the Group for the first time. The Chinese company is a MAHLE majority joint venture with the local partner Hubei Tri-Ring Company Ltd. for the production of engine valves. This is the first time MAHLE has been represented in this product segment in China, and the joint venture substantially strengthens its position in this rapidly growing market in the automotive sector. Around 20 million valves are produced annually by the 1,600 employees. The introduction of new production technologies is already planned for 2007.

In connection with the Argentinean company, efforts are being made to further strengthen the market presence of the Valve Train Systems product line in the Mercosur region. The company, which currently employs around 800 people, has all the necessary technical processes to manufacture passenger car, commercial vehicle, and motorsport valves as well as valves for small engines, and generates the majority of its sales of around USD 40 million through exports to the NAFTA region and Europe. Following the acquisition of the two companies, the valves product segment now has a presence in all of the world's major automobile regions.

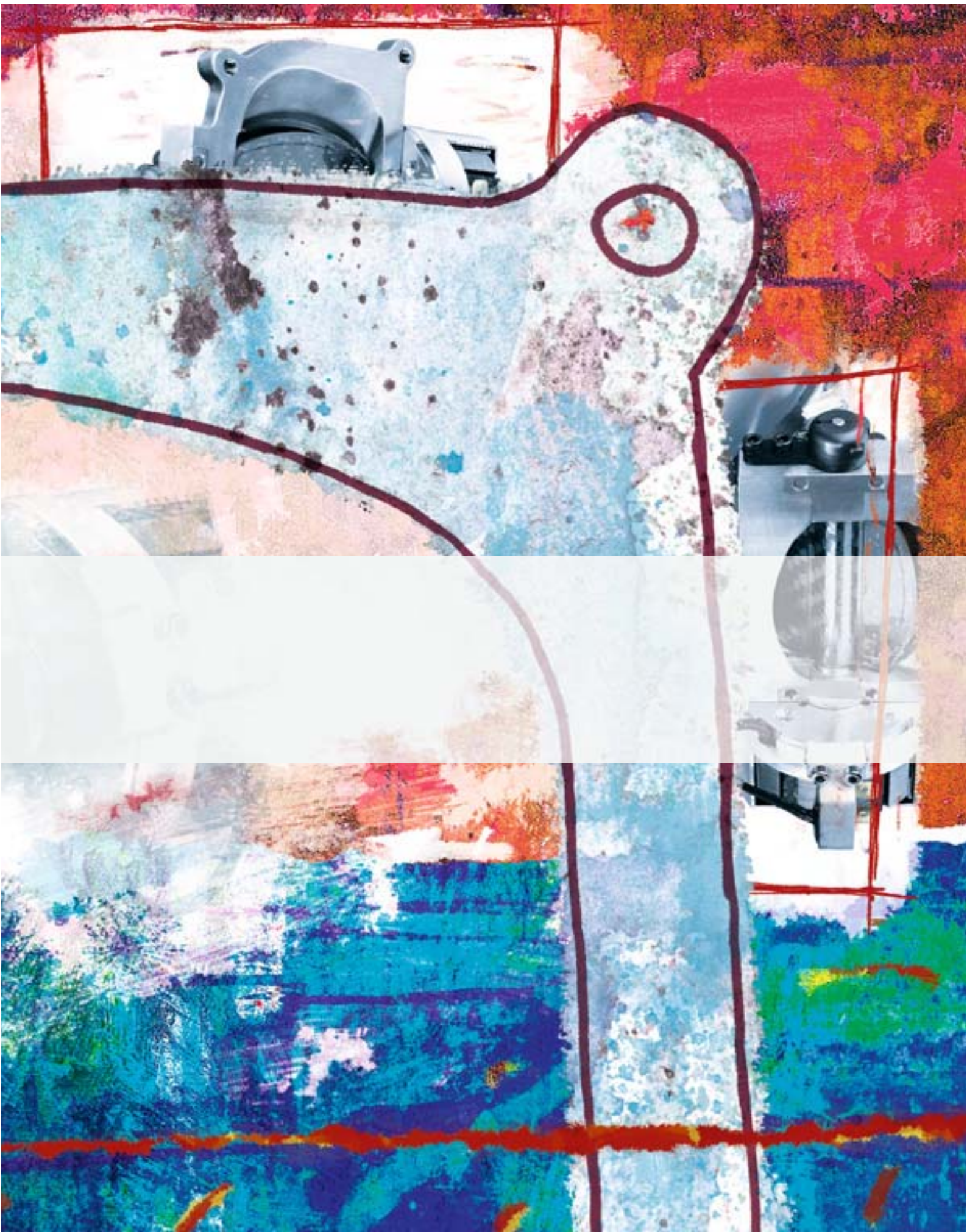
On the basis of the expected developments, the MAHLE Group anticipates a significant sales increase from 2006 to 2007. The Group's expected profit, however, will be affected by the low operational earning power currently prevailing in some areas, the imminent expenditure for restructuring measures, and integration costs for parts of the acquired business segments, and will not exhibit the expected profit relationships until subsequent years.



The background is a vibrant, abstract collage of colors including reds, oranges, pinks, purples, blues, and greens. A large, dark red outline of a washing machine is superimposed on the artwork. The washing machine's door is open, revealing the drum and internal components. The text is centered over a white horizontal band that spans the width of the page.

LETTING RESULTS

SPEAK FOR THEMSELVES





BALANCE SHEET OF THE MAHLE GROUP
AS OF DECEMBER 31, 2006

Assets

in EUR '000		Dec. 31, 2006	Dec. 31, 2005
Fixed assets			
Intangible assets			
Industrial rights and similar rights	14 533		13 820
Goodwill	115 629		134 351
Advance payments	696		685
	130 858		148 856
Property, plant and equipment			
Land, leasehold rights and buildings including buildings on third-party land	411 097		414 847
Technical equipment and machinery	675 209		663 997
Other equipment, fixtures and furniture	66 273		65 554
Advance payments and assets under construction	82 592		94 575
	1 235 171		1 238 973
Financial assets			
Shares in affiliated enterprises	1 456		4 105
Shares in associated enterprises	918		835
Other equity investments	1 584		2 268
Long-term investments	10 397		8 074
Other loans	1 097		1 264
	15 452		16 546
		1 381 481	1 404 375
Current assets			
Inventories			
Raw materials and supplies	133 094		128 008
Work in process	131 610		128 564
Finished goods and merchandise	219 094		215 392
Advance payments	5 318		5 481
	489 116		477 445
Accounts receivable and other assets			
Trade receivables	725 162		656 995
Receivables from affiliated enterprises	432		2 358
Receivables from enterprises in which investments are held	1 476		832
Other assets	99 746		117 754
Deferred tax assets	86 537		100 385
	913 353		878 324
Marketable securities	76 880		61 936
Cash on hand and at banks	406 478		197 151
		1 885 827	1 614 856
Prepaid expenses		9 445	7 434
		3 276 753	3 026 665

Equity and liabilities

in EUR '000		Dec. 31, 2006	Dec. 31, 2005
Equity			
Subscribed capital	150 000		150 000
Capital reserves	166 430		166 430
Revenue reserves	958 585		849 429
Unappropriated retained earnings	6 011		6 339
Minority interests	82 457		99 210
		1 363 483	1 271 408
Accruals			
Accruals for pensions and similar obligations	354 496		343 753
Accruals for current taxes	31 632		47 015
Accruals for deferred taxes	47 484		54 752
Other accruals	449 166		441 569
		882 778	887 089
Liabilities			
Liabilities to banks	554 432		411 312
Advance payments received on account of orders	2 254		4 308
Trade payables	378 482		312 469
Liabilities on bills accepted and drawn	2 450		3 280
Payables to affiliated enterprises	881		790
Payables to enterprises in which investments are held	3 988		6 988
Other liabilities	84 735		124 230
Taxes:	22 142 (previous year 30 071)		
Relating to social security and similar obligations:	15 328 (previous year 25 983)		
		1 027 222	863 377
Deferred income		3 270	4 791
		3 276 753	3 026 665



DEVELOPMENT OF FIXED ASSETS OF THE MAHLE GROUP

in EUR '000	Accumulated acquisition or production cost as of Jan. 1, 2006	Changes in the Group in 2006	Additions in 2006	Write-ups in 2006	Disposals in 2006	Transfers in 2006	Accumulated depreciation and amortization	Net book value as of Dec. 31, 2006	Depreciation and amortization expense for the year
Intangible assets									
Trademarks and similar rights	62 447	41	9 834	–	6 946	238	51 081	14 533	6 684
Goodwill	310 841	–	30 206	–	30 671	2 561	197 308	115 629	48 036
Advance payments	3 285	–	51	–	42	– 2 598	–	696	–
	376 573	41	40 091	–	37 659	201	248 389	130 858	54 720
Property, plant and equipment									
Land, leasehold rights and buildings including buildings on third-party land	767 005	1 319	19 740	–	3 793	21 074	394 248	411 097	28 097
Technical equipment and machinery	2 506 507	18	132 059	–	83 468	65 991	1 945 898	675 209	169 746
Other equipment, fixtures and furniture	374 031	241	22 061	–	33 161	7 877	304 776	66 273	25 724
Advance payments, assets under construction	91 472	–	89 666	–	1 894	– 95 143	1 509	82 592	–
	3 739 015	1 578	263 526	–	122 316	– 201	2 646 431	1 235 171	223 567
Financial assets									
Shares in affiliated enterprises	11 438	–	31	–	5 988	–	4 025	1 456	–
Shares in associated enterprises	17 935	–	–	83	11 909	–	5 191	918	–
Other equity investments	2 167	–	–	–	583	–	–	1 584	–
Long-term investments	8 769	–	4 350	–	1 920	–	802	10 397	15
Other loans	2 769	–	181	–	243	–	1 610	1 097	20
	43 078	–	4 562	83	20 643	–	11 628	15 452	35
	4 158 666	1 619	308 179	83	180 618	–	2 906 448	1 381 481	278 322

INCOME STATEMENT OF THE MAHLE GROUP
FROM JANUARY 1 TO DECEMBER 31, 2006

in EUR '000	2006	2005
Sales	4 314 020	4 121 782
Cost of sales	- 3 324 752	- 3 161 068
Gross profit on sales	989 268	960 714
Selling expenses	- 221 181	- 207 258
General administrative expenses	- 197 781	- 200 240
Research and development expenses	- 241 618	- 218 546
Other operating income	141 514	167 485
Other operating expenses	- 151 087	- 161 436
	- 670 153	- 619 995
Investment income	123	530
From affiliated enterprises: 0 (previous year 139)		
From associated enterprises: 85 (previous year 347)		
Income from other investments and long-term loans	195	782
Other interest and similar income	17 836	10 901
From affiliated enterprises: 2 (previous year 2)		
Amortization of financial assets and of marketable securities	- 35	- 1 162
Relating to shares in associated enterprises: 0 (previous year 235)		
Interest and similar expenses	- 42 609	- 77 025
To affiliated enterprises: 6 (previous year 5)		
Income from ordinary business activities	294 625	274 745
Taxes on income	- 91 053	- 98 841
Other taxes	- 11 760	- 16 896
Net income for the year	191 812	159 008
Profit applicable to minority shareholders: 22 079 (previous year 22 135)		
Loss applicable to minority shareholders: 543 (previous year 1 656)		



NOTES TO THE FINANCIAL STATEMENTS OF THE MAHLE GROUP

GROUP OF CONSOLIDATED COMPANIES

MAHLE GmbH, Stuttgart, Germany, (parent company) as well as 17 German and 65 foreign subsidiaries are included in the consolidated financial statements. In addition, three companies were valued at equity. The consolidated companies are shown in the statement of shareholdings. The following companies were consolidated for the first time in 2006:

- MAHLE Trading Japan Co., Ltd., Okegawa, Japan, as of January 1
- MAHLE GmbH & Co. Grundstücksvermietung OHG, Düsseldorf, Germany, as of June 30
- MAHLE NFV GmbH, Hamburg, Germany, as of January 1
- MAHLE AKO GmbH, Flintbek, Germany, as of June 1
- MAHLE Trading (Shanghai) Co., Ltd., Shanghai, China, as of January 1

The companies consolidated for the first time accounted for EUR 5 million of the balance sheet total and EUR 28.5 million of total sales.

In 2006, two companies were merged into other Group companies and one Group company was liquidated.

In the year under report, 9 companies were not consolidated because of their immateriality for the preparation of the consolidated financial statements (previous year: 9).

EXEMPTION REGULATIONS FOR GERMAN COMPANIES

The following subsidiaries make use of the exemption provision of Sec. 264, para. 3 HGB concerning the publication of their financial statements:

MAHLE International GmbH, Stuttgart; MAHLE Filtersysteme GmbH, Stuttgart; KLF GmbH, Stuttgart; MWP MAHLE-J. Wizemann Beteiligungen GmbH, Stuttgart; MAHLE Ventiltrieb GmbH, Stuttgart; MAHLE Aftermarket GmbH, Stuttgart; MAHLE Industriebeteiligungen GmbH, Stuttgart; MAHLE Versicherungsvermittlung GmbH, Stuttgart; MAHLE NFV GmbH, Hamburg.

METHOD OF CONSOLIDATION

Consolidation was performed using the book value method. Under this method, the value of the investments on the books of the parent company as of the date of the first consolidation upon acquisition of the holding is offset against the underlying equity of the subsidiaries. Any differences resulting from this process are shown net in the balance sheet. Credit differences are amortized over ten years. Impairment losses of EUR 22,523k were also recorded. As of December 31, 2006, this resulted in an asset balance of EUR 105,105k, comprising:

Goodwill	EUR	116,838k
Negative goodwill from capital consolidation	EUR	11,733k

Credit differences of EUR 5,653 million arising from capital consolidation in previous years have been released to the income statement.

Associated companies were valued at equity according to the book value method. Values were determined at the time of their initial inclusion in the consolidated financial statements. This did not result in any material effects in the year under report.

Intercompany transactions and receivables and payables were offset against each other. Intercompany profits were eliminated.

Deferred taxes resulting from consolidation measures affecting net income were formed at the Group-wide tax rate of 24%.

ACCOUNTING AND VALUATION PRINCIPLES

The accounting and valuation methods applied in the past were maintained.

Intangible assets and property, plant and equipment were valued at cost of acquisition or production, less scheduled amortization and depreciation. Scheduled depreciation was recorded using the straight-line method of depreciation, based on the estimated useful life. Wherever it was possible or appropriate to show assets at a lower value, impairment losses were recorded.

Financial assets were also shown at the lower of cost or market value, whenever a sustained impairment in value was identified.

Inventories were capitalized at cost of acquisition or production; work in process and finished goods were carried at cost including an appropriate portion of material and production overhead. Adequate depreciation was recorded wherever market prices or the values determined were lower than the book values or where the salability of products and assets was impaired.

Accounts receivable and all *other current assets* were shown at their nominal value. Appropriate allowance was made for any specific bad debts identified. A general bad debt allowance was recorded to cover general credit risk.

Uncertain debts and potential losses from pending transactions were shown to an appropriate extent as accruals on the liabilities side.

Accruals for pensions and similar obligations were calculated according to the actuarial principles of IAS 19 and discounted to their present value throughout the Group.

Accruals for current taxes and *for deferred taxes* and *other accruals* provide appropriate cover of uncertain debts and potential losses from pending transactions. The item also comprises expense accruals as well as deferred tax accruals taken from the individual financial statements.

Liabilities are shown at the amount repayable.

Accounts receivable and *accounts payable in foreign currencies* were shown at cost of acquisition or at the lower/higher currency exchange rate applicable on the balance sheet date. Bank balances denominated in foreign currency were converted at the bank selling rate on the balance sheet date.

It is extremely difficult to gage the risk presented to our operational business by movements in exchange rates and interest rates. In order to minimize this risk, appropriate hedging activities were adopted, e.g., derivatives. Transactions are only concluded with banks, whose creditworthiness is impeccable, and then in accordance with uniform guidelines and strict internal auditing processes. The involvement of these banks is restricted to securing the business transaction and the financial investment and financing processes involved.

Deferred tax assets and liabilities were determined for all timing differences between the taxation and balance sheet values in accordance with the regulations of GAS 10 Deferred Taxes in Consolidated Financial Statements. The deferred taxes were determined on the basis of the tax rates expected at the time of recognition. These are based on the regulations adopted at the balance sheet date. No deferred tax assets on tax loss carry forwards or tax credits were formed.

CONVERSION OF CURRENCIES

The financial statements of the foreign companies which do not report in euro were converted as follows:

- Equity: exchange rate at the time of acquisition or, alternatively, at the time of first consolidation
- Other items in the balance sheet: exchange rate as of the balance sheet date
- Items in the income statement: average exchange rate over the year

Values were adjusted to the regulations of GAS 14. Accordingly, all items in the income statement, including the net income for the year, have been converted using the average exchange rate for the first time in the 2006 business year.

In the development of fixed assets, exchange differences arising from the application of the current rate method have been netted with the opening balances, while deviations from the conversion of movements during the current year have been netted with disposals.

As in the past, any differences resulting from the conversion of items shown in the balance sheet into euro were offset against revenue reserves.



NOTES ON THE BALANCE SHEET OF THE MAHLE GROUP

Goodwill

The disposals include write-offs of fully amortized goodwill amounting to EUR 29,427k.

Accounts receivable and other assets

in EUR '000	Carrying value Dec. 31, 2006	Thereof with a remaining period of more than 1 year
Accounts receivable		
Trade receivable	725 162	963
Receivables from affiliated enterprises	432	–
Receivables from enterprises in which investments are held	1 476	–
Other assets	99 746	20 705
Deferred tax assets	86 537	39 649
Total	913 353	61 317

In the previous year, trade receivables (EUR 422k), other assets (EUR 25,752k), and deferred tax assets (EUR 42,625k) had a remaining term of more than one year.

The *deferred tax assets* were formed as a result of deductible timing differences. A valuation allowance of EUR 12,562k was made for deferred tax assets in the business year for which the probability of recognition was considered insufficient.

Prepaid expenses comprise the differences between net loan proceeds and the amount repayable to banks (debt discounts) amounting to EUR 176k (previous year: EUR 246k).

The *unappropriated retained earnings* equal that of the parent company and contain the amount carried forward from the previous year of EUR 39k.

Other accruals are comprised mainly of potential losses from pending transactions, obligations with regard to personnel matters, warranty-related risks, and expenditure arising in the years to come.

Liabilities

in EUR '000	Carrying value Dec. 31, 2006	Thereof with a remaining period of up to 1 year	Thereof with a remaining period of up to 5 years
Liabilities to banks	554 432	310 391	25 952
Advance payments received on account of orders	2 254	2 120	–
Trade payables	378 482	378 146	79
Trade notes payable	2 450	2 450	–
Payables			
To affiliated enterprises	881	881	–
To enterprises in which investments are held	3 988	3 988	–
Other liabilities	84 735	80 298	880
Total	1 027 222	778 274	26 911

In the previous year, liabilities to banks (EUR 184,722k), advance payments received on account of orders (EUR 4,210k), trade payables (EUR 312,469k), liabilities on bills accepted and drawn (EUR 3,280k), payables to affiliated enterprises (EUR 790k), payables to enterprises in which investments are held (EUR 6,978k) and other liabilities (EUR 106,385k) had a remaining term of less than one year.

Of the liabilities to banks, EUR 15,657k is secured by property liens and EUR 4,724k by similar rights.

Contingent liabilities

in EUR '000	
Contingents from notes	14 882
Bonds and guarantees	2 618
Collateral for third-party liabilities	–
Warranties	446

Other financial obligations

in EUR '000	
Purchase commitments	40 455
Financial obligations resulting from rent and lease agreements	48 060
Others	970

NOTES ON THE INCOME STATEMENT OF THE MAHLE GROUP

In order to align more closely with the international standards, the income statement of the MAHLE Group is grouped in accordance with the cost of sales method for the first time in 2006. The sales are set against the expenditure incurred in their realization, which is allocated in principle to the functional divisions production, sales, general administration, and research and development. The previous year's figures were adjusted accordingly.

The cost of sales includes the material and production costs incurred in the realization of the sales and the landed costs of the trade business. The costs of the allocation to accruals for warranties are also included in this item.

The marketing costs include, in particular, personnel and equipment costs, depreciation allocated to the sales division, logistics, market research, sales promotion, shipping and handling, and advertising costs.

The general administration costs include personnel and equipment costs as well as depreciation allocated to the administration division.

The personnel and equipment costs and depreciation allocated to the research and development division are of considerable importance to the MAHLE Group. In order to present the economic status of the Company more clearly, they have been included as separate items in the breakdown.

Sales by business unit

in EUR '000	
Product line Piston Systems	1 279 025
Product line Cylinder Components	482 686
Product line Valve Train Systems	527 291
Product line Air Management Systems	690 324
Product line Liquid Management Systems	509 603
Profit center Aftermarket	450 990
Profit center Small Engine Components	122 960
Profit center Large Engine Components	94 218
Profit center Motorsports	46 868
Profit center Industrial Filtration	81 424
Profit center Engineering Services and others	28 631
Total	4 314 020

Sales by geographically defined market

in EUR '000	
Europe	2 336 563
America	1 212 647
Asia, Africa, Australia	764 810
Total	4 314 020

Personnel expenses

in EUR '000	
	1 209 007

Depreciation on property, plant and equipment

in EUR '000	
Total	223 567
Thereof extraordinary on account of limited use	–

Interest and similar expenses

The interest expense from the appropriation to accruals for pensions and similar obligations, amounting to EUR 15 205k, is shown here.

Taxes on income

The taxes on income include deferred tax expenses of EUR 936k.



OTHER NOTES

Average headcount (without apprentices) over the year

Blue collar workers	28 074
White collar workers	9 492
Total	37 566

Derivatives as of December 31, 2006

Derivatives not yet settled at the balance sheet date in accordance with Secs. 285, 314 HGB can be broken down as follows:

in EUR '000	Nominal amounts	Current value* to be attributed
Transactions relating to interest	177 669	823
Transactions relating to currency	313 336	26 156
Transactions relating to commodity	38 342	- 146
Transactions relating to credit default	13 364	- 676

* The current value attributed to the currency-related transactions corresponds to the market value of the derivatives at the balance sheet date which is identified in accordance with the mark-to-market method. All other transactions are based on recognized financial/mathematical models.

The derivative contracts as of December 31, 2006 are placed exclusively with banks. Appropriate accruals were formed to cover any potential losses from the transactions mentioned above.

Remuneration paid to the members of the Supervisory Board and the Management Board of MAHLE GmbH (parent company)

in EUR '000	
Supervisory Board	147
Management Board	4 350

The total remuneration paid to the Management Board comprises fixed and variable components. The fixed portions for 2006 came to EUR 1,622k, and the variable compensation for 2006 to EUR 2,304k. The remuneration shown also includes a partial amount for the 2005 business year. The fixed portions include benefits in kind, which consist primarily of the non-cash benefits of having company cars.

Remunerations paid to former executive directors and their descendants amounted to EUR 1,554k.

An amount of EUR 10,300k is set aside for this group of persons in the pension accruals as of December 31, 2006.

Stuttgart, March 20, 2007

The Executive Directors of MAHLE GmbH


Heinz K. Junker


Hans Peter Coenen


Hans-Josef Enning


Michael Glowatzki


Peter Grunow


Bernhard Volkmann

AUDIT OPINION

The auditors has issued the following opinion on the complete consolidated financial statements and group management report.

We have audited the consolidated financial statements prepared by MAHLE GmbH, Stuttgart, comprising the balance sheet, the income statement, the notes to the consolidated financial statements, cash flow statement, and statement of changes in equity, together with the group management report for the fiscal year from January 1 to December 31, 2006. The preparation of the consolidated financial statements and the group management report in accordance with German commercial law is the responsibility of the Company's management. Our responsibility is to express an opinion on the consolidated financial statements and on the group management report based on our audit.

We conducted our audit of the consolidated financial statements in accordance with Sec. 317 HGB ("Handelsgesetzbuch": German Commercial Code) and German generally accepted standards for the audit of financial statements promulgated by the Institut der Wirtschaftsprüfer (Institute of Public Auditors in Germany: IDW). Those standards require that we plan and perform the audit such that misstatements materially affecting the presentation of the net assets, financial position and results of operations in the consolidated financial statements in accordance with German principles of proper accounting and in the group management report are detected with reasonable assurance. Knowledge of the business activities and the economic and legal environment of the Group and expectations as to possible misstatements are taken into account in the determination of audit procedures. The effectiveness of the accounting-related internal control system and the evidence supporting the disclosures in the consolidated financial statements and the group management report are examined primarily on a test basis within the framework of the audit. The audit includes assessing the annual financial statements of the entities to be included in consolidation, the determination of the entities to be included in consolidation, the accounting and consolidation principles used and significant estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements and the group management report. We believe that our audit provides a reasonable basis for our opinion.

Our audit has not led to any reservations.

In our opinion, based on the findings of our audit, the consolidated financial statements comply with the legal requirements and give a true and fair view of the net assets, financial position and results of operations of the Group in accordance with German principles of proper accounting. The group management report is consistent with the consolidated financial statements and as a whole provides a suitable view of the Group's position and suitably presents the opportunities and risks of future development.

Stuttgart, March 23, 2007

Ernst & Young AG
Wirtschaftsprüfungsgesellschaft
Steuerberatungsgesellschaft

Elkart
German Public Auditor

Marbler
German Public Auditor



BALANCE SHEET OF MAHLE GMBH
AS OF DECEMBER 31, 2006

Assets

in EUR '000		Dec.31, 2006	Dec.31, 2005
Fixed assets			
Property, plant and equipment	74 273		68 081
Financial assets	786 657		787 348
		860 930	855 429
Current assets			
Inventories	51 491		53 758
Accounts receivable and other assets			
Trade receivables	57 729		50 927
Other accounts receivable and other assets	117 090		154 629
		174 819	205 556
Cash and cash equivalents	217 519		40 208
		443 829	299 522
Prepaid expenses		35	270
		1 304 794	1 155 221

Equity and liabilities

in EUR '000		Dec.31, 2006	Dec.31, 2005
Equity			
Subscribed capital	150 000		150 000
Capital reserves	166 430		166 430
Revenue reserves	512 400		404 500
Unappropriated retained earnings	6 011		6 339
		834 841	727 269
Accruals			
Accruals for pensions and similar obligations	133 509		135 783
Other accruals	87 277		95 467
		220 786	231 250
Liabilities			
Liabilities to banks	78 362		99 208
Trade payables	25 206		19 315
Other liabilities	145 599		78 179
		249 167	196 702
		1 304 794	1 155 221

INCOME STATEMENT OF MAHLE GMBH
FROM JANUARY 1 TO DECEMBER 31, 2006

in EUR '000	2006	2005
Sales	484 644	499 353
Cost of sales	- 403 749	- 436 266
Gross profit on sales	80 895	63 087
Selling expenses	- 25 905	- 27 249
General administrative expenses	- 39 586	- 35 870
Research and development expenses	- 31 189	- 25 149
Other operating income	35 811	55 416
Other operating expenses	- 38 084	- 36 905
	- 18 058	- 6 670
Investment income	30 494	35 365
Income/expense from profit and loss transfers	134 251	106 952
Amortization of financial assets	- 21 886	- 26 675
Interest	- 1 906	- 5 542
Income from ordinary business activities	122 895	103 430
Taxes on income	- 8 513	- 4 233
Other taxes	- 510	- 555
Net income for the year	113 872	98 642



MEMBERS OF THE SUPERVISORY BOARD

Dr. rer. pol. Klaus P. Bleyer*Chairman*

Former Chairman of the Management Board of ZF Friedrichshafen AG, Friedrichshafen, Germany

Jörg Hofmann*Deputy Chairman**until December 31, 2006*

District Administrator of Industriegewerkschaft Metall Baden-Württemberg, Stuttgart, Germany

Bernd Hofmaier Schäfer*Deputy Chairman**effective January 1, 2007*

Chairman of the Central Works Council of MAHLE Group Germany

Rolf Allmendinger

Former Chairman of the Supervisory Board of WMF Aktiengesellschaft, Geislingen, Germany

Herbert Bossert

Executive Secretary of the Central Works Council of MAHLE Group Germany

Martin Bücher

Deputy Chairman of the Central Works Council of MAHLE Group Germany

Anton Czink*until December 31, 2006*

Deputy Chairman of the Central Works Council of MAHLE Group Germany

Hubert Dünneleier*effective January 1, 2007*

Union Secretary of Industriegewerkschaft Metall, Local Administrative Office, Stuttgart, Germany

Prof. Dr. jur. Wolfgang Fritzemeyer

LL. M., Attorney-at-Law
Baker & McKenzie, Munich, Germany

Dipl.-Kfm. Horst H. Geidel

Chairman of the Supervisory Board of Behr GmbH & Co., Stuttgart, Germany

Dr. rer. pol. Rolf A. Hanssen

Former Chairman of the Management Board of MTU Friedrichshafen GmbH, Friedrichshafen, Germany

Thomas R. Letsch

Vice President Sales and Application Engineering Commercial Vehicles of MAHLE International GmbH

Prof. Dr.-Ing. Stefan Pischinger

Director and Professor, Institute of Combustion Engines RWTH Aachen, Germany

Willi Ritter

Chairman of the Works Council of Stuttgart plant and the European Works Council of MAHLE Group

Hansjörg Schmierer

Managing Director of Industriegewerkschaft Metall, Local Administrative Office, Stuttgart, Germany

Dipl.-Kfm. Dieter Schnabel

Former Chairman of the Management Board of Robert Bosch Ltda., Campinas, Brazil

Manfred Steidle*effective January 1, 2007*

Deputy Chairman of the Central Works Council of MAHLE Group Germany

Dipl.-Ing. Hans-Ulrich Wacker

Former Executive Vice President of MAHLE Group

REPORT OF THE SUPERVISORY BOARD



Dr. Klaus P. Bleyer

The Supervisory Board would like to express its gratitude to member and Deputy Chairman of the Supervisory Board, Jörg Hofmann, who retired as of December 31, 2006, for his many years of constructive cooperation. Hubert Dünneleier was appointed member of the Supervisory Board by the Stuttgart district court ("Amtsgericht Stuttgart") for the remaining term of office. Bernd Hofmaier-Schäfer was elected Deputy Chairman of the Supervisory Board as of January 1, 2007.

Anton Czink also left the Supervisory Board as of December 31, 2006, having reached retirement age. Mr. Czink had been a member of the Supervisory Board since 1993. The Supervisory Board would like to thank Mr. Czink for his many years of valuable work on this committee. His elected successor, Manfred Steidle, replaces him as a member of the Supervisory Board as of January 1, 2007.

During the year under report, the Supervisory Board was informed regularly through oral and written reports from the Management Board and during meetings on the status and development of business of the Company and the MAHLE Group. The Supervisory Board held three ordinary meetings and one extraordinary meeting.

Ernst & Young AG Wirtschaftsprüfungsgesellschaft Steuerberatungsgesellschaft, Stuttgart, Germany, audited the Annual Financial Statements and the Status Reports of the MAHLE Group and of MAHLE GmbH for the 2006 business year, rendering an unqualified audit opinion. The Supervisory Board agrees with the results of the audit.

The Supervisory Board approves the Annual Financial Statements and the Status Reports of the MAHLE Group and of MAHLE GmbH, and does not raise any objections to the appropriation of income as proposed by the Management Board.

Stuttgart, April 20, 2007

For the Supervisory Board

A handwritten signature in blue ink, appearing to read "K.P. Bleyer".

Dr. Klaus P. Bleyer
Chairman



MANAGEMENT BOARD

Prof. Dr.-Ing. Heinz K. Junker

Chairman and CEO

Sales and Advanced Development
Communications, Legal, and Internal Audit
Product Line Cylinder Components
Profit Centers Aftermarket and Motorsports

Dr.-Ing. Hans Peter Coenen

Corporate Executive Vice President and
General Manager
Product Line Piston Systems
Profit Centers Large Engine Components and
Small Engine Components

Dr.-Ing. Hans-Josef Enning

Corporate Executive Vice President and
General Manager
Product Line Valve Train Systems
Corporate Quality Management

Michael Glowatzki

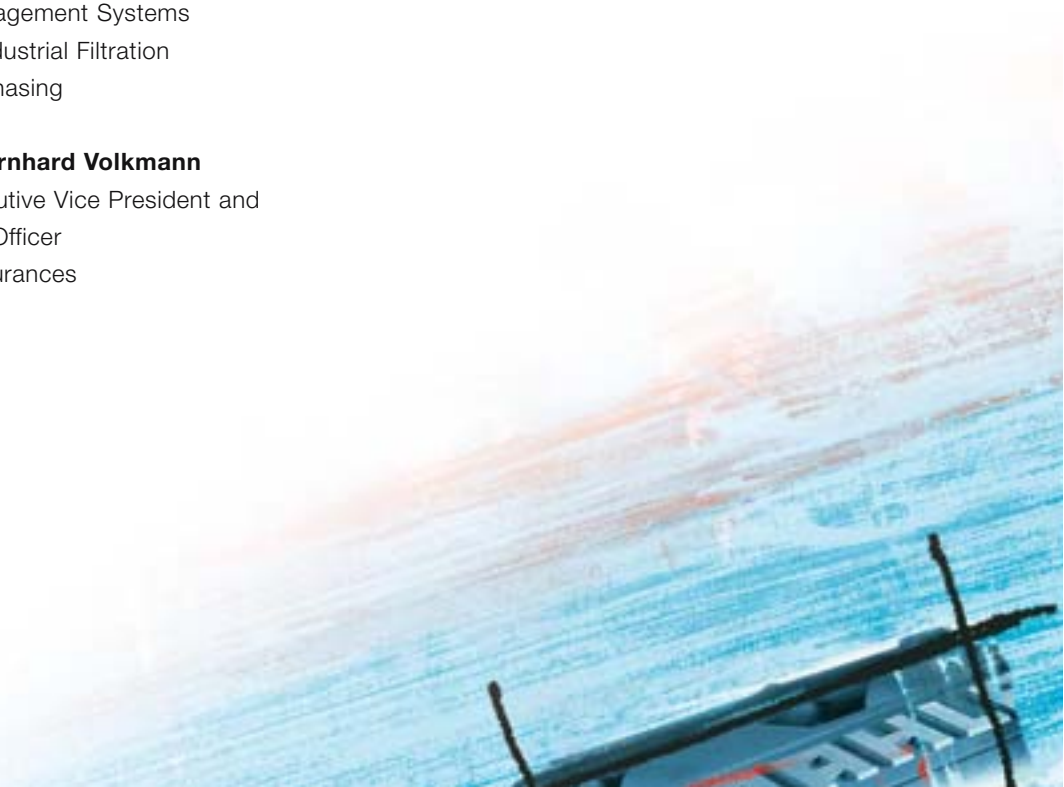
Corporate Executive Vice President
Human Resources

Dipl.-Kfm. Peter Grunow

Corporate Executive Vice President and
General Manager
Product Lines Air Management Systems
and Liquid Management Systems
Profit Center Industrial Filtration
Corporate Purchasing

Dr. rer. pol. Bernhard Volkmann

Corporate Executive Vice President and
Chief Financial Officer
IT Services, Insurances







COMMERCIAL/GENERAL GLOSSARY

Acquisition

Purchase of companies or parts of companies.

Aftermarket

Sale of products to independent market: in spare part business parallel with or following series production.

Audit

Investigation procedures used to assess employed processes of the organization in terms of the fulfillment of requirements and guidelines.

Best practice

Method for success—Anglo-American business term. When a company acts according to best practice, it uses proven, cost-effective processes, technical systems, and business processes, which make it an industrial model for others, at least in the major fields of activity.

BRIC countries

Acronym for Brazil, Russia, India, and China. These countries are generally regarded as major emerging growth markets.

Consolidation

In the consolidation process, intercompany holdings, receivables, liabilities, expenditure, income, and profits are eliminated in order to compile consolidated financial statements in line with the entity theory.

Consolidation group

Comprises the parent company, all subsidiaries and participations that must be considered in accordance with the regulations of the HGB on the date on which the consolidated financial statements are drawn up.

Corporate identity

The strategically planned and operationally implemented self-portrayal and behavior of a company, both internally and externally, based on an established corporate philosophy, a long-term corporate mission statement and a defined (ideal) image—with the aim of achieving uniform internal and external representation in everything that the company does.

Cost of sales method

Type for the presentation of the profit and loss statement. In the cost of sales method, the sales are set against the manufacturing costs of the goods and services sold. Expenditures are mainly allocated to the corporate divisions' production, sales, and general administration.

Deferred tax assets

As a result of different accounting regulations for the tax and commercial balance sheets, the net income according to tax law and according to commercial law may differ. Because, in this case, the tax expense derived from the tax balance sheet considers the net income according to commercial law only to a limited extent, deferred tax assets are recognized in the balance sheet to compensate for differences.

EBIT

Earnings before interest and taxes.

First consolidation/new consolidation

First consideration of Group member companies in the balance sheet of the absorbing subsidiary (usually if holding exceeds 50%).

Forward sourcing

Purchasing activities during the development process.

German Corporate Governance Code

Sets basic statutory standards for the management and for monitoring of German companies listed on the Stock Exchange (corporate governance) and comprises internationally and nationally recognized standards of good and responsible corporate governance.

Gross domestic product (GDP)

Measure of the economic performance of a national economy during a specified period. It measures the value of the goods and services (added value) produced within the country, except those treated as intermediate consumption for the production of other goods and services.

Joint venture

Business entity which is operated jointly by two or more companies on the basis of a cooperation agreement.

Key account structure

Type of sales organization geared toward purchasers or purchaser groups. The key account manager is available to key customers as a permanent contact.

Knowledge management

Consciously managing knowledge as a resource and using it in a targeted manner within the company.

Mercosur

Mercosur (Mercado comum do Cone Sul—Southern Common Market), is a trade network made up of Argentina, Brazil, Paraguay, and Uruguay, as well as the two new partner countries Bolivia and Chile, which is modeled on the European Union and officially came into effect on January 1, 1995.

NAFTA

Acronym for the free trade zone founded on January 1, 1994—North American Free Trade Agreement. Its members are the United States of America, Canada, and Mexico.

Net financial situation

Net amount of liabilities to banks and monetary current assets.

OE/OEM

Original Equipment, Original Equipment Manufacturer.

OES

Original Equipment Services—original spare parts.

Organic growth

Part of the growth (of a company) resulting from internal forces and not from acquisitions.

Profit and loss statement

Method for determining a company's profit or loss. In accordance with the HGB, the possible methods are the cost of sales method and the total cost method.

Profit center

The profit center is an organizational subdivision for which the profit for the period is calculated separately. The profit centers usually operate as independent companies, with the aim of earning as high a profit as possible (profit responsibility).

Trade balance deficit

If a country imports more goods and services than it exports, the trade balance of a national economy shows a deficit.

TECHNICAL GLOSSARY

Air impulse valve

Valve located in the intake pipe ahead of the cylinder head, which is regulated electromagnetically in order to achieve variable charge exchange control.

Articulated piston

MAHLE developed the 2-piece FERROTHERM® piston to accommodate the high loads on high-performance engines in commercial vehicles. The two parts of the piston are connected only by the piston pin, i.e., the guiding and sealing functions are separated, as are the heat dissipation and transmission of power.

CamInCam® camshaft

Variable camshaft consisting of two shafts, one inside the other. The exhaust cams are connected firmly to the outer shaft, and the intake cams are joined to the inner camshaft. This achieves the functionality of two adjustable camshafts in the installation space of one camshaft.

Camshaft, cast

Casted in the single piece, the camshaft is then machined.

Camshaft, composite

The composite camshaft consists of the individual parts main shaft, drive element, cams, and other parts, assembled by means of thermal shrink fit.

Chilled cast iron camshaft

When manufacturing a camshaft using chilled cast iron, casting techniques ensure that the cast iron on the cams solidifies more quickly, forming a hard carbide structure.

Dethrottling

Reducing the throttling loss, for example by means of exhaust gas recirculation, low-displacement supercharged engines, calibration of the intake pipe and exhaust system, cylinder shut-off, or by completely removing the throttle valve.

Downsizing

The performance and torque characteristics of smaller engines are improved by increasing the mean effective pressure, allowing them to replace larger engines.

EGR assembly

Assembly consisting of EGR valve and EGR cooler with bypass. Depending on the definition used, the mixing chamber is part of either the EGR module or the intake module.

Exhaust gas recirculation (EGR)

In exhaust gas recirculation, some of the exhaust gas is added to the intake air. This results in a reduction of nitrogen oxides (NO_x) during combustion, allowing the compliance with emissions limits.

Flex-fuel vehicle (FFV)

Flex-fuel vehicles (FFV) or dual-fuel vehicles can run on either pure gasoline or a variety of similar fuels, such as mixtures of ethanol, bioethanol, or methanol and gasoline.

Forged fracture-split connecting rod, cracking technology steel connecting rod

The fracture-splitting of the big end connecting rod in two parts is referred to as cracking.

Fully variable valve train

Type of valve control in which valve lift, valve opening time, and valve timing can be varied. Its main objective is to allow the engine to run without a throttle valve to reduce throttling loss.

HCCI—homogeneous charge compression ignition

An engine concept in which the combustion of a homogeneous mixture of fuel and air, distributed evenly within the combustion

chamber, begins almost simultaneously throughout the combustion chamber. The ignition is triggered by the increase in temperature resulting from the compression and any radicals remaining in the combustion chamber.

Hollow valve

Lightweight steel valve configured as a hollow body. The stem consists of a precision steel pipe. Valve cone and valve plate are manufactured from sheet metal parts. Sodium-filled hollow valves are used for engines subject to extremely high thermal loads.

Intake module

Assembly consisting of several combustion air guide components located in front of the combustion chamber, including the intake pipe, throttle valve, and, in vehicles with exhaust gas recirculation, the mixing chamber.

Intermetallic phase

Intermetallic compound (also called intermediate phase)—a homogeneous chemical compound of two or more metals.

Impactor

Component in which particles are deposited as a result of their inertia, i.e., because of their mass and diameter, the particles cannot follow the flow field of the carrier gas and therefore collide with an obstacle.

MONOTHERM® piston

MAHLE trademark for a single-piece forged steel piston. The piston skirt is firmly connected to the pin bore and the piston crown.

NIKASIL®-coated cylinder crankcase

MAHLE trademark for a protective surface coating for engine components, particularly cylinder liners. It improves the tribological properties of the cylinder bore and the interaction between cylinder liner and piston.

Piston/connecting rod assembly

Assembly consisting of piston, piston rings, connecting rod, piston pin, and pin retainer.

Power cell unit (PCU)

Assembly consisting of piston, piston pin and pin retainer, rings, cylinder liner, connecting rod, and bearings.

PVD coating

Physical vapor deposition—vacuum-based coating methods or thin-film technologies in which the coating is vapor-deposited directly onto the surface by means of condensation of a material vapor of the starting material.

Roller-type cam follower, switchable; roller tappet

The movement of the valves is triggered by the camshaft and transferred to the valve shaft via transfer elements, e.g., roller-type cam followers or roller tappets. Switchable roller-type cam followers make it possible to switch between full, partial, and zero valve stroke.

Supercharging

Increases the efficiency of a combustion engine: More air and thus more oxygen is pumped into the combustion chamber, thereby improving its volumetric efficiency and performance.

Tribology

Tribology is the science of friction, lubrication and wear of interacting bodies in relative motion.

Valve train

Assembly for controlling the opening and closing of the gas exchange valves of a combustion engine.



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