Kolbenschmidt Pierburg AG

Annual Report 2004

KOLBENSCHMIDT
PIERBURG

Kolbenschmidt Pierburg in Figures

[1] Kolbenschmidt Pierburg in figures		2000	2001	2002	2003	2004
Net sales	€ million	1,776.2	1,825.5	1,882.6	1,884.2	**1,940.8**
EBITDA	€ million	202.0	238.4	234.8	239.1	**260.7**
EBIT	€ million	54.5	90.5	97.4	103.1	**138.9**
EBT	€ million	21.6	49.5	60.1	72.6	**110.8**
Net income	€ million	7.4	31.8	36.7	43.2	**79.4**
Gross cash flow	€ million	160.8	174.1	170.0	170.0	**188.1**
[2] [3] Capital expenditures	€ million	171.1	174.6	144.3	126.5	**132.7**
[4] Amortization/depreciation	€ million	147.5	145.6	133.9	132.0	**121.8**
R+D expenditures	€ million	79.1	79.8	85.6	81.4	**97.2**
Accounting equity	€ million	313.7	341.1	332.9	363.2	**428.3**
Total assets	€ million	1,384.0	1,338.3	1,251.9	1,214.3	**1,224.9**
EBIT margin	in %	3.1	5.0	5.2	5.5	**7.2**
ROCE	in %	6.4	10.1	11.8	13.8	**20.0**
Earnings per share	€	0.28	1.18	1.32	1.51	**2.79**
Total dividend	€ million	34.6	14.0	14.0	14.0	**19.6**
Dividend per share	€	1.30	0.50	0.50	0.50	**0.70**
Headcount (Dec. 31)		12,164	11,662	11,535	11,316	**11,364**

[1] *2001 after adjustment under IAS 8; the adjustments are insignificant, both individually and in the aggregate*

[2] *Excluding financial investments and additions to goodwill*

[3] *Beginning in 2002, tooling grants/allowances have been directly offset against capital expenditures*

[4] *As from 2001, excluding goodwill amortization*

Kolbenschmidt Pierburg Group at a glance

Locations

Divisions

Pierburg

Systems and components
for air supply
and emission control

Oil and water pumps,
vacuum pumps

Sales
€890 million

Headcount
3,470

Location
Germany
France
Italy
Spain
Czech Republic
USA
Brazil
China (Joint Venture)

KS Pistons

Passenger car pistons
Piston modules

Commercial-vehicle pistons

Large-bore pistons

Sales
€580 million

Headcount
5,570

Location
Germany
France
Czech Republic
USA
Canada
Brazil
Japan
China (Joint Venture)

KS Plain Bearings

Plain bearings, Bushings
Thrust washers

Dry bearings (Permaglide)

Continuous NF castings

Sales
€160 million

Headcount
980

Location
Germany
USA
Brazil

KS Aluminum Technology

Aluminum
Engine blocks

Sales
€180 million

Headcount
930

Location
Germany

Motor Service

Automotive parts
for engine repair
and workshops

Sales
€160 million

Headcount
380

Location
Germany
France
Turkey
Brazil
Czech Republic

Kolbenschmidt Pierburg lays the foundations for sustained growth and a further improvement in profitability

Under circumstances that continued to be difficult both at home and abroad, in fiscal 2004 the Kolbenschmidt Pierburg Group achieved another clear improvement in performance. In the process, we exceeded our operational goals for the year and initiated important steps to ensure the long-term growth of the company.

During the year under review, the strategic development of the company was characterized by

- the launch of an innovation campaign fueled by a 19.4 percent increase in R&D spending;
- the successful market debut of pioneering new product innovations;
- the acquisition of highly promising, forward-looking projects thanks to technologically superior solution concepts;
- the continuation of our ongoing strategy of internationalization, including a significant rise in the volume of business in North America and the creation of a development center in Japan; and
- the successful integration of the new aftermarket units acquired in Germany and the expansion of aftermarket operations in Brazil.

The company's operating performance is revealed by positive trends in the following ratios:

- a 4.6 percent increase in organic growth;
- a 1.7 percentage point rise in return on sales to 7.2 percent;
- a 6.2 percent improvement in ROCE to 20.0 percent;
- a 83.8 percent increase in net income for the year to €79.4 million;
- an improvement in free cash flow by 76.6 percent to €119.9 million; and
- a substantial reduction in liabilities owed to banks, making the company virtually free of debt owed to financial institutions.

Contents

Report of the Supervisory Board

During fiscal 2004, the Supervisory Board of Kolbenschmidt Pierburg AG performed the functions and duties incumbent on it under law and the bylaws. It regularly advised the Executive Board, monitoring its management of the company. The Supervisory Board was included in decisions of fundamental importance to the company.

The Executive Board reported regularly, timely and comprehensively to the Supervisory Board on the Company's and the Group's situation and development, as well as on fundamental issues of business policy, management and corporate planning, including finance, capital expenditure and human resources planning, the risk position and risk management matters. In addition, the Supervisory Board was regularly briefed in writing on the Kolbenschmidt Pierburg Group's business situation and trends.

The Supervisory Board met twice in the first and twice in the second half-year periods of 2004. The Supervisory Board's Personnel Committee members convened twice in fiscal 2004 (March 17 and September 1, 2004) and took the actions considered necessary.

When the Auditing Committee (previously known as the Finance Committee) met on March 11, 2004, it dealt with the preparatory deliberations concerning the 2003 annual accounts. At its meeting of November 15, 2004, the Auditing Committee decided on the main points of the 2004 annual accounts audit, after which the Chairman of the Supervisory Board awarded contracts to the statutory auditors. There was no reason for the Slate Submittal Committee to convene.

The full Supervisory Board was duly informed about its committees' activities. At the full Supervisory Board meetings, the members discussed in detail the situation and development of the Group, the various divisions and all major subsidiaries in Germany and abroad, as well as all significant transactions. At its meeting held on November 22, 2004, the Supervisory Board passed the Declaration on the German Code of Corporate Governance published on January 10, 2005. In addition, a review of the Supervisory Board's efficiency was also carried out in 2004.

Furthermore, the Supervisory Board dealt with issues of strategic and organizational orientation and, at its meeting of November 22, 2004, deliberated on the Group's medium-term plans. All Executive Board actions requiring Supervisory Board approval were submitted in full on a timely basis to the Supervisory Board. After careful scrutiny and detailed discussion, all items were approved.

The Chairman of the Supervisory Board was briefed continuously and promptly on all major transactions involving the company and the Group. He had major matters and issues referred to the Supervisory Board for discussion and met regularly with the Chairman of the Executive Board to review strategy, current business, and risk management issues. The separate and consolidated financial statements and the management reports of Kolbenschmidt Pierburg AG and the Group for the fiscal year ended December 31, 2004, including the accounting system, were all audited by PwC Deutsche Revision AG, Wirtschaftsprüfungsgesellschaft of Stuttgart, which had been appointed as statutory auditors by the annual stockholders' meeting on May 5, 2004.
On February 28, 2005, the statutory auditors issued their unqualified opinion on both sets of financial statements. Within the scope of the audit, the statutory auditors also had to examine whether the Execu-

tive Board had duly implemented the legally required procedures, and especially if it had set up a monitoring system that would identify at an early stage any risks likely to jeopardize the company's continued existence as a going concern. The auditors declared that the Executive Board had met the requirements of Art. 91(2) German Stock Corporation Act ("AktG"). At its meeting on March 10, 2005, the financial committee of the Supervisory Board reviewed and approved the separate and consolidated financial statements for fiscal 2004 on the basis of the reports and findings of the statutory auditor. The statutory auditors participated in this meeting, reporting on the essential results of the audit and answering questions. No objections were raised. Well before the balance sheet meeting of the Supervisory Board on March 16, 2005, all the members of the Supervisory Board were provided with the annual accounts, the separate and consolidated financial statements, the management reports on the company and the Group, and the report of the statutory auditor. At the balance sheet meeting, the Supervisory Board reviewed these documents in great detail.

The Supervisory Board concurs with the results of the audit, and has reviewed the separate and consolidated financial statements, the management reports on the Company and the Group, and the profit appropriation as proposed by the Executive Board, having raised no objections. At its meeting on March 16, 2005, the Supervisory Board approved the separate and consolidated financial statements for fiscal 2004 as submitted by the Executive Board, which are thus adopted. The Supervisory Board endorses the Executive Board's proposal to the General Meeting for the appropriation of the net earnings for fiscal 2004 that a cash dividend of €0.70 per no-par share be distributed, as well as the allocation of €9,892,546.35 to profit reserves.

The Executive Board's report on affiliations in fiscal 2004 as defined by Art. 312 AktG, and the pertinent report of the statutory auditors, were submitted to the Supervisory Board, which examined the report of the Executive Board and concurs with it, as with the results of the examination by the statutory auditors.

The auditors issued the following opinion on the dependency report of the Executive Board concerning affiliations:

"Based on our examination, which we performed with due professional care, and on our evaluation we certify that

(1) the facts stated in the report are valid;
(2) the Company's consideration for the legal transactions referred to in the report was not unreasonably high."

After reviewing the final results of its own examination, the Supervisory Board has found no reasons for objections to the Executive Board's concluding representation in the report on affiliations for fiscal 2004.

The Supervisory Board thanks all employees of the Kolbenschmidt Pierburg Group for their dedication and commitment in 2004.

Düsseldorf, March 16, 2005

The Supervisory Board

Klaus Eberhardt
Chairman

Letter from the Executive Board

Dr. Gerd Kleinert (57) has been a member of the Executive Board of Rheinmetall AG since 2001. Born in Rüsselsheim, he is responsible for Rheinmetall's Automotive component, and is also Chairman of the Executive Board of Kolbenschmidt Pierburg AG. Dr. Kleinert, who holds a PhD in engineering, previously worked for TRW, VDO, and Adam Opel AG.

Dr. Peter Merten (51) has served on the Executive Board of Kolbenschmidt Pierburg AG since 2002, where he has special responsibility for financial operations and controlling, as well as IT. Born in Stuttgart, he has a PhD in business studies. Dr. Merten previously worked for Rheinmetall DeTec AG, as well as Dornier and the Daimler Benz group.

Ladies and gentlemen,

In fiscal 2004, the Kolbenschmidt Pierburg Group was able not only to maintain the momentum of a very good prior year, but substantially surpassed it with respect to all the main measures of corporate success.

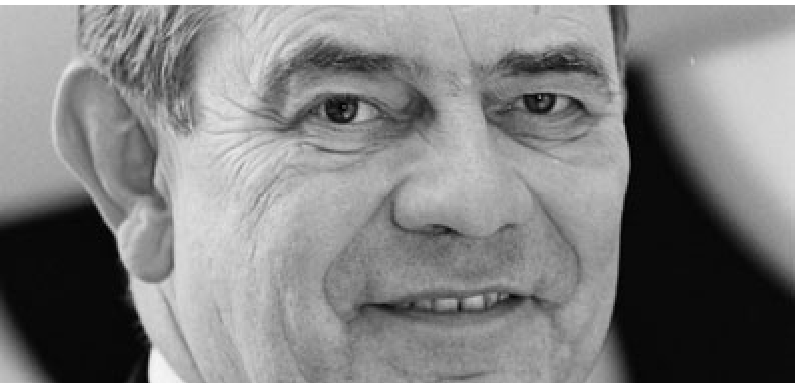
Sales rose to €1,940.0 million from €1,884.2 million. Net income for the year, still €43.2 million the previous year, increased sharply again to €79.4 million.

At the same time, spending on research and development was increased by 19.4 percent, which, coupled with additional investment in internationalization, sets the stage for a global innovation campaign and with it, sustained organic growth.

This extremely gratifying development meant that, with the help of gross cash flow (which increased to €188.1 million), we were able to reduce substantially our liabilities to banks, meaning that the company now owes practically no debts to financial institutions.

This success is the outcome of the global streamlining of structures and the optimization of flows carried out over the past three years, as well as the systematic orientation of the Group's research and development efforts to product and process innovations clearly geared to future needs.

Meriting particular mention was the return to profitability of the Aluminum Technology division, which, still in the red the previous year, ended fiscal 2004 in positive territory.
Moreover, thanks to newly booked orders for the manufacture of engine blocks for premium carmakers, utilization of the division's



Dr. Jörg-Martin Friedrich (59) joined the Executive Board of Kolbenschmidt Pierburg AG in 1998, where he has special responsibility for human resources and legal affairs. Dr. Friedrich, a lawyer with a PhD in law, performed the same duties on the Executive Board of Kolbenschmidt AG from 1988 to 1997, when the company merged with Pierburg AG.

capacity is assured for several years to come. But the KS Pistons and KS Plain Bearings divisions also succeeded in surpassing the previous year's results, in part quite substantially.

At the same time, our divisions were able to expand their operations in markets with strong future growth potential. In the process, the Pierburg division focused on the markets of North and South America, and, by establishing the company Pierburg s.r.o. in the Czech Republic in summer 2004, now has an additional production facility in Eastern Europe. KS Pistons has been busy expanding its operations in East Asia, especially in Japan and China. Thanks to new acquisitions in Germany, the Motor Service division has laid the groundwork for expanding its market presence and optimizing its array of products.

This positive trend clearly vindicates our business policy. In the future, we intend to go on improving our strategic positions, assuring sustained profitable growth through the Group.

We would like to thank you for your confidence in Kolbenschmidt Pierburg and hope that we will be able to count on your continued support in the coming year.

Dr. Kleinert   Dr. Merten   Dr. Friedrich

Kolbenschmidt Pierburg stock

After rising in 2003, the stock market was characterized by a broadly sideways trend in 2004. The DAX fluctuated in a relatively narrow band, ranging roughly between 3,700 and 4,200 points.

Despite the persistently difficult economy environment, Kolbenschmidt Pierburg stock clearly bucked the general trend:

On December 22, 2004 the share peaked at €37.00. At the end of 2004, it closed at €36.01, representing a rise of 57.6 percent compared to the beginning of the year. (In 2003, our share price had already risen from €8.65 to €22.85.)

Rheinmetall AG increased its stake in Kolbenschmidt Pierburg AG to 96.48 percent in December 2004 (Source: Deutsche Börse AG). Kolbenschmidt Pierburg continues to be traded in the Prime Standard.

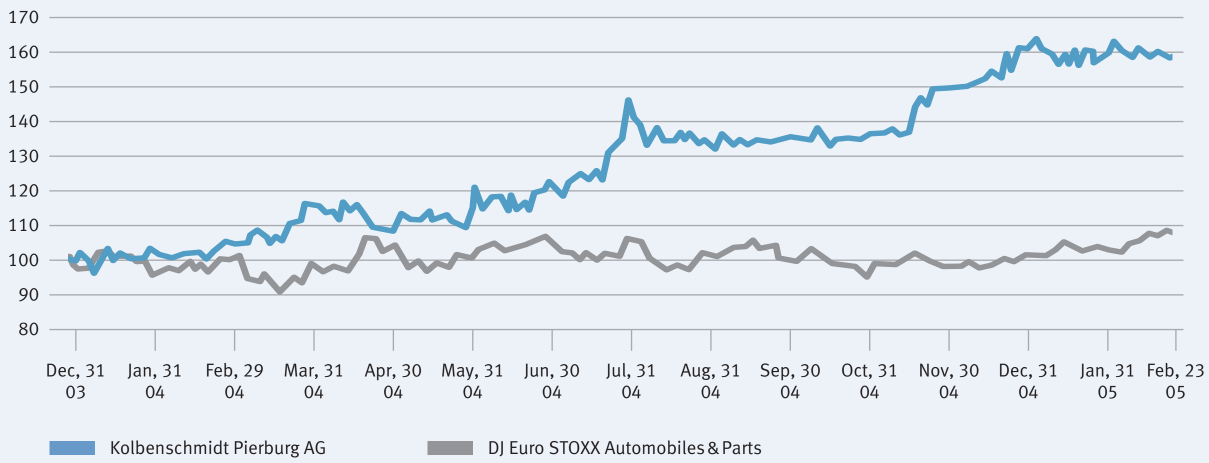
During the year under review, the rating agency Moody's confirmed Kolbenschmidt Pierburg's rating of Baa2. On February 1, 2005, Moody's upgraded the company's Outlook to a Baa2 positive.

Share data

	2003	**2004**
Market capitalization / EBIT	6.2	7.3
Price-earnings ratio (PER)	15.1	12.9
Dividend per share (€)	0.50	0.70
Dividend yield (%)	2.2	1.9

Kolbenschmidt Pierburg AG vs. DJ Euro STOXX Automobiles & Parts

Indexed to Kolbenschmidt Pierburg stock at December 30, 2003 (up to February 23, 2005)



Corporate Governance

Kolbenschmidt Pierburg AG adheres to a policy of responsible and transparent corporate management and control, oriented to securing a sustained increase in corporate value. Even in the past, the company's practices largely corresponded to the recommendations and suggestions of the German Corporate Governance Code. The intention is to reinforce further the confidence of German and international investors, our business partners, our employees and the public at large in the management and monitoring of the Kolbenschmidt Pierburg Group. Kolbenschmidt Pierburg AG sees Corporate Governance as a continuous process for improving the management and control of the company in response to ongoing experience and regulations as well as steadily evolving national and international standards.

The Executive Board

The Executive Board has overall responsibility for managing the company's operations in accordance with uniform objectives, plans and guidelines. The responsibilities and prerogatives of the Executive Board derive from statutory regulations, the bylaws of Kolbenschmidt Pierburg AG and the internal operating procedures of the Executive Board. The Executive Board of Kolbenschmidt Pierburg AG consists of three members, with each member assigned special responsibility for a particular sphere; however, they are enjoined to place the overall wellbeing of the company above the interests of their own particular sphere. The Chairman of the Executive Board coordinates the work of the Executive Board.

In the notes to the consolidated financial statements, the compensation of the entire Executive Board of Kolbenschmidt Pierburg AG is stated in summarised, informative fashion, broken down into fixed, performance-related and long-term incentive portions. For the shareholder, it is crucial to have an impression of the entire Executive Board, which, as a collegiate body, is charged with joint responsibility for managing the company. The summarized presentation contains all the information necessary for making a rational assessment of the performance of the Executive Board, as well as enabling an assessment of whether the ratio of fixed and performance-related compensation components is appropriate, and whether the necessary performance incentives for the members of the Executive Board have been established. A statement of individual compensation would not contain information relevant to the capital market, nor would it improve the overall quality of the information provided. Moreover, it should be noted that disclosing the compensation paid to individual members of the Executive Board can lead to an undesirable leveling of task- and performance-related remuneration, while the disclosure of salaries could result in a ranking in the importance of individual members of the Executive Board.

Compensation is set by the Supervisory Board at an appropriate level and on the basis of a personal performance assessment, with due regard to any other compensation paid by the Group. Assessment criteria for defining an appropriate remuneration of Executive Board members include each member's responsibilities and personal performance, as well as the financial strength, success and future prospects of the company, taking into account comparable companies in the industry. Compensation is set at an internationally competitive level capable of attracting highly qualified executives; the amount and structure of Executive Board compensation is oriented to that of comparable German and foreign firms.

Normally, remuneration consists of a 60 percent fixed-income component and a 40 percent variable component, with 70 percent of the variable component in turn consisting of so-called Result Contribution 1 (a comparison of projected and actual figures viz. the plan of one's own unit), and 30 percent relating to Result Contribution 2 (a comparison of projected and actual figures viz. the plan of the next higher own unit), based on the performance indicators EBIT, EBT and ROCE.

A further program has been established to serve as an additional incentive model. It is not linked to the company's share performance, but instead depends exclusively on the absolute increase in "fundamental equity value" based on defined corporate performance ratios.

Introduced in 2004, the program applies to all members of the Executive Board as well as to the top two layers of management beneath the Executive Board.

At the General Meeting on May 5, 2004, the Chairman of the Supervisory Board informed the Executive Board concerning the essential features of the com-

Corporate Governance

pensation system. The basic features of the compensation system also appear on the company's website.

During the year under review, no loans or advances were extended to members of the Executive Board.

The corporation has taken out a Directors' and Officer's Liability Insurance policy for the Executive Board; an appropriate deductible was agreed.

Supervisory Board

The Supervisory Board consists of 12 members. In accordance with the German Codetermination Act of 1976, six members represent the shareholders, while six represent the company's employees. Its current term expires at the end of the General Meeting in 2008. It conducts its activities on the basis of the laws and bylaws, as well as the rules of procedure in force since 2003.

Its committees, composed of an equal number of members, deal with complex issues which fall under the purview of the full Supervisory Board, as well as preparing resolutions of the Supervisory Board. Specifically, the tasks of the committees are as follows:

Personnel Committee
The Personnel Committee is responsible for all personnel matters pertaining to members of the Executive Board, and represents the company in its dealing with members of the Executive Board. Furthermore, it makes preparations for the appointment and reappointment of Executive Board members, submits recommendations to the full Supervisory Board, and, in cooperation with the Executive Board, engages in long-term planning for an orderly succession.

Audit Committee
The Supervisory Board has established an Audit Committee which is responsible for the tasks specified in Clause 5.3.2 of the May 21, 2003 version of the Code. Moreover, it prepares resolutions of the Supervisory Board relating to capital measures and approval of the annual accounts. It is also charged with monitoring the financial structures of the Kolbenschmidt Pierburg Group.

Arbitration Committee
Mandated by the German Codetermination Act, the Arbitration Committee submits personnel proposals to the Supervisory Board when the majority necessary for the appointment of members of the Executive Board has not been attained.

Compensation paid to the Supervisory Board consists of a fixed and a variable component, the latter depending on the amount of the dividend paid out by the company. The existing system of Supervisory Board compensation is set forth in detail in Art. 13 of the company's Articles of Association. Pursuant to Clause 5.4.5, Subclause 1 of the Code, the chairmanship and membership of committees should be taken into account when determining Supervisory Board compensation.

A survey of members of the Supervisory Board revealed no conflicts of interest as defined in Clauses 5.5.2 and 5.5.3 of the Code.

During the year under review, no loans or advances were extended to members of the Supervisory Board.

The corporation has taken out a Directors' and Officer's Liability Insurance policy for the Supervisory Board; an appropriate deductible was agreed.

At the meeting on November 22, 2004, the Supervisory Board reviewed its activities during fiscal 2004, as well as conducting an efficiency audit.

Transparency

Pursuant to Art. 15 of the German Securities Trading Act ("WpHG"), members of the Executive Board and Supervisory Board of Kolbenschmidt Pierburg AG are required to disclose the purchase or sale of Kolbenschmidt Pierburg AG stock. Kolbenschmidt Pierburg AG received no reports of purchase or sale during the period under review; nor did any shareholdings exist which were reportable under the terms of Clause 6.6 of the German Corporate Governance Code.

Originally published on the company's website in January 2005 as a declaration of conformity by the Executive Board and Supervisory Board of Kolbenschmidt Pierburg AG, a statement of the recommendations of the May 21, 2003 version of the Code not adopted by the company appears below:

Declaration of Conformity pursuant to Art. 161 AktG

Pursuant to Art. 161 of the German Stock Corporation Act ("AktG"), Kolbenschmidt Pierburg AG's Executive and Supervisory Boards declare that Kolbenschmidt Pierburg AG has, since the issuance of the preceding declaration of conformity in December 2003/March 2004, fully carried out or will act on, the recommendations of the German Corporate Governance Code Government Commission as amended up to May 21, 2003 and published in the digital Federal Gazette, except for the following recommendation that neither has been nor will be implemented:

– The remuneration paid to each individual Executive and Supervisory Board member (4.2.4 and 5.4.5 of the Code, respectively) will not be disclosed in the notes to the consolidated financial statements.

Since the preceding declaration of conformity disclosed in December 2003/March 2004 Kolbenschmidt Pierburg AG has adopted the following recommendations of the Code as amended up to May 21, 2003:

– As proposed by the Executive Board, the annual stockholders' meeting resolved on May 5, 2004 to amend the clause in Article 13 of Kolbenschmidt Pierburg AG's bylaws on the remuneration of Supervisory Board members to conform with the recommendations of 5.4.5 of the Code. This amendment to the bylaws was recorded by the Commercial Register on May 24, 2004.

– At its September 6, 2004 meeting the Kolbenschmidt Pierburg Executive Board approved by unanimous resolution its rules of procedure regulating the allocation of areas of responsibility and the cooperation in the Executive Board (4.2.1 of the Code).

Düsseldorf, November 2004

The Executive Board   The Supervisory Board

Underlying economic conditions

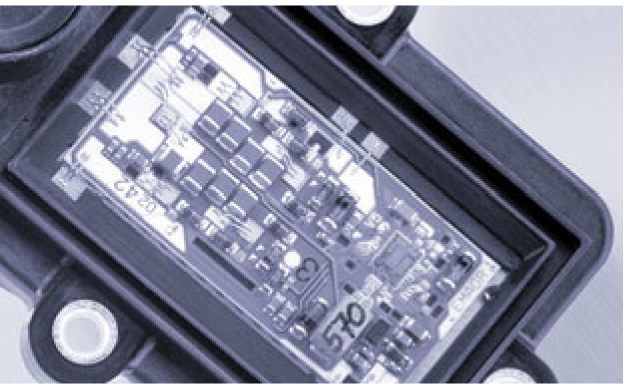
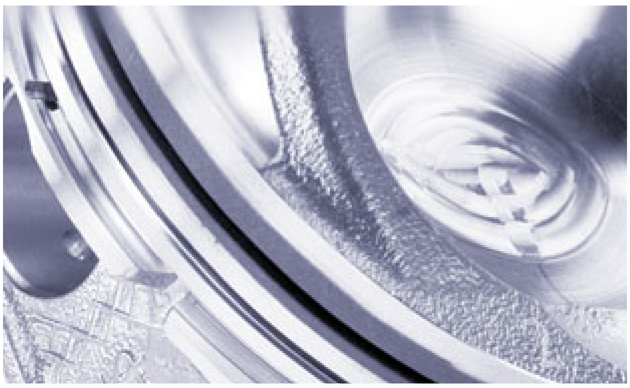
Performance of the world economy

Recovering from a generally weak 2003, the pace of global economic growth picked up appreciably during the course of 2004. According to initial estimates, the world economy grew in real terms by some four percent. Though this positive trend lost momentum during the second half of the year owing to slower growth in the United States and China, it nevertheless represents the world economy's strongest showing since the year 2000. Sharp increases in the price of oil and other raw materials were the primary cause of this slowdown in growth during the final months of 2004.

The contribution of the developed nations to global economic output in 2004 was less marked than that of the emerging markets, which once again grew at an impressive pace. According to OECD estimates, for example, China's gross domestic product expanded by a good nine percent. The Autumn Report of the most important German economic institutes states that the economies of East Asia as a whole grew by nearly 5.5 percent. Russia, too, continues to grow at a very dynamic rate, which the experts put at seven percent.

The OECD estimates that economic growth in the United States topped four percent in 2004, after having come in just under 3.0 percent the year before. In 2004, the Japanese economy grew by 2.6 percent – proving more robust than at any point since 1996. Growth picked up in the euro zone, too, albeit at a moderate level. According to preliminary estimates, economic output in the European Union expanded by 2.4 percent, well up on the previous year's figure of just 1.0 percent.

Germany continues to bring up the rear here, though its rate of growth in 2004, estimated at 1.7 percent, was at least higher than the year before. Private consumption remained sluggish, increasingly burdened by higher energy prices as the year wore on; yet the strength of the world economy clearly benefited German exporters.

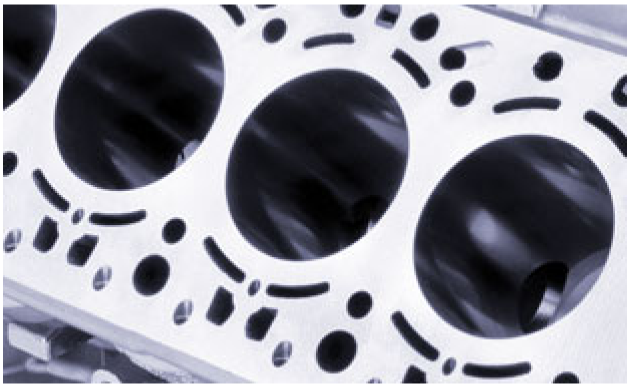

Trends in world automobile production

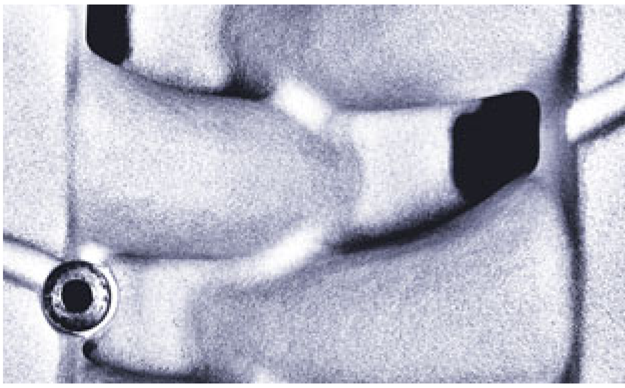
Compared to the figures for the previous year, the international automotive sector recovered somewhat in 2004. According to the best available estimates, global production of light vehicles (i.e. cars and light commercial vehicles) rose by around five percent to 59.3 million units, clearly outstripping the previous year's rate of growth of just two percent. Whereas vehicle output in the Triad markets recovered from last year's fall to rise by one percent to 41.6 million units, production jumped by 23 percent in fast growing South America and by 18 percent in Eastern Europe; the Asia-Pacific region (excluding Japan) likewise attained a double-digit rate of growth, rising by 13 percent.

The Triad markets developed along divergent lines, with the NAFTA countries – the United States, Canada and Mexico – experiencing a one percent decline in production. This was caused by a two percent fall in output (despite rebates and other sales promotion measures) in the US and Mexico, which a six percent increase in Canada was unable to offset. Led by Germany and France, where production grew by two percent and six percent respectively, production in Western Europe increased by two percent. In Japan, output edged up by one percent.

In 2004, the Asia-Pacific region (excluding Japan) was once again the engine of global growth in production. Apart from the greater number of vehicles produced in South Korea, where output was up by seven percent, this was due first and foremost to production hikes in China, where, despite fears of the market overheating, 14 percent more vehicles were made than in 2003. With an output of 3.8 million vehicles, in 2004 China numbered among the world's Top 5 vehicle producers.

In 2004, as the automotive industry gradually shifted into higher gear, the diesel-powered vehicle segment recorded the strongest gains. In Western Europe, an estimated 48% of all newly registered passenger cars were powered by diesel engines. Around the world, sales of vehicles featuring greater fuel efficiency and lower emissions generally grew fastest – with a sustained, simultaneous trend toward higher performance engines. Lightweight materials like aluminum and magnesium, as well as products incorporating mechanical and electronic technologies, continued to make headway.





The situation of the Group

Significant events

Via its subsidiary MSD Motor Service Deutschland GmbH (formerly: MTS Motorenteile-Service GmbH), the Motor Service division took over the engine parts activities of the companies E. Trost GmbH & Co. KG of Stuttgart and PV Autoteile GmbH of Duisburg, effective January 2, 2004. These units were merged with the former MTS Motorenteile-Service GmbH to form a new company, MSD Motor Service Deutschland GmbH. In addition, during the second quarter of 2004, the engine parts activities of Willy Konczewski GmbH & Co. KG of Berlin were acquired and added to MSD Motor Service Deutschland GmbH.

At the beginning of January 2004, the Pierburg division sold its remaining 49% interest in Pierburg Instruments GmbH to the majority shareholder, AVL Holding Ges.m.b.H. of Graz, Austria.

In creating the company Pierburg s.r.o. at Usti in the Czech Republic on May 7, 2004, the Pierburg division laid the groundwork for a further increase in competitiveness and improved earnings power in selected segments. During the second half of 2004, the purchase of land and the construction of a production hall rapidly brought the project to fruition. Production and assembly operations have since commenced.

As part of the ongoing strategic reorganization of the KS Aluminum Technology division, Ideko GmbH was re-founded as KS ATAG GmbH with a simultaneous increase in capital of €5 million, marking the start of a major reorganization. Subsequently, KS Aluminium-Technologie AG was sold by Kolbenschmidt Pierburg AG to KS ATAG GmbH, which in the future will act as the division's holding company. In order to finance the purchasing price, a further increase in capital of €20,0 million was carried out at KS ATAG GmbH. In addition, following the resolution of the General Meeting of Kolbenschmidt Pierburg AG on May 5, 2004 and the entry of KS ATAG in the Register of Companies, a profit transfer agreement was concluded on May 18, 2004 between KS ATAG GmbH and Kolbenschmidt Pierburg AG, coming into force with retroactive effect on January 1, 2004.

In order to provide adequate scope for growth, capital increases were also carried out at the companies Metal a.s., KS Gleitlager GmbH, MSI Motor Service International GmbH and KS Motorac S.A.S.

The trend in sales and earnings

In fiscal 2004, Group sales of Kolbenschmidt Pierburg reached €1,940.8 million, a rise of 3.0 percent compared to the year before. This comparison with the previous year's figure was negatively influenced by the altered foreign exchange rate parities, especially the substantial weakening of the US dollar. Adjusted for these conversion-related currency exchange rate effects, sales actually increased by 4.6 percent. Growth at Kolbenschmidt Pierburg was thus nearly on par with the 4.7 percent increase in global automobile ouput. With regard to the Group's current core markets – Western Europa (which grew by two percent) and NAFTA (which contracted by one percent) – Kolbenschmidt Pierburg significantly outpaced the market.

Breakdown of sales by region *in %*

Compared to the previous year, sales to customers in Germany rose by two percentage points to 34 percent of total Group sales. The share of sales to customers in Europe (excluding Germany) remained unchanged at 44%. Here, declining sales to customers in Hungary, France and the United Kingdom were offset by stronger demand from Poland and Spain. Beyond Europe, the countries of North and Central America were the most important markets, notwithstanding a renewed decline of two percentage points. This was largely due to the decline in business in the US, where conversion-related currency exchange rate effects clearly had an impact. Calculated in local currency, sales exceeded the previous year's level. The remaining world markets continued to account for eight percent of total sales. Not included in the sales figures for the Asia/Pacific region is our share in the sales of the Group's two Chinese joint ventures (both consolidated at equity), which totaled €47.2 million.

Sales by region *€ million*

	2003	**2004**	*change € million*	*change in %*
Germany	604.1	666.5	*62.4*	*10.3*
Europe (without Germany)	833.1	843.7	*10.6*	*1.3*
North and Central America	301.6	272.7	*(28.9)*	*(9.6)*
South America	52.3	62.3	*10.0*	*19.1*
Asia [1]	71.2	71.0	*(0.2)*	*(0.3)*
Other regions	21.9	24.4	*2.7*	*12.3*
Group	**1,884.2**	**1,940.8**	***56.6***	***3.0***

[1] *without the Chinese joint ventures (share of sales in 2003: €46,0 million; in 2004: €47,2 million)*

With the exception of the KS Pistons division, all of the divisions increased their sales in 2004 compared to the year before. In 2004, too, the KS Pistons division generated substantial sales through its production units outside the euro zone. Unfavorable exchange rates compared to 2003 meant that its sales appeared to decline after conversion into euros. Adjusted for the effects of adverse exchange rates, sales of the KS Pistons were up 2.1 percent compared to the figure for the previous year.

Sales by division *€ million*

	2003	**2004**	*change € million*	*change in %*
Pierburg	877.5	889.1	*11.6*	*1.3*
KS Pistons	593.6	581.9	*(11.7)*	*(2.0)*
KS Plain Bearings	147.3	160.2	*12.9*	*8.8*
KS Aluminum Technology	159.8	182.8	*23.0*	*14.4*
Motor Service	138.5	161.4	*22.9*	*16.5*
Other/consolidation	(32.5)	(34.6)	*(2.1)*	*(6.5)*
Group	**1,884.2**	**1,940.8**	***56.6***	***3.0***

The situation of the Group

Sales of the Pierburg division grew by 1.3 percent to €889.1 million. After a slight dip the year before, sales of the division's Air Supply product unit recovered handsomely. Sales of the Emission Control unit remained unchanged compared to 2003. Thanks to strong sales in all of its product groups, the Pumps product unit came close to compensating for the decline in sales brought about by the disposal of its Electrical Fuel Pumps segment the previous year.

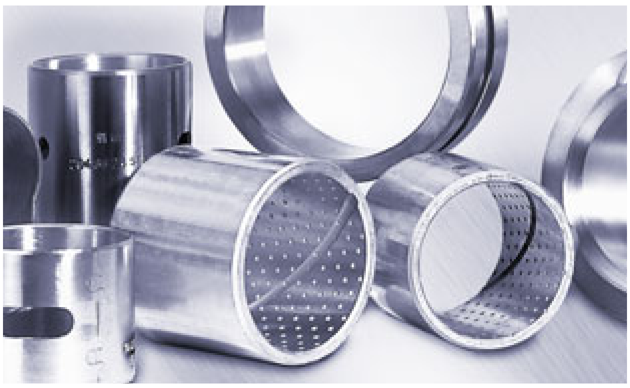
The KS Pistons division ended fiscal 2004 with sales of €581.9 million, a decline of two percent compared to 2003. When adjusted for exchange rate-related effects, however, the decline in sales becomes an increase. In particular, the division's largest unit in North America and the subsidiaries in South America recorded major gains in terms of local currencies.

Following its modest sales performance in 2003, sales of the KS Plain Bearings division rose during the period under review by 8.8 percent to €160.2 million, with all of its product groups contributing to the increase. Meriting particular mention are the Continuous Casting and Metallic Plain Bearings product groups, with the performance of the former reflecting not just larger production volume but also the passing on of higher materials prices.

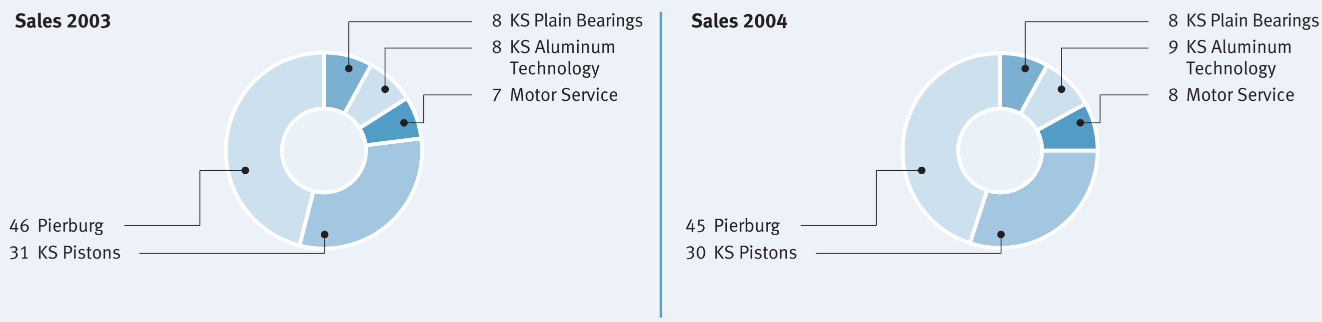
Following the advance payments of the previous year, the KS Aluminum Technology division achieved the expected increase in sales. At €182.8 million, its sales surpassed the previous year's figure by a respectable 14.4 percent. Though sales in the Pressure Casting segment also rose slightly, the bulk of the increase came in the Low Pressure Casting segment, which had already attained significantly higher volume in 2003.

Sales of the Motor Service division expanded by 16.5 percent to €161.4 million. Much of this growth was due to the acquisitions made during the course of 2004. But, despite the difficult market situation in Western Europe and the Middle East, the division achieved organic growth as well, thanks to stronger sales particularly in South America and Eastern Europe.

Compared to the previous year, the distribution of sales among the divisions changed only marginally. Accounting for 45% of Group sales, Pierburg remained the largest division in 2004, followed by KS Pistons with 30%. Each of these divisions gave up one percentage point to the substantially smaller KS Aluminum Technology and Motor Service divisions. The share of KS Plain Bearings remained unchanged at eight percent.



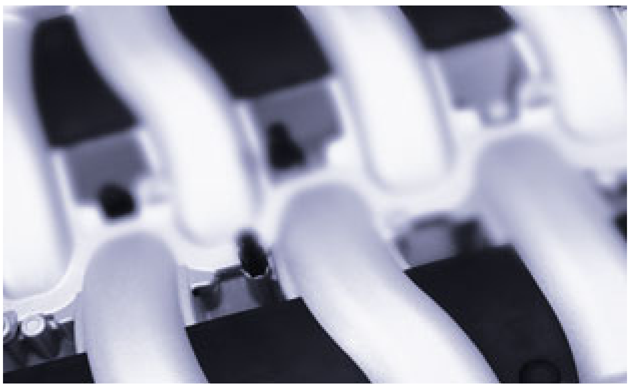
Share of sales by division *in %*



Expanded sales and heightened inventory changes resulted in higher total operating earnings in the Group, which rose by €65.2 million to €1,966.6 million. Other operating earnings declined by €10.4 million to €52.3 million, due first and foremost to the book profit from the sale of the Electrical Fuel Pumps product unit carried the previous year. Material expenses came to €1,010.6 million in 2004, €40.0 million more than the year before. As a result, the material expenses ratio moved up slightly by 0.4 percentage points to 51.4 percent. Conversely, personnel expenses rose by just 5.6 million to €520.8 million. Spending on wages and salaries edged up by €2.1 million to €415.9 million, while expenditure on retirement benefits increased by €3.5 million to €104.9 million. Compared to a year earlier, the sum of material and personnel expenses reveals a slight improvement of 0.2 percentage points to 77.9 percent.

Owing to measures introduced the previous year to limit capital expenditure as well as the decision to dispense with the planned amortization of goodwill (€4 million in 2003), depreciation and amortization declined by €14.2 million to €121.8 million. Other operating expenses edged up by €0.4 million to €243.2 million. Notable was the increased spending on outplacement assistance and severance packages, as well as data processing, maintenance, and research and development. Savings were achieved on expenses for the formation of accruals, guarantees, semi-retirement programs, outsourced services and legal and consulting fees.

The financial result improved by €15.2 million to (€11.7 million). Rising by €2.4 million, the net interest component contained in this figure developed along positive lines, with net interest income remaining at


The situation of the Group

the previous year's level and net interest expense declining to (€28.1 million). Contained in the interest expense are the early repayment penalties for the ahead-of-schedule discharge of liabilities due to banks for 2004, which in subsequent years will lead to a further appreciable decrease in the interest burden. At €15 million, income from trade investments for the period under review exceeded that of the previous year by €7.4 million, largely due to the sale of a trade investment. In the item "other financial expenses and income", income exceeded expenses in 2004, producing a positive result of €1.4 million. The year before, expenses outweighed income, culminating in a loss of €4.0 million. In fiscal 2004, especially positive was the balance of currency gains and currency losses.

Earnings before interest and tax (EBIT) of the Kolbenschmidt Pierburg Group rose by 34.7 percent to €138.9 million. Whereas the KS Aluminum Technology division was forced to report a negative EBIT the previous year, in 2004 all of the divisions contributed to this successful Group result.

It should be noted that the division results for 2004 contained for the first time a complete allocation of the overhead costs of the holding companies.

EBIT by divisions *€ million*

			change	
	2003	**2004**	*€ million*	*in %*
Pierburg	57.7	67.4	*9.7*	*16.8*
KS Pistons	38.1	37.1	*(1.0)*	*(2.6)*
KS Plain Bearings	9.0	16.6	*7.6*	*84.4*
KS Aluminum Technology	(3.3)	5.0	*8.3*	*>100*
Motor Service	16.4	13.0	*(3.4)*	*(20.7)*
Other/consolidation	(14.8)	(0.2)	*14.6*	*98.6*
Group	**103.1**	**138.9**	***35.8***	***34.7***

Just as last year, the Pierburg division was the largest single contributor to earnings, ending fiscal 2004 with an EBIT of €67.4 million. This represents a gain of 16.8 percent compared to the previous year. This improvement in earnings was due in part to restructuring efforts in Germany and Italy, though the sale of the division's interest in Pierburg Instruments GmbH also led to extraordinary earnings.

The KS Pistons division reported earnings before interest and tax for 2004 of €37.1 million, 2.6 percent lower than last year's figure. Spurred by inflation, steep hikes in the cost of personnel and materials pushed the EBIT of its Brazilian subsidiary to below last year's level. Increased production volumes, price increases in its home market, and savings resulting from strict cost management were able to offset these burdens only in part. Added to this was the negative impact on earnings of conversion-related exchange rate effects. KUS Inc. made a gratifying positive contribution to the division's results. Thanks to further improvements in productivity, the turnaround achieved the year before was confirmed. In Japan, the earnings of Kolbenschmidt K.K. likewise benefited from increased sales.

The KS Plain Bearings division increased its EBIT by €9.0 million to €16.6 million, a gain of 84.4 percent. With the earnings of its German and Brazilian units holding steady, the rise resulted from operational improvements at its US subsidiary. Unlike the year before, in 2004 these earnings were not eroded by the need for precautionary measures.

A further reduction in reject rates and improvements in productivity, coupled with greater capacity utilization especially in its Low Pressure segment, boosted the KS Aluminum Technology division's EBIT by €8.3 million to €5.0 million.

With an EBIT of €13.0 million, the Motor Service division fell short of the previous year's figure by 20.7 percent. Apart from the special burden of integrating the engine component units acquired in Germany in 2004, sharper price competition in Western Europe and higher prices for our products in US dollar-oriented markets likewise hurt earnings. These factors were only partly offset by the encouraging trend in earnings at the division's Brazilian and Turkish units.

The EBIT of the other companies, including Group consolidation, is determined by the result of Kolbenschmidt Pierburg AG, which, adjusted for income from trade investments with a neutral effect on Group earnings, rose compared to the previous year by €15.1 million. Apart from other small operating expenses, this related first of all to higher allocation and service earnings.

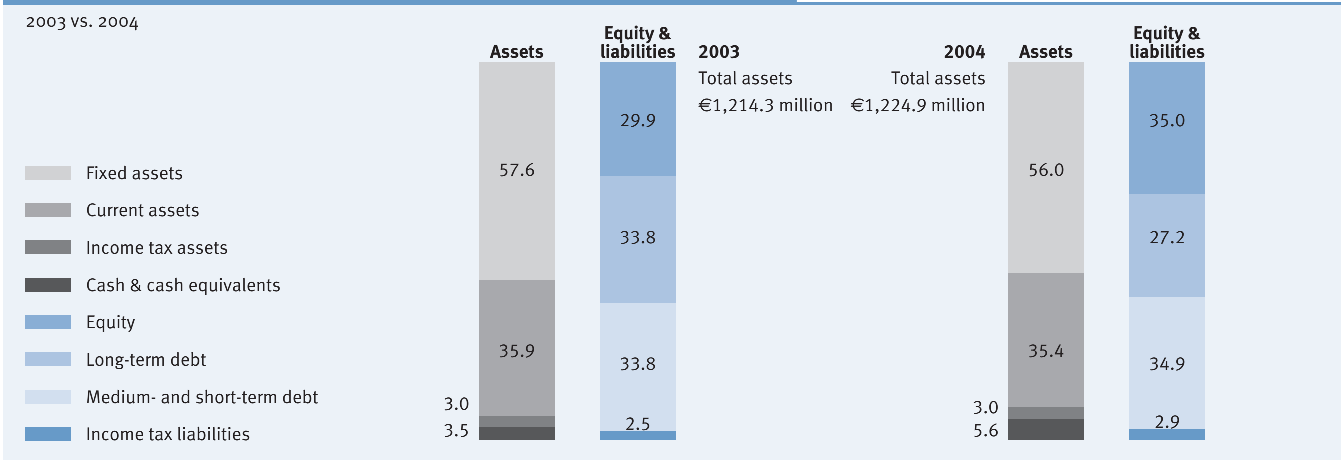
Our share in the earnings of the Group's two Chinese joint venture companies (both of which are consolidated at equity) amounted to €6.5 million, €1.1 million below the figure for 2003.

For fiscal 2004, Kolbenschmidt Pierburg reported earnings before tax (EBT) of €110.8 million, an increase of 52.6 percent over the previous year. Income tax expense rose by €2.0 million to €31.4 million; this equates to an income tax load ratio of 28.3 percent, down from 40.5 percent the year before. Profits after taxation (i.e. Group net income) thus rose by €36.2 million to €79.4 million. Taking into account the share in Group net income due to minority shareholders, earnings per share came to €2.79, up from €1.51 in 2003, with the number of shares remaining constant.

Asset and capital structure

At December 31, 2004, total assets increased compared to a year earlier by 0.9 percent to €1,224.9 billion. Despite this rise, 2004 witnessed a further improvement in key balance sheet ratios.

Balance sheet structure *in %*



The situation of the Group

At the end of 2004, fixed assets amounted to €685.6 million. This represents a decline of 1.9 percent compared to a year earlier. While intangibles rose as a result of the acquisitions made by the Motor Service division, tangible and financial assets fell below the previous year's level. In the case of fixed assets this was due to additions exceeding depreciation during the period under review, as well as to exchange rate influences during the period under review. Financial assets primarily reflect the sale of the Group's interest in Pierburg Instruments GmbH. The share of fixed assets in total assets declined to 56.0 percent, down from 57.6 percent the previous year.

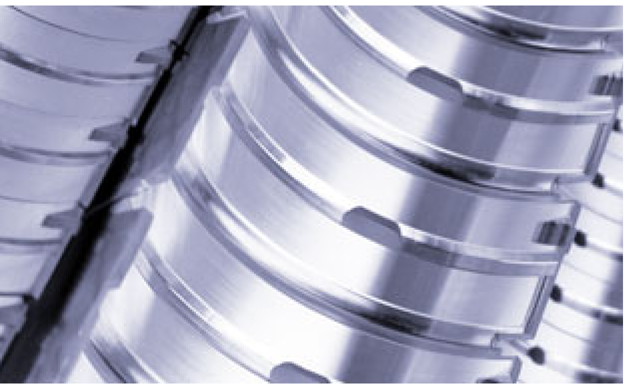
Current assets–without cash and cash equivalents–amounted to €433.9 million at December 31, 2004, a scant 0.6 percent less than a year earlier. Because of the increased volume of business and the acquisitions in the Motor Service division, it was not possible to keep the amount of capital tied up in inventories–approximately €7 million–at the low level attained in 2003. In particular, the volume of unfinished goods and services increased. The portfolio of receivables was smaller than a year earlier. This was chiefly due to the sale of receivables under the ABS program. For one thing, the number of Group companies participating in the program expanded; for another, the volume of receivables sold by those companies already participating in the program last year increased. The share of capital tied up in current assets in the balance sheet total declined slightly to 35.4 percent, down from 35.9 percent a year earlier.

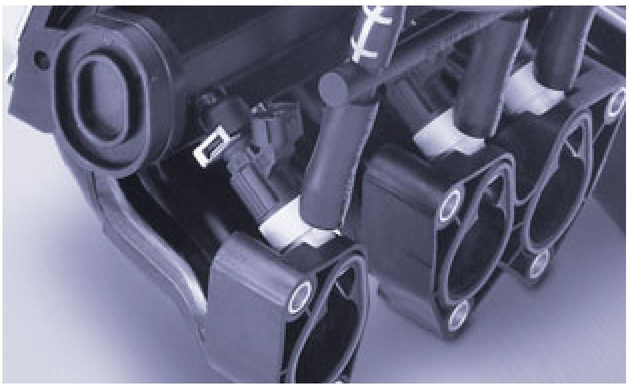
Augmented by increased cash flow, the item "cash and cash equivalents" rose substantially. At €68.2 million (or 5.6 percent) of total assets, the amount of cash and cash equivalents held exceeded the previous year's figure by €25.5 million.

At December 31, 2004, equity had risen to €428.3 million, an increase of 17.9 percent compared to a year earlier. This was essentially due to Group net income of €78.1 million (after minority interests). The equity ratio rose by 5.1 percentage points to 35.0 percent.

At the end of 2004 long-term liabilities came to €333.9 million, 18.7 percent below the previous year's figure. In the category of financial liabilities, it was once again liabilities due to banks that declined most steeply, though leasing liabilities fell as well. Pension accruals were also down. Exchange rate effects and special payments into the US fund contributed materially to this trend. The share of long-term liabilities in the balance sheet total declined to 27.2 percent, down from 33.8 percent a year earlier.

Medium-and short-term liabilities grew by 5.7 percent to €427.6 million. Short-term accruals declined as a result of altered reporting requirements for liabilities arising from incoming invoices. In fiscal 2004, these were recorded as receivables. After adjustment, other accruals increased. Above all, accruals for bonuses and severance pay increased compared to the previous year. Liabilities arising from receivables rose due to the aforementioned change in reporting requirements, as well as to a rise in the volume of payments received on account. Owing to the monies to





be transferred under the ABS program, the volume of other liabilities exceeded the previous year's figure. The share of medium- and short-term liabilities in the balance sheet total increased to 34.9 percent, up from 33.8 percent the year before.

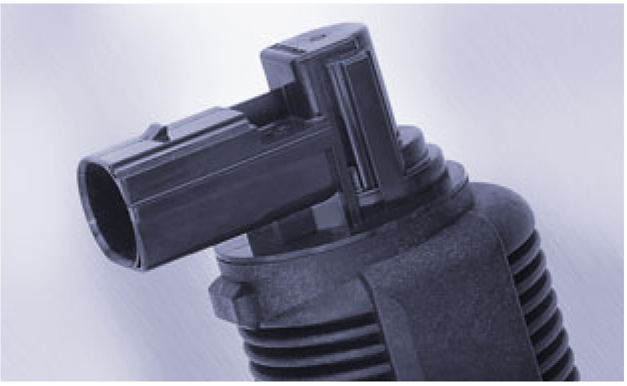
At December 31, 2004, coverage of fixed assets by equity rose by 62.5 percent compared to a year earlier, when this ratio was 52.0 percent. Together, equity and long-term debt completely covered fixed assets at the end of 2004. Net financial liabilities still amounted to €104.6 million at the end of 2003; by December 31, 2004, this amount had been completely drawn down and replaced by a surplus of €3.8 million.

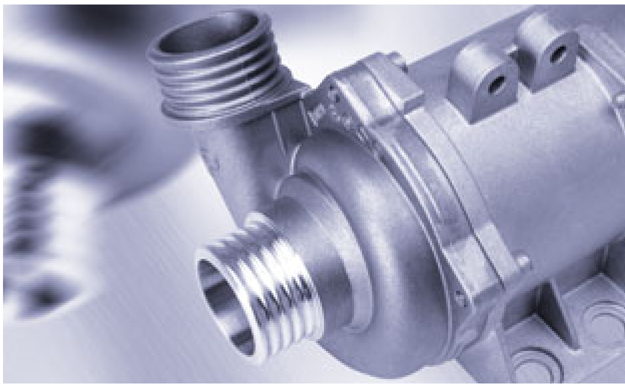
Thanks to improved EBIT and a simultaneous reduction in average capital employed, the return on capital employed (ROCE) expanded by 6.2 percentage points to 20%.

Value added

In fiscal 2004 Kolbenschmidt Pierburg generated a value added of €689.8 million, up from €649.3 million the previous year. Despite the decline in other operating earnings, the underlying group's operational performance expanded as a result of higher sales, greater financial earnings, and improved income from trade investments, rising by €72.9 million to €2,068.4 million. The necessary advances grew by €46.6 million, reaching €1,256.80 million. This rise was due chiefly to changes in the product mix, but also to increased raw materials prices. Depreciation of intangible and tangible assets was down sharply thanks to our carefully focused policy of capital expenditure in recent years, as well as to the decision to dispense with the planned depreciation of goodwill.

Value added per employee rose from €56,000 to €60,000. Apart from an absolute increase in value added, a 0.8 percent reduction in the average number of employees contributed to this shift.





The situation of the Group

Source and use of value added *€ million*

	2003		**2004**	
Source				
Group's total operating performance	1,995.5		2,068.4	
Input	1,210.2		1,256.8	
Amortization/depreciation	136.0		121.8	
Value added	**649.3**		**689.8**	
Use		in %		in %
Employees	531.1	82	536.0	78
Treasury	37.1	6	39.0	6
Lenders (banks)	37.9	6	35.4	5
Stockholders	14.0	2	19.6	3
Kolbenschmidt Pierburg Group	29.2	4	59.8	8
Value added	**649.3**	**100**	**689.8**	**100**

Of the total amount of valued added, €536.0 million went to the employees, who accounted for a 78 percent share, with the State receiving €39.0 million (or six percent), and lenders, €35.4 million (or five percent). At the General Meeting on May 4, 2005 a dividend of €19.6 million will be proposed, equating to three percent of the value-added. The Group thus retains €59.8 million (or eight percent) of value-added.

Capital expenditure and depreciation

In fiscal 2004, Kolbenschmidt Pierburg invested €132.7 million in intangible assets (excluding goodwill) and tangible assets, as opposed to €126.5 million the year before. Contained here are capital outlays in the divisions aimed at bolstering the company's position in the German after market, as well as the acquisition of a Japanese piston manufacturer the year before. Adjusted for these structural effects, capital expenditure volume in 2004 amounts to €126.9 million for 2004 and €117.2 million for 2003. The ratio of capital expenditure to sales rose to 6.5 percent, up from 6.2 percent a year earlier.

With the aim of further improving the productivity of capital, we continued in 2004 to adhere to our established policy of highly selective capital expenditure.

Just as last year, capital expenditure was nearly evenly distributed between the Group's domestic and foreign units, with Germany accounting for around 51 percent of spending.

Capital expenditures by division *€ million*

			change	
	2003	**2004**	*€ million*	*in %*
Pierburg	50.3	54.1	*3.8*	*7.6*
KS Pistons	43.6	46.0	*2.4*	*5.5*
KS Plain Bearings	6.7	8.8	*2.1*	*31.3*
KS Aluminum Technology	14.1	12.9	*(1.2)*	*(8.5)*
Motor Service	0.6	0.9	*0.3*	*50.0*
Other/consolidation	1.9	4.2	*2.3*	*›100*
Group	**117.2**	**126.9**	***9.7***	***8.3***

As was already the case the year before, the Pierburg and KS Pistons divisions absorbed the bulk of capital expenditure in 2004. Apart from replacement and rationalization measures, the creation and expansion of capacity for new customer projects was the prime focus of investment.

In Germany, the Pierburg division invested in preparations for the full-scale production of two new intake manifolds for the 6- and 8-cylinder engines of premium German carmakers, as well as in an innovative electrical coolant pump for gasoline-powered engines. Capacity for manufacturing electrical throttle bodies and the accompanying electro-motors was also increased.

Elsewhere in Europe, capital expenditure by Carbureibar S.A. of Spain focused on exhaust gas re-circulating valves and vacuum pumps, while in Italy, spending by Pierburg S.p.A. concentrated on intake manifolds, exhaust gas re-circulating valves, and oil pumps. In France, meanwhile, Pierburg S.à.r.l. once again placed the accent on water and oil pumps, as well as on infrastructure measures for improving its production processes. In the United States, the expansion of a line for manufacturing electric throttle bodies continued to form the prime focus of capital expenditure at Pierburg Inc.

At the KS Pistons division's German plants, resources were directed at replacing existing equipment, as well as at expanding capacity for the production of new gasoline engine pistons. Furthermore, new plant was acquired for its foundry and processing units. Outside of Germany, capital expenditure was used to create capacity for new projects as well as to expand existing capacity, though here investment focused on pistons for gasoline- and diesel-powered engines. Furthermore, conditions were created for enabling new features to be produced under existing programs.

In fiscal 2004, the focus of capital expenditure by the KS Plain Bearings division in Germany was on expanding capacity for the production of primary products, as well as on creating the conditions for an expanded range of products at its plant in St. Leon-Rot. The productivity of existing primary materials lines for Permaglide products was considerably enhanced thanks to a number of well-targeted measures.

Capital expenditure in the United States was geared to improving the flexibility and productivity of the cast line for bronze materials. In addition, special tools were procured, and the division also invested in equipment for improving worker safety.

The Aluminum Technology division continued to concentrate its capital expenditure in 2004 on the Low Pressure Casting unit. Capacity was expanded in order to permit production run-ups of new products.

Additions to financial assets in fiscal 2004 amounted to just €0.1 million, compared to €9.1 million the year before. The hefty figure for 2003 related to our increased stake in the Chinese joint venture Kolbenschmidt Shanghai Piston Co. Ltd., as well as the high equity results of both Chinese joint ventures.

For the period January 1 to December 31, 2004, Kolbenschmidt Pierburg achieved a gross cash flow of €188.1 million (2003: €170.0 million). This meant that all capital expenditure could be financed internally.

Depreciation of tangibles and amortization of intangibles (excluding goodwill) of the Kolbenschmidt Pierburg Group came to €121.8 million at December 31, 2004, down from the previous year's figure of €132.0 million. Owing to the voluntary application of IFRS 3 and IAS 36 and 38, the planned amortization of goodwill no longer features. The impairment tests conducted did not result in unscheduled amortization or depreciation. Planned amortization and depreciation the previous year amounted to €4.0 million.

Adjusted for the acquisition-related increase, capital expenditure in fiscal 2004 amounted to €126.9 million, exceeding (by approximately four percent) depreciation and amortization of €121.8 million. The year before, capital expenditure undershot depreciation and amortization by some 11 percent.

The situation of the Group

Research and development

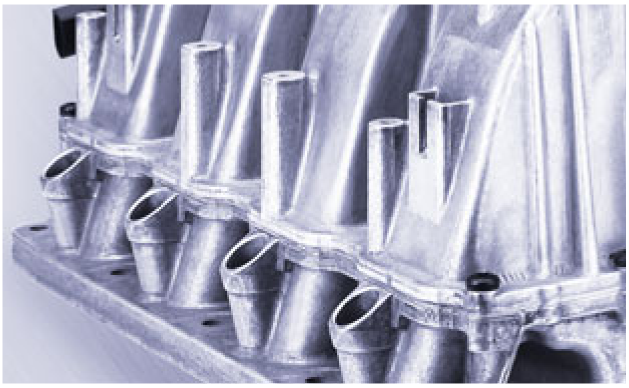
In fiscal 2004, the Group spent €97.2 million on research and development, 19.4 percent more than the previous year. In addition to this comes €4.8 million in R&D services (2003: €5.4 million) which meet IFRS criteria for capitalization. The R&D ratio, defined as expenditure in relation to sales, rose to 5.0 percent, up from 4.3 percent the year before. The percentage of Group employees engaged in research and development activities increased slightly to 6.2 percent, up from 6.0 percent in 2003.

Research and development expenditures by division *€ million*

			change	
	2003	**2004**	*€ million*	*in %*
Pierburg	51.4	55.2	*3.8*	*7.4*
KS Pistons	25.1	32.4	*7.3*	*29.1*
KS Plain Bearings	2.7	3.5	*0.8*	*29.6*
KS Aluminum Technology	2.2	6.1	*3.9*	*›100*
Group	**81.4**	**97.2**	***15.8***	***19.4***

Once again, the primary objectives of the Pierburg R&D program in fiscal 2004 were improved engine performance coupled with emission and weight reduction. As in the past, numerous projects involved electrical and electronic products, which, unlike conventional mechanical components, lead to reduced fuel consumption thanks to demand-controlled operation.

The Air Supply product unit successfully concluded the development of various applications relating to intake manifolds–including two major projects featuring a magnesium design–as well as electrical throttle bodies and drive modules. Development of an integrated intake manifold also commenced. The advantage of combining the intake manifold, air intake valve and exhaust gas recycling module is that it saves space and eliminates the customer's need for interfaces. Following the successful market launch of an electromotor-driven exhaust gas recycling valve for diesel applications and an electrical bypass valve for turbo chargers, the Emission Control product unit won a number of new orders during the year under review; the necessary modifications for these projects are already under development. Furthermore, development began of an integrated module for exhaust



gas recycling, consisting of an exhaust gas recycling unit with a cooler and bypass valve. Just as with the integrated intake manifold module, advantages arise with respect to space requirements and interfaces. For the Pumps product unit, the start of main production of the first application of a demand-controlled electric coolant pump was the largest project of the year. Ongoing development of a variable oil pump formed a further focus of activity.

In 2004, the Pierburg division spent €55.2 million on research and development, an increase of 7.4 percent. The R&D ratio thus came to 6.2 percent of sales. At December 31, 2004, 410 employees were engaged in research and development activities.

In the KS Pistons division, the quest for increased power density and further reductions in fuel consumption and emissions have for many years propelled the development of new engine components.

In the case of diesel engines, this generally entails increasing the power density by means of direct fuel injection and/or variable valve control. This poses huge demands on the pistons, which must combine durability with low weight. The technology developed by the KS Pistons division in response to this task, LiteKS, first used in 2003, is now found in the majority of products currently in serial production. It has been expanded to include groove protection features (ring carrier), now being employed in gasoline-powered engines for the first time.

Owing to increasing power densities, pistons for new automobile turbo diesel engines can only be achieved by using cooling galleries. Along with cooled ring carriers – GalleriKS – coolant ducts with a variable cross-section can be used for serially manufactured products – ContureKS – for pistons with large recess dimensions. The design and casting technology necessary for advanced variable geometries was developed in 2004. Recess edge and groove temperature reductions of approximately 20°C are possible.

In the utility vehicle segment, all-steel pistons continued to be the prime focus of development. These pistons are suitable for cylinder pressures of up to 250 bar, which engines will need in order to meet future emissions standards.

Last year, improved advanced materials capable of withstanding extreme thermal and mechanical stress in automobile and utility vehicle engines reached the point where they were ready for production.

For use in large engines, multiple- and single-part steel pistons are also being developed; the first prototypes have already been dispatched to customers for field testing.

In fiscal 2004, expenditure for research and development activities jumped by 29.1 percent to €32.4 million in the Pistons division, or 5.6 percent of sales. At December 31, 2004, a total of 213 Pistons employees worked in R&D worldwide.



The situation of the Group

At the beginning of 2004, a new organization came into effect in the KS Plain Bearings division's research and development unit, bringing about a clear separation of materials development from product and process development.

In the materials development section, sample bearings made of lead-free alloys were produced in the following materials families in 2004: steel-aluminum, steel-sintered bronze, and steel-bronze. Component trials, especially engine tests, will be concluded in the coming months. Apart from advances in lead-free base materials, progress in lead-free galvanic coatings was also achieved. Entirely new were the first tests of coated-connecting rods.

In the product and processes development section, projects focused on reducing the cost of existing processes, as well as on expanding the portfolio of products. Constituting an innovative new niche product area is the division's new generation of flanged sleeves, which cannot be manufactured using conventional deformation processes. Here, the first sample parts were presented, intended for use in highly demanding applications. In parallel, a systematic investigation of alternative deformation processes for KS Plain Bearings materials commenced. This will enable us to supplement the current range of slide bush products with slide bushes which are attached to the base, thus creating a seal from one side.

On the one hand, well-targeted capital expenditure and maintenance measures in 2004 enabled the test field to be expanded and suitably equipped. On the other, important steps were taken to reduce delivery times for experimental parts and prototypes at the experimental parts production facility in St. Leon-Rot. These measures will significantly strengthen the KS Plain Bearings division's position as a supplier of prototype components.

In 2004, the KS Plain Bearings division spent €3.5 million on research and development activities, 29.6 percent more than the year before. The R&D ratio amounted to 2.2 percent. In all, 43 employees were active in research and development work.

Development activity in the KS Aluminum Technology division in fiscal 2004 focused on the use of virtual development tools in order to shorten lead times. On the one hand, this has been made necessary by the multiplicity of concurrent new projects, and on the other, by the fact that the development process has become very cost intensive both for KS Aluminum Technology and the OEMs: this is a way of optimizing that process.

In the process development segment, work focused on the creation of thin-walled filigree structures for the low-pressure casting of premium engine blocks.

By allocating increased human resources to the development of new processes, it proved possible to achieve sustained improvements during new product run-ups as well as lower production costs. As the business expanded, advanced cutting techniques were successfully applied in the final processing of engine blocks.

Compared to the previous year, R&D expenditure by the Aluminum Technology division more than doubled to €6.1 million in fiscal 2004, equivalent to 3.4 percent of sales. At year's end, the division employed 38 people in research and development.

Human resources

At December 31, 2004, the companies of the Kolbenschmidt Pierburg Group employed a global workforce of 11,364 employees, i.e. 48 more than a year earlier, a rise of 0.4 percent. Thus, the 4.6 percent increase in sales achieved in fiscal 2004 was achieved with practically no increase in staff. This was made possible by the successful restructuring of the Pierburg division's plants in Germany and Italy, the German units of KS Pistons, and the US plants of KS Plain Bearings. The acquisition of the engine components activities of E. Trost GmbH & Co. KG had a countervailing effect, as did the creation of Pierburg s.r.o. in the Czech Republic. In the KS Pistons division, fresh hiring at Metal a.s. in the Czech Republic (to ensure successful production run-ups) and at KS Pistões Ltda. (in response to stronger sales), more than offset the effects of restructuring. The increase in the number of staff in the Aluminum Technology division essentially resulted from higher sales.

At December 31, 2003, the Kolbenschmidt Pierburg Group had 5,759 employees in Germany, down by a modest 1.3 percent from a year earlier. The share of Group personnel employed in Germany thus declined to 50.7 percent, down from 51.6 percent at the end of 2003.

Headcount

			change	
	12/31/2003	**12/31/2004**	*absolute*	*in %*
Pierburg	3,536	3,471	*(65)*	*(1.8)*
KS Pistons	5,483	5,568	*+85*	*1.6*
KS Plain Bearings	1,004	982	*(22)*	*(2.2)*
KS Aluminum Technology	913	925	*+12*	*1.3*
Motor Service	344	379	*+35*	*10.2*
other	36	39	*+3*	*8.3*
Group	**11,316**	**11,364**	***+48***	***0.4***
of which Germany	*[5,836]*	*[5,759]*	*[(77)]*	*[(1.3)]*
of which abroad	*[5,480]*	*[5,605]*	*[+125]*	*[2.3]*

Per capita sales in fiscal 2004 came to €170,000, exceeding the previous years figure of €163,000, a gain of 4.3 percent.

Personnel expenses incurred by the Kolbenschmidt Pierburg Group in 2004 totaled €520.8 million (2003: €515.2 million). Wages and salaries accounted for €415.9 million of this amount (2003: 413.8 million), social security contributions for a further €71.9 million (2003: €71.0 million), while pension expenses absorbed €33.0 million (2003: 30.4 million).

In February 2004, new labor agreements were concluded at the Group's plants in Germany, valid until February 28, 2006. Wages roses by 2.2 percent starting March 1, 2004, and will rise by a further 2.7 percent starting March 1, 2005. Furthermore, a more flexible weekly working hours structure was agreed. Implementation of the terms of the framework pay agreements concluded up until 2003 commenced in local labor agreements at all of our German plants.

Based on existing framework agreements at the individual plants, in 2005 a share in the profits will again be disbursed to rank-and-file staff of the Group's management companies in Germany in recognition of the attainment of earnings targets in 2004.

In 2004 also, policies on semiretirement were agreed on the basis of a company framework agreement, oriented to the needs of the Kolbenschmidt Pierburg Group's German plants. Just as in previous years, the Group succeeded in introducing additional flexible working hour arrangements at its plants, as well as in expanding the use of group work at its international locations.

The situation of the Group

Numerous training courses, not only in the field of modern working techniques but also in management and communication, were conducted in order to sharpen the skills of our employees both in and outside of Germany. A continuous strengthening of employee qualifications and motivation is an essential means of coping with the ongoing process of change brought about by new technologies and the steady transition to contemporary, more efficient forms of business organization.

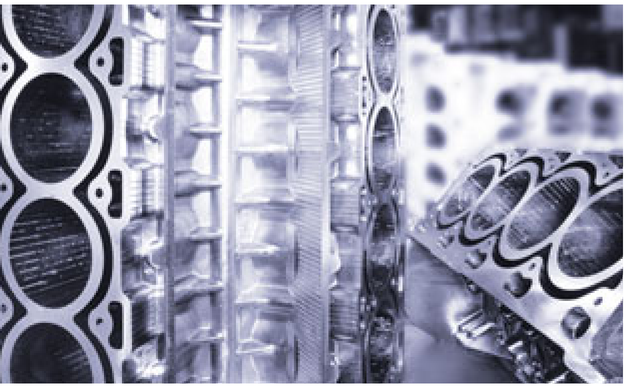
Another aspect of this is the continuous process of improvement to which all our plants are subject. Moreover, our Corporate Suggestions Scheme taps into a steadily growing potential for improving internal workflows. In submitting these suggestions, our employees demonstrate their interest in improving the efficiency of the organizations where they work.

In 2004, the existing potential of all senior and junior executives at our German companies was systematically identified, analyzed and evaluated. The objective is to support the career development of junior and senior executives through professional qualification and training measures, thus permitting succession and staffing plans to be prepared on a timely basis. The Group-wide concept “Leading by Goals” was extended to new layers of management and other senior staff, and linked to performance-related compensation components. In the future, this concept will be extended all the way down to the shop floor, based on new framework pay accords and local agreements.

We continued to attach great importance to apprenticeship training, seeing in it a crucial means of improving the competitiveness of our company. At December 31, 2004, Kolbenschmidt Pierburg employed 361 apprentices (2003: 356).

The employee representatives at every one of our companies cooperated actively and constructively in putting necessary measures into effect. Invariably based on mutual trust, cooperation with the works councils and staff representatives on the Supervisory Board has always been a factor of fundamental importance in the success of the entire Group.

We thank all the employees of the Kolbenschmidt Pierburg AG companies for their great commitment and exceptional achievements in fiscal 2004.



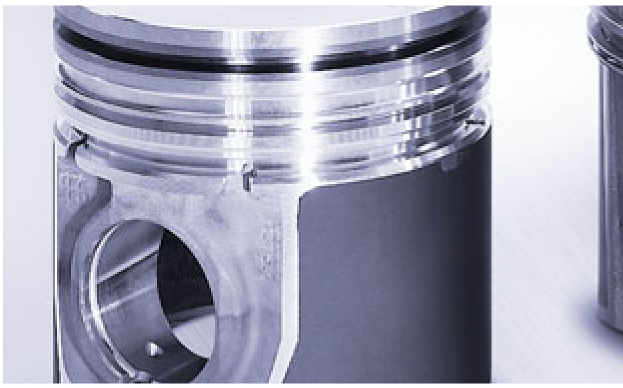
Dependency report

Through the Berlin-based company Rheinmetall Berlin Verwaltungsgesellschaft mbH of Berlin, Rheinmetall Verwaltungsgesellschaft mbH of Ratingen and KP Beteiligungs GmbH & Co. KG of Düsseldorf, Rheinmetall AG of Düsseldorf owns the majority of Kolbenschmidt Pierburg AG's stock. No intercompany agreements exist between Kolbenschmidt Pierburg AG and Rheinmetall Berlin Verwaltungsgesellschaft, KP Beteiligungs GmbH & Co. KG, Rheinmetall Verwaltungsgesellschaft mbH or Rheinmetall AG.

Pursuant to Art. 312 AktG, a report concerning affiliations was prepared by the Executive Board and then examined by PwC Deutsche Revision AG, Wirtschaftsprüfungsgesellschaft, the Stuttgart-based statutory auditors who issued their unqualified opinion thereon. This dependency report of the Executive Board closes with the following statement:

"Under the circumstances which were known to us at the time legal transactions were entered into and actions taken or omitted, our company has in all cases received an equitable consideration. No disadvantages for our company have been involved in connection with such acts or omissions."





Risk management

The instruments for early recognition, control and monitoring of risks are defined in Risk Management Regulations applicable throughout the Group. Thanks to clear organizational and management structures, unambiguous procedural instructions and guidelines, as well as efficient information and control systems, a well-structured system exists enabling the timely recognition of risks and the adoption of appropriate measures to meet them.

The management of risks is based on an annual update of the existing risk environment, in which potential risks are registered and categorized with respect to their likelihood and the potential loss volume. Embedded in the annual strategic and operative plans and accompanied by monthly controlling reviews, risk reports and meetings of the Risk Committee, the risk management system ensures that all potential risks are identified in good time and their implications assessed. As a result, necessary provisions or remedial action can be initiated early on at the individual companies, divisions, or at Group level. Moreover, whenever a defined ceiling is exceeded, the Supervisory Board and the parent company are alerted.

The effectiveness of our risk management system is also subject to regular audits by the Group's parent company, Rheinmetall AG, as well as during the annual audit by the statutory auditors (elected by the General Meeting).

Economic and sector risks

Kolbenschmidt Pierburg AG and its subsidiaries develop and manufacture components, modules and systems for the international automotive industry. Hence, the future growth of the Group and its subsidiaries largely depends on global automobile sales.

The impact of individual markets and customers on Kolbenschmidt Pierburg's business performance is mitigated by the de facto internationalization of the Group. Furthermore, the Group's diversified customer base helps to offset fluctuations in production numbers among individual carmakers.

Pressure from customers for further price reductions remains undiminished. One way of limiting risk is to create additional price/cost latitude, achieved through product and process innovations as well as continuous improvement processes and the enforcement of strict cost management.

Operational risks

The organic growth envisaged in the sales plans of Kolbenschmidt Pierburg calls for a whole host of complex, technologically advanced new product start-ups which, because of their number, extent and in some cases the limited availability of skilled labor, inherently involves risks. From the drawing board and the invitation to bid through to initial and full-scale production, every phase of a new product's emergence is subject to comprehensive project and quality management, ensuring that it translates into profitable growth. In the 2004 annual accounts, the accrual for impending losses on individual product start-ups adequately provides for any losses.

Various Kolbenschmidt Pierburg companies are vulnerable to fluctuating raw materials prices. Thanks to contractual provisions, increased prices for aluminum – the single most important raw material for the Group – can generally be passed on to customers. Short- and medium-term changes in the price of other important raw materials, especially steel, copper, nickel, and tin, are covered in purchasing agreements or, if possible, through forward transactions. On the other hand, longer-term prices increases pose potential risks.

Financing risks

Owing to the international nature of Kolbenschmidt Pierburg's operations, certain currency and interest rate risks may arise. These are profiled centrally by the Kolbenschmidt Pierburg AG Treasury and – whenever feasible and economically warranted – hedged by means of interest rate caps and currency futures in accordance with the guidelines laid down by the Executive Board. For details see Note (38), Hedging Policy and Financial Derivatives.

Carmakers will continue to reduce their vertical integration, shifting more and more value added and development operations to their parts suppliers. For the latter, this entails new challenges with respect to R&D, production and quality standards; it also means greater pressure on the financial resources needed to fund input and additions to tangible assets. Thus, during the budgeting and PIA approval stages, the allocation of investment resources in the Kolbenschmidt Pierburg Group's divisions is closely scrutinized with regard to economic efficiency in order to relieve cash flows.

Legal risks

Sufficient insurance coverage has been taken out to cover adequately risks from loss or damage by natural forces and the resulting interruption of business, as well as warranty, product liability, and recall risks. The existing insurance coverage is regularly reviewed for adequacy and, where necessary, modified. At the same time, ongoing projects for process reliability as well as extensive quality assurance programs aim at preventing such risks from occurring. In the 2004 balance sheet, adequate accruals provide for those risks, which, despite the aforementioned measures, are covered only partially or not at all (deductible loss).

Since 1998, a court of arbitration has been examining the appropriateness of the conversion ratio calculated with regard to the merger of Kolbenschmidt Pierburg (Rheinmetall participations). On the basis of preliminary figures, the expert appointed by the Heilbronn District Court has now submitted an interim report that arrives at significantly deviating estimates of the worth of the two companies, which merged in January 1998. Kolbenschmidt Pierburg AG, however, after having read and considered this interim report, sees no grounds for distancing itself from the originally calculated value comparisons. At the time of the merger of the two companies, these value comparisons were calculated by two independent accounting companies and confirmed by a court-appointed merger and acquisitions expert. Kolbenschmidt Pierburg assumes that the value estimates, which were documented by three different experts, will be vindicated in the final ruling. So as not to prejudice the outcome of this process, we will desist from commenting further on this matter.

From today's vantage point, no fundamental economic or legal risks or other risks posing a threat to the continued existence of Kolbenschmidt Pierburg or its divisions are apparent, nor are any risks posing a sustained, significant threat to the Group's net assets, financial position or operating results.

Future prospects

Significant subsequent events

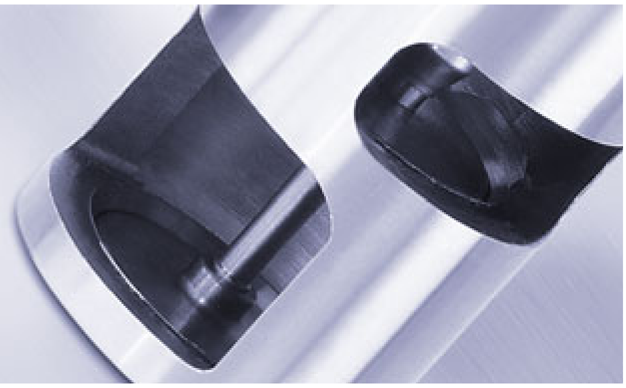
At the beginning of February 2005, contracts were signed for the gradual increase in KS Kolbenschmidt GmbH's stake in Shriram Pistons & Rings Ltd. of New Delhi, India, by 15 percent to 17.53 percent. Shriram has already been manufacturing pistons under a KS Pistons license for 35 years. Our increased participation in Shriram represents a first step in moves to expand our presence in the Indian market, and forms part of the KS Pistons division's Southeast Asia strategy.

Outlook

In 2005 growth in global output of light vehicles is once again expected to top four percent, reaching a total of some 62 million finished vehicles. For the Triad markets – NAFTA, Western Europe and Japan – the predicted rise in production is rather more modest, i.e. roughly one percent. Conversely, the forecast for Asia (excluding Japan) points to a strong increase in production, marking a continuation of the established upward trend.

The Kolbenschmidt Pierburg Group is off to a strong start in fiscal 2005, creating a robust platform for continued organic growth and for attaining our 2005 earnings targets.

To a decisive degree, growth for 2005 as a whole – and the attainment of the planned increases in performance in each of the Group's divisions – will be determined by our ability to realize the following key business objectives:



– a continuation of our aggressive policy of innovation in all the divisions with the aim of tapping into new and rewarding market segments, as well as the further expansion of existing market positions;

– a systematic implementation of our strategy of internationalization, focusing primarily on Southeast Asia and North and South America;

– a carefully-targeted study of the value-adding growth potential of acquisitions and cooperation agreements;

– the progressive optimization of business processes and structures in relevant regions and/or on a global basis;

– the continued pursuit of a highly selective policy of capital expenditure as well as stringent working capital management in order to reinforce our financial strength.

Provided our fundamental assumptions prove accurate – e.g. steady underlying political and economic conditions as well as stability among our suppliers and customers – meeting, or at least coming close to meeting, these goals will lead to additional growth and at a minimum, a strong, stable performance for 2005 as a whole.

Düsseldorf, February 25, 2005

Kolbenschmidt Pierburg AG
The Executive Board

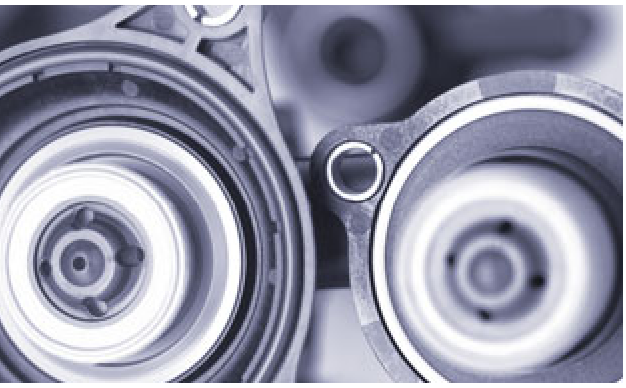
Dr. Kleinert Dr. Merten Dr. Friedrich

Kolbenschmidt Pierburg AG

As the parent company of the Kolbenschmidt Pierburg Group, Kolbenschmidt Pierburg AG engages primarily in Group management and service activities in the areas of accounting, controlling, financing, legal services, marketing and personnel. It does not conduct operational business in the sense of production, sales or distribution of products. Unlike the consolidated financial statements, Kolbenschmidt Pierburg AG's separate financial statements are prepared in accordance with the German Commercial Code (HGB) since they form the basis for calculating dividend distribution.

Owing to its role as a holding company, Kolbenschmidt Pierburg AG's earnings are made up of investment income, service fees and allocations, personnel expenses and the cost of materials, as well as net interest income from financing its operational affiliates.

Investment income rose in 2004 by €39.5 million to €78.6 million. The contribution to investment income received from Pierburg GmbH was higher than a year earlier. Earnings transferred by the companies MSI Motor Service International GmbH and KS Gleitlager GmbH may have been lower than in 2003, but nevertheless remained substantial. Another loss by KS Kolbenschmidt GmbH was taken over, though little more than half as large as the previous year's. Last year, a loss by KS Aluminium-Technologie AG had to be taken over. In 2004, the company generated a positive result, which, however, was offset with the existing net loss for the year. As a result, KS Aluminium-Technologie AG made no contribution to earnings. Apart from the transferred earnings, for the first time the investment income contained the trade tax transfer to affiliated companies (carried as tax expenses last year), and amounting to €5.7 million, up from €5.4 million in 2003.

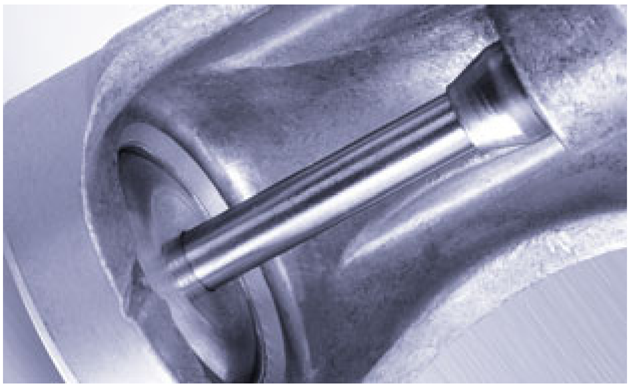


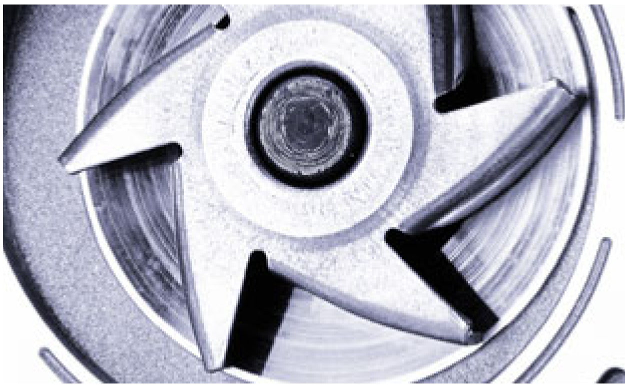
Net interest expense amounted in fiscal 2004 to €3.0 million, up from €2.6 million the year before. Interest incurred from financing current operations was lower than the year before. However, since loans were discharged ahead of schedule, early repayment penalties had to be paid.

Other operating earnings improved by €19.8 million to €37.5 million. Apart from increased currency exchange profits, this was due primarily to higher transfer and service income. Personnel expenses amounted to €12.3 million (2003: €9 million). The increase was caused on the one hand by the takeover of functions and personnel involved in these activities from the divisions and from Rheinmetall AG, and on the other by an increase in accruals for salaries. Other operating expenses increased by €3.7 million to €25.9 million. Currency exchange rate losses and expenses relating to services and coordination functions were higher than in 2003.

Earnings before taxes in 2004 amounted to €74.8 million, as opposed to €28.3 million the previous year. Net income for the year likewise rose, increasing by €40 million to €59.0 million. After allocation of €29.5 million to reserves retained from earnings, net earnings amounted to €29.5 million. The Executive and Supervisory Board will propose to the annual stockholders' meeting to distribute a cash dividend for 2004 of €0.70 per Kolbenschmidt Pierburg share (€0.20 more than the year before), totaling €19.6 million, as well as the allocation of a further €9.9 million to retained earnings.

At December 31, 2004, Kolbenschmidt Pierburg AG had 39 employees, three more than a year earlier, the result of taking over employees from the divisions as well as from Rheinmetall AG, our parent company. On average, the company had 38 employees during the period under review, up from 34 in 2003.





Pierburg division

Indicators Pierburg *€ million*			change	
	2003	**2004**	*€ million*	*in %*
Net sales	877.5	889.1	*11.6*	*1.3*
EBIT	57.7	67.4	*9.7*	*16.8*
EBT	48.7	58.8	*10.1*	*20.7*
Net income	33.0	41.0	*8.0*	*24.2*
Capital expenditures	50.3	54.1	*3.8*	*7.6*
Headcount at Dec. 31	3,536	3,471	*(65)*	*(1.8)*
EBIT margin *in %*	6.6	7.6	--	--
ROCE *in %*	25.9	35.5	--	--

The Pierburg division comprises the Group's series production and aftermarket operations in the product areas Air Supply, Emission Reduction, and Pumps. Pierburg GmbH is the division's parent company.

At the beginning of 2004 Pierburg GmbH sold its interest in Pierburg Instruments GmbH to the majority shareholder, AVL GmbH. In May 2004, a new company was founded in the Czech Republic, Pierburg s.r.o.; it is already generating sales.

In fiscal 2004, sales of the Pierburg division reached €889.1 million, exceeding the previous year's figure of €877.5 million by 1.3 percent. In the Air Supply product group, sales in the two main product segments–throttle bodies and intake manifolds–were higher than in 2003. In the Emission Controls segment, stronger sales of exhaust gas recycling valves and air mass sensors made up for weaker sales of other products. Overall sales volume remained constant. In the Pumps product group, the decline in sales resulting from the disposal (in 2003) of the Electrical Fuel Pumps product unit was all but offset by increased sales in all other product segments.

Compared to 2003, the sales volume of Pierburg GmbH fell by two percent. This was due to the aforementioned disposal of the Electrical Fuel Pumps unit, as well as to declining sales of secondary air pumps and solenoid valves. Across the board, Pierburg GmbH's affiliates achieved higher sales than the year before. Particularly gratifying was the trend at its subsidiaries in France and the United States, both of which reported a decline in sales a year earlier.

But it was Pierburg GmbH's Italian subsidiary whose sales grew fastest, with strong demand from Italian customers accounting for the bulk of the increase.

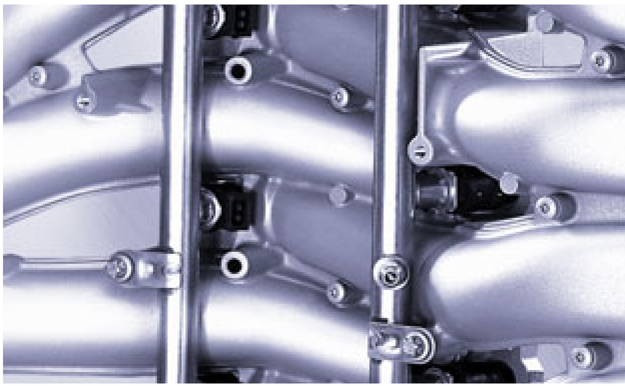
The Pierburg division's earnings before interest and tax reached €67.4 million in 2004, outstripping the previous year's figure by 16.8 percent. This increase in earnings resulted primarily from the successful restructuring of its units in Germany and Italy, as well as the book profit from the sale of its interest in Pierburg Instruments GmbH.

With the exception of the new unit Pierburg s.r.o., all of the companies once again made a positive contribution to the division's earnings. At Pierburg s.r.o., start-up costs brought about a negative result. Thanks to previous restructuring measures, higher investment income, and the book profit from the sale of Pierburg Instruments GmbH, Pierburg GmbH reported stronger earnings than the year before. Driven by sales, Carbureibar S.A. of Spain and Pierburg S.à.r.l. of France both reported strong earnings, even though neither company was able to match the previous year's performance. In Italy, Pierburg S.p.A. reported a positive result, the outcome of increased sales and successful restructuring. Though lower than in 2003, the positive results of Pierburg Inc. of the United States and Pierburg do Brasil Ltda. in Brazil both contributed to the division's overall success.

Capital expenditure by the Pierburg division totaled €54.1 million in 2003, up from €50.3 million a year earlier, and was entirely financed from gross cash flow for the year, which amounted to €93.6 percent (2003: €97.3 million). Total assets in 2004 rose compared to the previous year by €15.1 million to €550.6 million. Thanks first and foremost to stronger earnings, return on capital employed (ROCE) improved in fiscal 2004 to 35.5 percent, up from 25.9 percent the year before.

Targets for 2005

The objective of the Pierburg division is to achieve continued profitable growth through innovation and globalization. In the process, the division will narrow the focus of its product portfolio, concentrating on core competencies and profitable market segments. It will also press ahead with its policy of optimizing operational flows so as to ensure the highest standard of quality. Finally, its expanding presence in North America and Asia should strengthen the division's position in these markets.



KS Pistons division

Indicators KS Pistons *€ million*

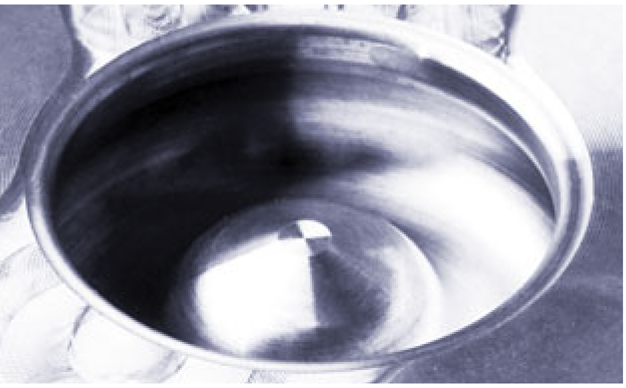
			change	
	2003	**2004**	*€ million*	*in %*
Net sales	593.6	581.9	*(11.7)*	*(2.0)*
EBIT	38.1	37.1	*(1.0)*	*(2.6)*
EBT	28.5	29.6	*1.1*	*3.9*
Net income	19.1	28.6	*9.5*	*49.7*
Capital expenditures	43.6	46.0	*2.4*	*5.5*
Headcount at Dec. 31	5,483	5,568	*85*	*1.6*
EBIT margin *in %*	6.4	6.4	--	--
ROCE *in %*	11.7	11.8	--	--

The Pistons division develops, manufactures and markets pistons for gasoline and diesel engines used in passenger and commercial vehicles. It also develops and manufactures pistons for 2-stroke and compressor engines, as well as large-bore pistons for stationary engines, marine diesel engines, and locomotives. KS Kolbenschmidt GmbH is the parent company of the Pistons division.

In fiscal 2004, the KS Pistons division generated €581.9 million in sales. Thus, despite the upward trend in its markets, its sales were €11.7 million (or two percent) lower than last year, the result of altered exchange rate parities. Calculated in local currencies, the division's units in North and South America produced substantially higher sales. When adjusted for the negative effects of currency fluctuations, the division's sales figures compare positively with those of the previous year.

At KS Kolbenschmidt GmbH, the return on sales for fiscal 2003 contracted by some three percent. In particular, sales of pistons for passenger cars fell, which could not be fully offset by stronger sales of pistons for utility vehicle and large pistons, which benefited from positive market trends and the production launch of steel pistons for utility vehicles.

The division's subsidiaries in France and the Czech Republic reported highly encouraging increases in sales, thanks mainly to the start of full-scale production in a number of new product programs, principally diesel pistons. In terms of local currency, sales of KUS Inc. of the United States rose; when translated into euros, however, its annual sales come in below last year's figure. Despite the sharp depreciation of the Brazilian real against the euro, KS Pistões Ltda. of Brazil achieved a robust increase in sales both at home and abroad, surpassing the previous year's



performance even when calculated in euros. Included in the scope of consolidation for the first time in 2003, the Japanese company Kolbenschmidt K.K. developed along very positive lines.

At €37.1 million, the KS Piston division's EBIT for fiscal 2004 undershot the previous year's figure by 2.6 percent. Adjusted for the negative effects of altered exchange rates, however, EBIT actually attained last year's level.

KS Kolbenschmidt GmbH's reported a slightly better result for fiscal 2004 than last year, though it is true that the figure for 2003 was marred by the write-down of the investment book value of the holding company of the North American companies, which could only be partially compensated for through a special disbursement by the division's Brazilian subsidiary.

The contribution of KUS Inc. was encouragingly positive. Thanks to further improvements in productivity, the turnaround achieved the previous year was confirmed. At KS Pistões Ltda. in Brazil, sales volume increased, though a shift to pistons with a weaker contribution margin meant that its earnings were lower than the year before. The decline in the value of the real against the euro was an additional detrimental factor. The division's Czech subsidiary, Metal a.s., achieved the previous year's level: an altered production structure coupled with run-up costs and price reductions prevented higher sales from turning into higher earnings. On the other hand, the earnings of France's Société Mosellane de Pistons S.A.S. and of Kolbenschmidt K.K. of Japan both benefited from stronger sales achieved by these companies.

At €46.0 million, capital expenditure by the KS Pistons division in fiscal 2004 exceeded the previous year's figure of €43.6 million. The increase in gross cash flow, which rose from €46.1 million in 2003 to €53.0 million, more than covered this amount. The availment ratio in 2004 came to roughly 87 percent.

At December 31, 2004, the division's total assets amounted to €435.4 million, little changed from the previous year's figure of €442.1 million. Coupled with the €10.1 million rise in equity to €191.3 million, the equity ratio increased to 43.9 percent (2003: 40.9 percent). Largely owing to the reduction in capital employed, the division's ROCE increased slightly from 11.7 percent in 2003 to 11.8 percent in the year under review.

Targets for 2005

The prime objectives of the division for fiscal 2005 are:

- continued restructuring at its German plants;
- ensuring that tangible benefits emerge from the optimization of structures and operational flows at its US plants;
- growing the operations of its pistons unit in Japan, coupled with an expansion of its activities in the Asian market;
- safeguarding market share and profitability in all other locations; and
- ongoing optimization of capital expenditure, including continuation of the working capital management program.

KS Plain Bearings division

Indicators KS Plain Bearings *€ million*			change	
	2003	**2004**	*€ million*	*in %*
Net sales	147.3	160.2	*12.9*	*8.8*
EBIT	9.0	16.6	*7.6*	*84.4*
EBT	7.2	15.1	*7.9*	*>100*
Net income	1.4	9.1	*7.7*	*>100*
Capital expenditures	6.7	8.8	*2.1*	*31.3*
Headcount at Dec. 31	1,004	982	*(22)*	*(2.2)*
EBIT margin *in %*	6.1	10.4	--	--
ROCE *in %*	18.9	38.4	--	--

The Plain Bearings division develops and produces bearings for engines and non-engine applications as well as maintenance-free sliding elements for the automotive and mechanical engineering sector. Moreover, it also manufactures copper-based continuous-casting products such as tubes, bars and profiles. The division's parent company is KS Gleitlager GmbH.

Sales of the KS Plain Bearings division in fiscal 2004 exceeded the previous year's figure by €12.9 million, an increase of 8.8 percent. To a substantial degree, this was the work of the division's parent company, KS Gleitlager GmbH, which accounted for roughly 11 percent of sales growth. This was due to higher sales volumes in all product categories. For example, despite lower prices, the return on sales in the Permaglide product segment was up by some €3 million on the previous year's figure. In the Metallic Bearings unit, sales grew by around €6 million as the result of higher volume. The same is true of the Continuous Casting segment, where sales likewise increased by about €6 million.



Sales of the division's North American affiliate, KS Bearings Inc., were slightly below the previous year's figure. Adjusted for the effects of currency conversion, the company's sales were actually higher than in 2003. In Brazil, the company KS Bronzinas Ltda. was able to increase its 2004 sales in terms of local currency and euros alike.

The KS Plain Bearings division generated an EBIT of €16.6 million, substantially above the previous year's level of €7.6 million. Earnings by KS Gleitlager GmbH were slightly up on the previous year's figure. However, owing to the in part considerably higher materials prices as well as a change in the product mix, the impact of higher sales on the contribution margin was disproportionately low. Compared to the previous year, the negative EBIT of KS Bearings Inc. narrowed significantly in 2004. This was the result of stronger sales (in US dollars) as well as successful restructuring. Earnings of the division's Brazilian unit improved slightly in fiscal 2004 as a result of higher sales.

Capital expenditure in the KS Plain Bearings unit during the period under review came to €8.8 million, up by €2.1 million from the year before. This expenditure was financed entirely from gross cash flow, which in 2004 amounted to €18.9 million (up from €12.3 in 2003). At €44.7 million, capital employed was slightly above the low level of the previous year. This is also reflected in the total assets figure, which at December 31, 2004 came to €72.1 million, a rise of €1.7 million. Owing to a capital increase at KS Gleitlager GmbH, the equity ratio rose by 3.0 percent to 11.6 percent at December 31, 2004. Due to improved earnings, the return on capital employed (ROCE) improved from 18.9 percent to 38.4 percent.

Targets for 2005

The overriding objective for 2005 is to press ahead with product innovations and to improve the efficiency of operational flows, thereby reducing costs. As part of this process, research and development into new materials will be stepped up. Furthermore, the division will proceed with internationalizing its business operations.

KS Aluminum Technology division

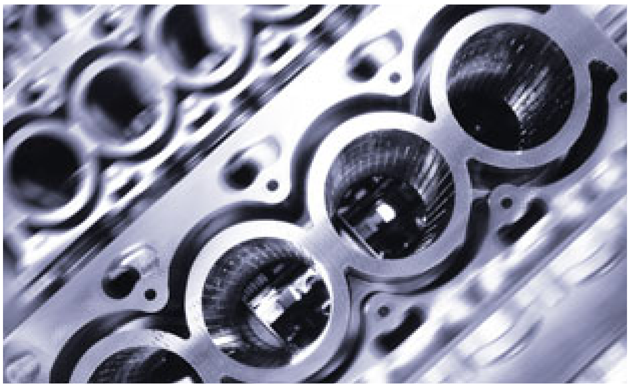
Indicators KS Aluminum Technology *€ million*

			change	
	2003	**2004**	*€ million*	*in %*
Net sales	159.8	182.8	*23.0*	*14.4*
EBIT	(3.3)	5.0	*8.3*	*>100*
EBT	(6.8)	0.8	*7.6*	*>100*
Net income	(4.8)	(0.1)	*4.7*	*>100*
Capital expenditures	14.1	12.9	*(1.2)*	*(8.5)*
Headcount at Dec. 31	913	925	*12*	*1.3*
EBIT margin *in %*	(2.1)	2.7	--	--
ROCE *in %*	(4.3)	7.9	--	--

The KS Aluminum Technology division manufactures cylinder crankcases (engine blocks) made of aluminum and aluminum-silicon alloys. The product groups correspond to the different casting methods used in production, i.e. high-pressure die casting and low-pressure die casting.

As part of the ongoing modernization of the KS Aluminum Technology division, at the end of March 2004 the company Ideko GmbH was renamed KS ATAG GmbH. Subsequently, Kolbenschmidt Pierburg AG sold KS Aluminium-Technologie AG to KS ATAG GmbH, which will henceforth serve as the holding company of the division as well as its lead company.

The KS Aluminium Technology division succeeded in improving its sales in fiscal 2004 by €23 million to €182.8 million, an increase of 14.4 percent. The bulk of the increase came in the Low-pressure Die Casting product unit, reflecting the run-up and shift to full production of new products. The absolute increase in sales in this segment amounted to around



€20 million. In the High-pressure Die Casting segment sales edged up too, advancing by €4 million. Due to the reduced volume of new projects, other sales (tools and development activities) undershot the previous year's figure by about €1 million.

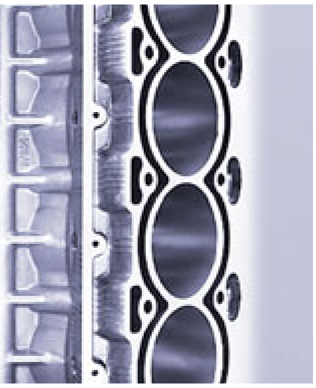
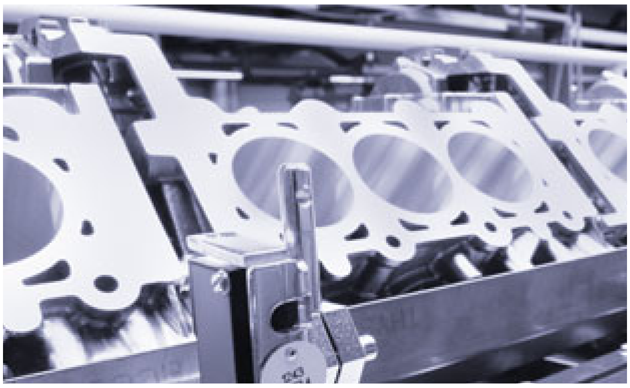
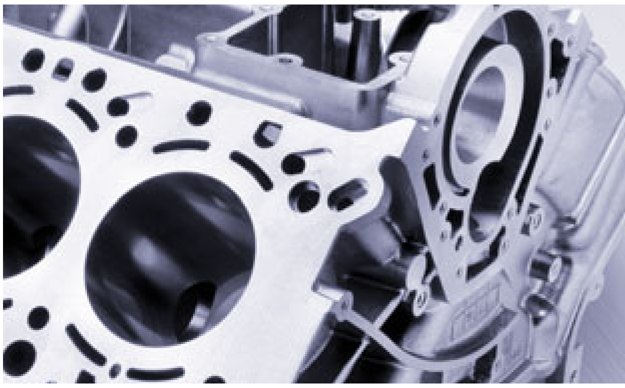
The division's earnings before interest and tax came to €5.0 million, representing a rise of over €8 million compared to 2003. After two years of generating substantial losses, the division has thus moved back into positive territory and is now on track to meet its long-term earnings targets. Essentially, its improved performance can be attributed to additional contribution margin from increased sales, an improved production cost structure, and the release of reserves for anticipated losses.

At €12.9 million, capital expenditure by the Aluminum Technology division in 2004 was €1.2 million (or 8.5 percent) lower than the year before, largely due to less spending in the Low-pressure Die Casting product segment. However, this segment continued to be the prime focus of investment activity, which was directed at increasing capacity for agreed customer projects. Thanks to the improved earnings situation, gross cash flow rose compared to 2003 to €13.6 million, sufficient to cover the division's total capital expenditure during the period.

Despite the sharp rise in sales, the division's total assets contracted slightly to €125.4 million, a decline of 1.3 percent; this was essentially due to a reduction in the volume of receivables. The equity ratio rose to 20.0 percent. The return on capital employed (ROCE) rose to 7.9 percent in fiscal 2004, up from a negative 4.3 percent the previous year, the result of better earnings and successful management of the capital employed.

Targets for 2005

In fiscal 2005, the division will continue pursuing its charted course to greater growth, coupled with further improvements in productivity. Low-pressure die casting is set to remain the prime engine of expansion.

Motor Service division

Indicators Motor Service *€ million*			change	
	2003	**2004**	*€ million*	*in %*
Net sales	138.5	161.4	*22.9*	*16.5*
EBIT	16.4	13.0	*(3.4)*	*(20.7)*
EBT	14.2	11.0	*(3.2)*	*(22.5)*
Net income	7.3	7.0	*(0.3)*	*(4.1)*
Capital expenditures	0.6	0.9	*0.3*	*50.0*
Headcount at Dec. 31	344	379	*35*	*10.2*
EBIT margin *in %*	11.8	8.1	--	--
ROCE *in %*	23.9	19.1	--	--

The Motor Service division embraces Kolbenschmidt Pierburg's worldwide aftermarket activities in the engine repair shop and the workshop field. MSI Motor Service International GmbH is the division's parent company.

Compared to fiscal 2003, sales of the Motor Service division rose by 16.5 percent to €161.4 million. Contributing materially here were the acquisitions undertaken in fiscal 2004 to expand its position in the German market, with new and existing units now united under the banner of MSD Motor Service Deutschland GmbH. But the division's Brazilian and Turkish subsidiaries also performed well in their respective markets. Thanks to new products and new customers, both companies succeeded in increasing their sales. Despite the difficult market situation in Western Europe, the Middle East and East Asia, MSI Motor Service International GmbH performed well at time when other units had to contend with declining sales. A further sharpening of price competition and price hikes in economies oriented to the US dollar both had a depressing effect on sales. In total, though, the division succeeded in offsetting the decline in sales volume experienced as a result of liquidating its former British sales component, even without the increase produced by its newly acquired German engine parts units.

With earnings before interest and tax of €13.0 million, the division fell short of its fiscal 2003 performance, experiencing a decline of 20.7%. Extraordinary expenses at MSD Motor Service Deutschland GmbH connected to the integration of the newly acquired engine parts units, coupled with sharper price competition in the German market, resulted in a loss, which – owing to its obligation to takeover the loss – had a negative impact on the earnings of Motor Service International GmbH also. As was also the case last year, the division's French unit, KS Motorac S.A.S., generated a slight loss owing to slow sales. By contrast, the Motor Service division's Turkish subsidiary, KS Istanbul A.S., ended the year with an improved EBIT. This came about as the result of higher sales and lower inflation. The distinctly improved performance of KS Produtos Automotivos Ltda., the division's Brazilian unit, was due to stronger sales.

Gross cash flow in 2004 amounted €10.2 million, up from €8.9 million the year before. The Motor Service division's total assets at December 31, 2004 came to €98.6 million, up by €10.6 million from a year earlier, reflecting its recent acquisitions in Germany. Containing a capital increase of €4.5 million, equity at the end of fiscal 2004 came to €21.7 million, meaning that the division's return on equity was 22.0 percent (2003: 17.6 percent). Return on capital employed came to 19.1 percent for 2004 compared to 23.9 percent the year before.

Targets for 2005

The earnings situation is expected to improve in fiscal 2005. Apart from the consolidation of Group-wide sales activities, this will be achieved through the expansion and further strengthening of the engine parts program. In addition, work is underway to expand the business volume of its subsidiaries, as well as reorienting the division's sales operations in East Asia.

Consolidated Financial Statements for 2004 of Kolbenschmidt Pierburg AG

Kolbenschmidt Pierburg Group
Consolidated balance sheet as of December 31, 2004

Assets € million	12/31/2003	12/31/2004	Note
Fixed assets			(6)
Intangible assets	77.1	82.2	(7)
Tangible assets	582.1	572.0	(8)
Investments stated at equity	37.3	29.6	(9)
Other financial assets	2.4	1.8	(9)
	698.9	**685.6**	
Current assets			
Inventories	212.4	238.7	(10)
Prepayments received	(7.1)	(12.4)	(10)
	205.3	**226.3**	
Trade receivables	194.8	179.7	(11)
All other receivables and sundry assets	33.4	26.2	(11)
Cash & cash equivalents	42.7	68.2	(12)
	476.2	**500.4**	
Income tax assets	36.2	37.3	(13)
Prepaid expenses & deferred charges	3.0	1.6	
Total assets	**1,214.3**	**1,224.9**	

Equity & liabilities € million	12/31/2003	12/31/2004	Note
Total equity			(14)
Kolbenschmidt Pierburg AG stockholders' equity			
Capital stock	71.7	71.7	
Additional paid-in capital	174.0	174.0	
Other reserves	71.4	100.1	
Group net income attributable to Kolbenschmidt Pierburg AG stockholders	42.4	78.1	
	359.5	**423.9**	
Minority interests	3.7	4.4	
	363.2	**428.3**	
Accruals			
Accruals for pensions	256.5	241.2	(15)
Other accruals	137.9	137.2	(16)
	394.4	**378.4**	
Liabilities			
Noncurrent financial debts	119.5	52.9	(17)
Current financial debts	27.8	11.5	(17)
Trade payables	191.7	224.6	(17)
All other liabilities	79.7	85.8	(17)
	418.7	**374.8**	
Income tax liabilities	30.0	35.1	(18)
Deferred income	8.0	8.3	(19)
Total equity & liabilities	**1,214.3**	**1,224.9**	

Kolbenschmidt Pierburg Group
Consolidated income statement for fiscal 2004

	€ million	2003	2004	*Note*
	Net sales	**1,884.2**	**1,940.8**	(20)
	Net inventory changes, other work and material capitalized	17.2	25.8	(21)
	Total operating performance	**1,901.4**	**1,966.6**	
	Other operating income	62.7	52.3	(22)
	Cost of materials	(970.6)	(1,010.6)	(23)
	Personnel expenses	(515.2)	(520.8)	(24)
	Amortization/depreciation/write-down	(136.0)	(121.8)	(25)
	Other operating expenses	(242.8)	(243.2)	(26)
	Operating result	**99.5**	**122.5**	
	Net interest expense	(30.5)	(28.1)	(27)
	Net investment income and other financial results	3.6	16.4	(28)
	of which profit shares of investees stated at equity	*[7.6]*	*[15.0]*	
	Net financial result	**(26.9)**	**(11.7)**	
	Earnings before taxes (EBT)	**72.6**	**110.8**	
	Income taxes	(29.4)	(31.4)	(29)
	Group net income	**43.2**	**79.4**	
	Minority interests	(0.8)	(1.3)	(30)
	Group earnings (after minority interests)	**42.4**	**78.1**	
1	EBIT	103.1	138.9	
2	EBITDA	239.1	260.7	
	Earnings per share (EpS) (diluted = undiluted)	1.51 EUR	2.79 EUR	(31)

1 *EBT plus net interest expense*

2 *EBT plus net interest expense and amortization/depreciation/write-down*

Kolbenschmidt Pierburg Group
Consolidated statement of cash flows for fiscal 2004

€ million	2003	2004
Cash & cash equivalents at January 1 (BoP)	**44.3**	**42.7**
Group net income	43.2	79.4
Amortization/depreciation/write-down of fixed assets	136.0	121.8
Change in pension accruals	(9.2)	(13.1)
Cash Flow	**170.0**	**188.1**
Net result from fixed-asset disposal	(12.5)	(9.8)
Change in other accruals	18.1	8.4
Change in inventories	10.6	(19.8)
Change in receivables, liabilities (excluding financial debts) and prepaid & deferred charges	(26.9)	53.0
Other noncash expenses and income	15.1	2.0
Net cash provided by operating activities	**174.4**	**221.9**
Cash outflow for additions to tangible and intangible assets	(117.2)	(126.9)
Cash inflow from the disposal of tangible and intangible assets	19.6	10.3
Cash outflow in divisions	(9.3)	(8.8)
Cash outflow for additions to financial assets	(3.1)	0.0
Cash inflow from the disposal of divisions	2.4	0.0
Cash inflow from the disposal of financial assets	1.1	23.4
Net cash used in investing activities	**(106.5)**	**(102.0)**
Dividends paid out	(14.2)	(14.3)
Financial debts raised	17.1	1.5
Financial debts redeemed	(72.4)	(81.4)
Net cash used in financing activities	**(69.5)**	**(94.2)**
Cash-based change in cash & cash equivalents	**(1.6)**	**25.7**
Parity-related change in cash & cash equivalents	0.0	(0.2)
Total net change in cash & cash equivalents	**(1.6)**	**25.5**
Cash & cash equivalents at December 31 (EoP)	**42.7**	**68.2**
The cash inflow from current operations contain		
interest income	3.1	2.2
interest expenditure	15.3	14.5
tax payments	19.0	28.6

The consolidated statement of cash flows is discussed in Note 32.

Kolbenschmidt Pierburg Group
Statement of changes in equity

€ million

	Capital stock	Additional paid-in capital	Retained earnings	Differences from currency conver-sion	Reserves from hedging operations	Other reserves	Group net income attributable to Kolben-schmidt Pierburg AG stock-holders	Stock-holders' equity of Kolben-schmidt Pierburg Group	Minority interests	Total equity
At January 1, 2003	**71.7**	**174.0**	**81.1**	**(34.5)**	**(0.4)**	**46.2**	**37.1**	**329.0**	**3.9**	**332.9**
Dividend payments			(14.0)			**(14.0)**		(14.0)	(0.2)	(14.2)
Exchange differences			12.4	(11.2)	0.2	**1.4**		1.4	(0.8)	0.6
Other comprehensive income			37.1		0.7	**37.8**	(37.1)	0.7		0.7
Group net income						**0.0**	42.4	42.4	0.8	43.2
At January 1, 2004	**71.7**	**174.0**	**116.6**	**(45.7)**	**0.5**	**71.4**	**42.4**	**359.5**	**3.7**	**363.2**
Dividend payments			(14.0)			**(14.0)**		(14.0)	(0.3)	(14.3)
Exchange differences			3.1	(3.3)		**(0.2)**		(0.2)	0.2	0.0
Other comprehensive income			42.9			**42.9**	(42.4)	0.5	(0.5)	0.0
Group net income						**0.0**	78.1	78.1	1.3	79.4
At December 31, 2004	**71.7**	**174.0**	**148.6**	**(49.0)**	**0.5**	**100.1**	**78.1**	**423.9**	**4.4**	**428.3**

Equity is explained in Note 14.

Segment report by divisions (primary segments)

€ million	2003	2004	2003	2004	2003	2004
Segments	Air supply, emission control & pumps		Large- and small-bore pistons		Plain bearings and continuous castings	
Divisions	Pierburg		KS Pistons		KS Plain Bearings	
Balance Sheet						
Segment assets	430.5	409.7	410.5	386.8	67.1	67.8
of which Goodwill	*[10.1]*	*[10.1]*	*[28.3]*	*[26.6]*	*[3.9]*	*[3.9]*
of which book values at equity	*[23.8]*	*[16.3]*	*[13.5]*	*[13.3]*	*[0.0]*	*[0.0]*
Segment liabilities	345.4	367.9	181.9	161.9	47.1	45.6
Total equity (1)	141.6	131.5	181.2	191.3	2.1	8.3
Pension accruals (2)	127.4	127.7	81.4	63.8	19.9	20.5
Net financial debts (3)	(58.1)	(90.2)	59.8	49.4	19.7	15.9
Capital employed (1) + (2) + (3)	210.9	169.0	322.4	304.5	41.7	44.7
Average capital employed	222.5	190.0	325.4	313.5	47.8	43.2
Income statement						
Net external sales	871.9	882.4	578.6	566.9	136.6	149.1
Intersegment transfers	5.6	6.7	15.0	15.0	10.8	11.1
Total segment sales	877.5	889.1	593.6	581.9	147.3	160.2
of which Germany in %	*[37.4]*	*[38.7]*	*[17.4]*	*[17.0]*	*[57.1]*	*[58.2]*
of which abroad in %	*[62.6]*	*[61.3]*	*[82.6]*	*[83.0]*	*[42.9]*	*[41.8]*
1 EBITDA	121.7	119.7	83.0	79.1	19.8	25.9
of which P/L at equity	*[4.7]*	*[12.7]*	*[2.9]*	*[2.3]*	*[0.0]*	*[0.0]*
Amortization/depreciation/write-down	(64.0)	(52.3)	(44.9)	(42.0)	(10.8)	(9.3)
of which special write-down	*[(5.2)]*	*[(2.1)]*	*[0.0]*	*[0.0]*	*[(1.0)]*	*[0.0]*
Segment EBIT	57.7	67.4	38.1	37.1	9.0	16.6
Net interest expense	(9.0)	(8.6)	(9.6)	(7.5)	(1.8)	(1.5)
EBT	48.7	58.8	28.5	29.6	7.2	15.1
Income tax	(15.7)	(17.8)	(9.4)	(1.0)	(5.8)	(6.0)
Net income/Net loss	33.0	41.0	19.1	28.6	1.4	9.1
Other data						
EBIT margin *in %*	6.6	7.6	6.4	6.4	6.1	10.4
ROCE *in %*	25.9	35.5	11.7	11.8	18.9	38.4
Capital expenditures	50.3	54.1	52.9	46.0	6.7	8.8
Headcount December 31	3,536.0	3,471.0	5,483.5	5,568.5	1,003.5	982.0

1 *EBT plus net interest expense and amortization/depreciation/write-down*

The segment reports are discussed in Note 33.

2003	2004	2003	2004	2003	2004	2003	2004	2003	2004
Aluminum Engine blocks		Aftermarket							
KS Aluminum Technology		Motor Service		Total		Other/Consolidation/ Holding		Group	
122.1	118.2	82.7	93.6	1,112.9	1,076.1	22.5	43.3	1,135.4	1,119.4
[4.6]	*[4.6]*	*[0.8]*	*[0.8]*	*[47.7]*	*[46.0]*	*[1.0]*	*[1.0]*	*[48.7]*	*[47.0]*
[0.0]	*[0.0]*	*[0.0]*	*[0.0]*	*[37.3]*	*[29.6]*	*[0.0]*	*[0.0]*	*[37.3]*	*[29.6]*
60.9	80.5	21.7	27.6	657.0	683.5	16.8	13.6	673.8	697.1
24.3	25.1	15.5	21.7	364.7	377.9	(1.5)	50.4	363.2	428.3
10.6	11.4	3.4	3.8	242.7	227.2	13.8	14.0	256.5	241.2
40.2	14.4	46.6	45.2	108.2	34.7	(3.6)	(38.5)	104.6	(3.8)
75.1	50.9	65.5	70.7	715.6	639.8	8.7	25.9	724.3	665.7
77.4	63.0	68.6	68.1	741.6	677.8	6.3	17.3	747.9	695.0
159.2	181.9	137.6	160.4	1,883.9	1,940.7	0.3	0.1	1,884.2	1,940.8
0.6	0.9	0.8	1.0	32.8	34.7	(32.8)	(34.7)	0.0	0.0
159.8	182.8	138.5	161.4	1,916.7	1,975.4	(32.5)	(34.6)	1,884.2	1,940.8
[63.1]	*[65.7]*	*[11.2]*	*[19.4]*	--	--	--	--	*[32.1]*	*[34.3]*
[36.9]	*[34.3]*	*[88.8]*	*[80.6]*	--	--	--	--	*[67.9]*	*[65.7]*
9.0	17.9	17.7	15.8	251.2	258.4	(12.1)	2.3	239.1	260.7
[0.0]	*[0.0]*	*[0.0]*	*[0.0]*	*[7.6]*	*[15.0]*	*[0.0]*	*[0.0]*	*[7.6]*	*[15.0]*
(12.3)	(12.9)	(1.3)	(2.8)	(133.3)	(119.3)	(2.7)	(2.5)	(136.0)	(121.8)
0.0	*(0.4)*	*0.0*	*0.0*	*(6.2)*	*(2.5)*	*0.0*	*0.0*	*(6.2)*	*(2.5)*
(3.3)	5.0	16.4	13.0	117.9	139.1	(14.8)	(0.2)	103.1	138.9
(3.5)	(4.2)	(2.2)	(2.0)	(26.1)	(23.8)	(4.4)	(4.3)	(30.5)	(28.1)
(6.8)	0.8	14.2	11.0	91.8	115.3	(19.2)	(4.5)	72.6	110.8
2.0	(0.9)	(6.9)	(4.0)	(35.8)	(29.7)	6.4	(1.7)	(29.4)	(31.4)
(4.8)	(0.1)	7.3	7.0	56.0	85.6	(12.8)	(6.2)	43.2	79.4
(2.1)	2.7	11.8	8.1	--	--	--	--	5.5	7.2
(4.3)	7.9	23.9	19.1	--	--	--	--	13.8	20.0
14.1	12.9	0.6	6.6	124.6	128.4	1.9	4.3	126.5	132.7
913.0	925.0	344.0	379.0	11,280.0	11,325.5	36.0	38.5	11,316.0	11,364.0

Segment report by regions (secondary segments)

€ million	2003	2004	2003	2004
Segments	Air supply, emission control & pumps		Large- and small-bore pistons	
Divisions	Pierburg		KS Pistons	
Germany				
Net external sales by customer location	322.8	337.6	91.8	96.8
Segment assets	231.4	216.8	138.4	125.5
Capital expenditures	27.8	26.4	9.9	13.0
Other Europe				
Net external sales by customer location	482.8	478.2	184.9	190.5
Segment assets	175.9	168.5	67.7	71.6
Capital expenditures	17.7	24.8	9.7	13.3
North America				
Net external sales by customer location	44.5	48.2	236.0	203.1
Segment assets	20.8	20.4	152.1	133.0
Capital expenditures	4.7	1.7	15.6	10.7
South America				
Net external sales by customer location	7.8	9.0	29.0	33.4
Segment assets	2.4	4.0	36.8	39.2
Capital expenditures	0.1	1.2	3.8	5.1
Other regions				
Net external sales by customer location	14.0	9.4	36.9	43.1
Segment assets	0.0	0.0	15.5	17.5
Capital expenditures	0.0	0.0	13.9	3.9

The segment reports are discussed in Note 33.

Plain bearings and continuous castings		Aluminum Engine blocks		Aftermarket			
KS Plain Bearings		KS Aluminum Technology		Motor Service		Total	
2003	2004	2003	2004	2003	2004	2003	2004
73.7	82.3	100.3	118.5	15.5	31.4	604.1	666.6
52.9	54.8	122.1	118.2	66.5	75.5	611.3	590.8
5.5	8.3	14.1	12.9	0.4	6.4	57.7	67.0
40.0	45.2	58.8	63.4	66.6	66.4	833.1	843.7
0.0	0.0	0.0	0.0	10.7	10.2	254.3	250.3
0.0	0.0	0.0	0.0	0.1	0.1	27.5	38.2
17.9	17.0	0.0	0.0	3.2	4.4	301.6	272.7
10.5	9.3	0.0	0.0	0.0	0.0	183.4	162.7
1.2	0.4	0.0	0.0	0.0	0.0	21.5	12.8
2.2	1.5	0.0	0.0	13.3	18.5	52.3	62.4
3.7	3.7	0.0	0.0	5.5	7.9	48.4	54.8
0.0	0.1	0.0	0.0	0.1	0.1	4.0	6.5
2.8	3.1	0.1	0.0	39.0	39.7	92.8	95.3
0.0	0.0	0.0	0.0	0.0	0.0	15.5	17.5
0.0	0.0	0.0	0.0	0.0	0.0	13.9	3.9

Notes
Accounting Principles

(1)
General

The consolidated financial statements of Kolbenschmidt Pierburg AG and its subsidiaries for the fiscal year 2004 have been prepared in accordance with the International Financial Reporting Standards (IFRS) of the International Accounting Standards Board (IASB). They are in harmony with the 7th EC Directive as interpreted by the Contact Committee on regulations governing consolidated accounts issued by the European Commission (Directive 83/349 EEC).

Since January 1, 2004, the provisions of the new IFRS 3 “Business Combinations” and the revised versions of IAS 36 (2004) and IAS 38 (2004) have been applied voluntarily in advance. This means that, since the beginning of the financial year, i.e. January 1, 2004, business combinations are carried in accordance with the new regulations; last year’s accounts have not been adjusted. From this point on, there will be no further scheduled amortization of goodwill. The value of goodwill is examined annually by means of an impairment test. In the 2004 consolidated accounts, the following revised standards (improvements) have been applied in advance for the first time:
- IAS 2: Inventories
- IAS 10: Events after the balance sheet date
- IAS 21: The effects of changes in foreign exchange rates
- IAS 28: Investments in associates
- IAS 31: Interests in joint ventures

In applying the revised standards, the interim regulations have been adhered to.

For enhanced transparency of presentation, certain items of the consolidated income statement and balance sheet have been subsumed in captions, however, which are broken down and discussed in detail in the notes below. The consolidated income statement has been prepared in the total-cost format. Along with the balance sheet and consolidated income statement, a consolidated statement of cash flows and a statement of changes in equity have been prepared.

The consolidated financial statements are presented in euros (€) which also represents the functional currency, current- and prior-year amounts being indicated in € million without exception.

Having elected to prepare its consolidated financial statements in accordance with IFRS, Kolbenschmidt Pierburg AG has exercised the exemption option under the terms of Art. 292a German Commercial Code (“HGB”), viz. to draw up the consolidated accounts in accordance with internationally accepted accounting principles in lieu of consolidated financial statements according to German commercial accounting regulations. The assessment of whether the consolidated financial statements and group management report meet the prerequisites of Art. 292a HGB has been made in conformity with the DRSC interpretation in German Accounting Standard DRS-1. The present consolidated statements substantially reflect the following accounting and valuation methods in derogation of the German Commercial Code (HGB):

- translation of non-euro receivables and payables at the current closing rate and recognition in net income of the resulting translation differences (IAS 21)
- unscheduled amortization of goodwill (IFRS 3/ IAS 36)
- recognition at fair value of certain financial instruments (IAS 39)
- capitalization of internally created intangible assets (IAS 38)
- capitalization of the asset and recognition of the residual liability under capital leases according to the definition criteria of IAS 17
- measurement of pension accruals according to the projected unit credit (PUC) method with due regard to future pay trends and the corridor rule of IAS 19
- waiver of providing for accrued liabilities if the probability of accrual utilization is below 50 percent (IAS 37)
- discounting of noncurrent accruals (IAS 37)
- accounting for deferred taxes according to the liability method in accordance with IAS 12

The fiscal year of Kolbenschmidt Pierburg AG and its subsidiaries equals the calendar year. As an officially listed company, Kolbenschmidt Pierburg AG is obligated pursuant to Art. 291(3)(1) HGB to prepare statutory consolidated financial statements. Kolbenschmidt Pierburg AG’s consolidated accounts will be included in the group accounts of Düsseldorf-based Rheinmetall AG as the highest tier of consolidation. Rheinmetall AG’s consolidated financial statements will be deposited with the Commercial Register of the Local Court of Düsseldorf under number HRB 39401.

(2)
Group of consolidated companies

Besides Kolbenschmidt Pierburg AG, the consolidated financial statements include all German and foreign subsidiaries in which either Kolbenschmidt Pierburg AG holds the majority of voting rights (whether directly or indirectly) or where the Group is otherwise able to control the financial and business policies. Companies are initially consolidated or deconsolidated when control is transferred. Companies in which an interest of between 20 percent and 49 percent and over which significant influence is exercised (associated companies) are reported at equity. Also carried at equity are companies in which a 50 percent stake is held and a joint management structure exists (joint ventures).

Group of consolidated companies

	12/31/2003	Additions	Disposals	**12/31/2004**
Fully consolidated companies	39	2	--	41
of which in Germany	*[17]*	*[1]*	--	*[18]*
of which abroad	*[22]*	*[1]*	--	*[23]*
Investees stated at equity	3	--	1	2
of which in Germany	*[1]*	--	*[1]*	*[0]*
of which abroad	*[2]*	--	--	*[2]*

During the year under review, two companies were consolidated for the first time. In the Czech Republic, the company Pierburg s.r.o., a wholly owned subsidiary of Pierburg GmbH, was founded in Ústí. The second company created was GVN Grundstücksverwaltungsgesellschaft Neuenstadt of Neckarsulm, a wholly owned subsidiary of Kolbenschmidt Pierburg AG. The disposal from the group of consolidated companies relates to the sale of the company Pierburg Instruments GmbH of Neuss, which was consolidated at equity.

The subsidiaries and the investees stated at equity which are included in the consolidated financial statements of Kolbenschmidt Pierburg AG are listed on pages 90/91. A comprehensive listing of the shareholdings of Kolbenschmidt Pierburg AG will be deposited with the Commercial Register of the Local Court of Düsseldorf (HRB 34883).

(3)
Consolidation principles

The financial statements of consolidated German and foreign companies are prepared in accordance with groupwide uniform accounting and valuation methods.

Since January 1, 2004, subsidiaries included in the consolidated accounts have for the first time been consolidated according to the purchase method, using a full revaluation method (IFRS 3). Here, the acquisition costs of the assets acquired are compared with the asset values, liabilities and contingency liabilities of the subsidiary (stated at fair value) at the time of acquisition. The acquisition costs are the fair values of the purchased assets, the debt taken over and the equity instruments issued by the purchaser, as well as related costs. The difference between the two will be shown as goodwill under intangibles.

A residual difference which would be carried as a badwill is immediately transferred to the consolidated income statement under other operating income.

The value of goodwill is regularly examined in an annual impairment test, unless evidence of a loss of value emerges in the intervening period. In the process, the book value is compared with the recoverable amount. The recoverable amount is calculated through the value in use. If this is worth less than the book value, a check is made to determine if the stated fair value (minus the selling expenses) will not result in a higher amount. The value in use of the cash-generating units is calculated according to the discounted cash flow (DCF) method. Here, based on company planning, a detailed planning period of three years is used. Corporate planning in the Kolbenschmidt Pierburg Group is done from the bottom up, considering past experiences and present forcasts.

Notes
Accounting Principles

Sales planning is based on sector forecasts for global automobile sales, the planned engine production figures of the automobile manufacturers, firm commitments by customers on individual projects, as well as company-specific adjustments.

The discount rate is based on the current weighted average cost of capital (WACC), 9.0 percent. For the period subsequent to the last planning year, a growth allowance is not applied as a corrective for the risk-specific discount rate before tax.

For acquisitions made prior to January 1, 2004, the previous form of consolidation stands, i.e. the book value method. The book values of goodwill generated through to December 31, 2003 are carried as procurement costs starting January 1, 2004. From this point on, there will be no further unscheduled amortization of goodwill. Value retention is regularly examined by means of an annual impairment test.

During the period under review, the goodwill of six cash-generating units was examined with regard to value retention. The cash-generating units correspond to the primary segments.

Shares of nongroup shareholders are disclosed as minority interests in the consolidatable capital of subsidiaries, including the profit or loss proratable to such minority interests. For acquisitions made starting January 1, 2004, the pro rata hidden reserves and burdens and the accompanying share of earnings are shown in minority interests.

Expenses and income as well as payables, liabilities and contingencies between consolidated companies are offset against each other. The intercompany supply of products and services is conducted on the basis of market prices as well as intercompany transfer prices, which regularly correspond to market prices. Unless they are not significant, intermediate results are eliminated. Accruals for deferred taxes are accrued based on the temporary, consolidation-induced differences in debt consolidation, the elimination of expenses and income, and the elimination of intermediate results.

Associated companies and joint ventures are carried at equity. Taking as point of departure the costs of acquisition at the time of purchase of these interests, the respective book value of the trade investment increases or decreases with changes in the equity of the associated companies or joint ventures, to the extent that these relate to the share of these companies owned by the Kolbenschmidt Pierburg Group.

Goodwill for investments calculated according to the equity method is calculated in accordance with the principles applying to full consolidation contained in IFRS 3; activated goodwill is carried under investments and is subject to an annual impairment test.

(4)
Currency translation

The functional currency concept has been adopted to translate the annual financial statements of non-German group companies into euros, one Turkish subsidiary excepted. As a rule, their functional currency equals the local currency. Therefore, assets and liabilities are translated at the mean current rates and the income statements at the annual average rates. The translation differences resulting there from, as well as those from translating prior-year carryovers are recognized in, and only in, equity. Goodwill created from the capital consolidation of non-German companies is carried at amortized historical cost and translated at the pertaining on the balance sheet date.

The financial statements of the Turkish subsidiary were prepared in accordance with the historical-cost concept and adjusted in line with the IAS 29 rules governing hyperinflationary economies. Due to changes in the general price level (GPL), the current financial statements and the 2003 comparatives were adjusted in the local currency by applying an inflation index of 14 percent (2003: 14%), and then translated into euros.

The exchange rate of the euro to other relevant currencies developed as follows:

Currency translation

		Mean rate in € at		Annual average rate in €	
		12/31/2003	**12/31/2004**	2003	**2004**
Brazil	*1 Brazilian real*	0.2771	0.2769	0.2890	0.2776
Great Britain	*1 pound sterling*	1.4207	1.4112	1.4501	1.4667
Canada	*1 Canadian dollar*	0.6104	0.6075	0.6284	0.6183
Czech Republic	*1 Czech koruna*	0.0308	0.0328	0.0314	0.0313
USA	*1 US dollar*	0.8001	0.7351	0.8824	0.8025
Turkey	*1.000.000 Turkish lira*	0.5473	0.5263	0.5635	0.5437
China	*1 Chinese yuan*	0.0967	0.0888	0.1066	0.0969
Japan	*1 Japanese yen*	0.0075	0.0071	0.0076	0.0075

In the local-currency financial statements of consolidated companies, currency receivables and payables as well as cash & cash equivalents are all translated at the current spot rate. Currency translation differences are duly recognized in the net financial result.

(5) Accounting and valuation methods

The financial statements of Kolbenschmidt Pierburg AG are prepared on the basis of Group-wide, consistently applied methods of accounting and valuation. Affiliated companies are valued according to the equity method.

Intangible assets

Purchased intangible assets are capitalized at acquisition cost, internally created intangibles from which the Group is believed to derive future economic benefits and which can reliably be measured are recognized at production cost, either type of intangible asset being amortized by straight-line charges over the estimated useful life. Production cost covers all costs directly allocable to the production process, including any proratable production-related overheads. The cost of finance is not capitalized. R&D costs are principally expensed. Development costs are exceptionally capitalized and amortized on a straight-line basis if a newly developed product or process can be clearly defined, technologically realized and used either internally or is destined for marketing (IAS 38), and if there is a reasonable assurance that its costs will be recovered by future cash inflows.

A differentiation is drawn between intangible assets with an unlimited period of utilization and those whose period of use is time-limited. Intangible assets with unlimited periods of utilization are those having no foreseeable limitations on their utilization. There is no scheduled amortization of these assets. Instead, they are subject to an annual impairment test, unless indications of a decline in value emerge during the course of the year. Under IFRS 3, goodwill always has an unlimited period of utilization. The impairment tests conducted during the fiscal year did no result in a requirement for amortization.

Intangible assets with a time-limited period of utilization are depreciated according to the straight-line method from the time utilization begins throughout the duration of its economically useful life. If certain factors hint at an impairment and the recoverable amount is below amortized costs, an intangible asset is written down. Wherever the reason for write-down has ceased to exist, the charge is reversed and the asset written up accordingly.

Notes
Accounting Principles

The following unchanged periods of utilization underlie amortization:

Useful life	
Concessions, franchises, industrial property rights	2–15 years
Development costs	5 years

Tangible assets

Tangible assets are carried at depreciated cost less any write-down. The production cost of internally made tangible assets comprises all costs directly allocable to the production or manufacturing process, including the proratable production-related overheads. Borrowing costs are not capitalized as part of cost. Tangible assets are principally depreciated on a straight-line basis over their estimated useful lives unless in exceptional cases another method better reflects the pattern of use.

As in 2003, tangible assets are systematically amortized over the following periods of utilization:

Useful life	
Buildings	20–77 years
Other structures	8–20 years
Production plant and machinery	3–20 years
Other plant, factory and office equipment	2–23 years

Public-sector subsidies and customer grants, whose characteristics cause them to fall into the category of investment subsidies, are shown separately from the respective investments and carried as assets.

Tangible assets obtained under capital leases are capitalized at the lower of their fair values or the present value of minimum rents and depreciated over the shorter of their estimated useful lives or underlying lease terms (IAS 17). If certain factors hint at an impairment and the recoverable amount is below depreciated cost, the tangible asset is written down. Wherever the reason for write-down has ceased to exist, the charge is reversed and the asset written up accordingly.

Financial assets

Shares in Group companies and associated affiliates not stated at equity, as well as the other long-term securities, all shown as financial assets and throughout belonging in the category available for sale, are carried at their fair values. When fair value cannot be reliably calculated, the assets are valued at historical cost. Unrealized gains and losses are accounted for in the reserve from fair valuation. Upon disposal, such gains or losses are duly recognized in the income statement. However, if a value has been impaired and fallen below cost, even unrealized losses are recognized in net income.

In accordance with IAS 39, long-term loans bearing interest at fair market rates are carried at amortized cost, whereas non- or low-interest loans are discounted.

Inventories

Inventories are recognized at cost, as a rule applying the average-price method to acquisition cost whereas production cost comprises all costs directly allocable to the production or manufacturing process, including proratable production-related overheads. The latter include indirect materials, indirect manufacturing costs (labor, etc.), as well as production-related depreciation and pension expenses. The calculation is based on normal employment. In accordance with IAS 23, borrowing costs are not activated as procurement or manufacturing costs. Risks inherent in inventories due to reduced utility or to obsolescence are adequately allowed for. If the net realizable value (NRV) of any inventories at balance sheet date is below their carrying value, such inventories are written down to NRV. These valuation allowances are treated as an increase in material expenses (raw material and supplies) or as a decrease in inventory (work-progress inventory and finished goods). If the NRV of inventories previously written down has risen, the ensuing write-up is offset against cost of materials (raw materials and supplies) or shown as increase in inventories of finished products and work in process (WIP).

Down payments for orders not constituting manufacturing orders as defined by IAS 11, are, in situations where manufacturing costs have already arisen in connection with a given contract, capitalized and carried separately from inventories. All other payments are stated as liabilities.

Receivables and sundry assets

Receivables and sundry assets are capitalized at cost. Adequate allowances provide for bad debts and doubtful accounts.

Without exception, securities contained in current assets fall into the category ‘available for sale’, and are stated at their fair value at the balance sheet date. Prior to realization, changes in the reported fair value of securities are treated as having a neutral effect on earnings. However, if substantial indications of a decline in value exist, the unrealized losses are shown with their effect on earnings.

Deferred taxes

Under the terms of IAS 12, deferred taxes are duly recognized on differences between the values of assets and liabilities in the consolidated balance sheet and those in the individual companies’ tax accounts. Deferred tax assets also include tax reduction claims from the expected future utilization of tax loss carryovers, always provided that their realization is reasonably certain. If the recent history of a company shows a series of losses, deferred tax assets from unutilized tax losses or credits are only recognized to the extent that the company reports sufficient taxable temporary differences or that conclusive substantive evidence exists which suggests with reasonable assurance that sufficient taxable income will be earned by the company to utilize the hitherto unused tax losses or credits. Deferred taxes are determined by applying the local tax rates current or announced in each country at balance sheet date.

The calculated rate of deferred taxation in Germany remained unchanged at 40 percent (including the corporation tax, solidarity surtax and municipal trade tax on income). Deferred taxation rates outside of Germany ranged between 26 and 40 percent (2003: 28 to 38 percent). In the Czech Republic and France new tax rates came into force.

On December 22, 2003, the system governing the tax treatment of losses in Germany was altered (“Korb II”, a law amending the Municipal Trade Tax Act and other laws). From January 1, 2004 onwards, the taxable income of a joint stock corporation can be netted by only 60 percent with tax loss carryover from previous years; a base amount of €1 million of income can be netted indefinitely. This rule also applies to Municipal Trade Tax loss carryovers.

Also altered was the rule governing tax exemption on capital gains from the sale of participations to joint stock corporations. Starting January 1, 2004, 5 percent of these capital gains must be allocated to taxable income as non-deductible operating expenses.

For fiscal 2004, these changes in the legal framework have had no impact on deferred tax expenditure or claims.

Deferred tax netting is based on the rules of IAS 12.

Notes
Accounting Principles

Minority interests

Minority interests represent those portions of a subsidiary's net income and equity which are allocable to shares not held by Kolbenschmidt Pierburg AG, whether directly, or indirectly via other subsidiaries. Minority interests are shown in separate lines, in addition to debt and stockholders' equity as well as to Group net income.

Accruals

Accruals for pensions and similar obligations are measured according to the internationally accepted projected unit credit (PUC) method, which is predicated not only on biometrical assumptions (life expectancy/mortality), expected future pay and pension trends, the variation in retiree assumption rates, interest rate trends, but also further actuarial and other parameters. The actuarial gains and losses ensuing from differences between actuarial assumptions and actual trends of the underlying parameters give rise to a gap between the present value of the defined benefit obligation (DBO) in accordance with IAS 19, and the pension liabilities accrued in the balance sheet. Actuarial gains and losses outside a 10-percent corridor of the DBO are distributed over the average residual service years of employees. The fair market value of any existing plan or pension fund assets is deducted from pension accruals. Service cost is treated as personnel expense while the interest portion of pension provisions in the fiscal year is shown within the net financial result. Contributions to defined contribution plans (DCPs), under which the company incurs no obligation other than the payment of contributions to earmarked pension funds or appropriated plans, are expensed in the year of their incurrence.

The remaining accruals according to IAS 37 provide at balance sheet date for all identifiable legal and constructive commitments and obligations to third parties if based on past transactions or events and if their amount, due date or maturity is uncertain. Accruals are measured at the best estimate of the settlement amount. Noncurrent accruals are shown, if the effect of discounting is significant, at the settlement amount discounted as of balance sheet date. The settlement amount also contains the cost increases to be taken into account.

Liabilities

Pursuant to IAS 39, liabilities are stated at amortized cost, which as a rule equals their settlement or repayment amounts. Liabilities under capital leases are recognized at the present value of future rents.

Prepaid and deferred items

Such items are disclosed to appropriately recognize pro rata temporis (p.r.t.) any rents, interest, insurance premiums, private-sector investment grants or allowances, etc. that have been prepaid or received in advance.

In accordance with IAS 20, non-investment related subsidies and grants for expenses are carried as income and appear in the consolidated income statement at the point in time they are used.

If the discounted interest effect on long-term prepaid income is substantial, it is carried at the discounted amount outstanding at the balance sheet date.

If the sale price of an asset that has been sold and leased back is above the booked costs of procurement and manufacturing, the capital gains are shown as a liability and stated in the consolidated income statement for the duration of the non-terminable basic period of lease.

Contingent liabilities and assets

Contingent liabilities are potential or existing liabilities, relating to past events or to cases where a fund outflow is unlikely.

Contingent assets are potential assets whose existence must be confirmed by the subsequent occurrence of one or more events, which are outside of the company's sphere of influence.

Contingent liabilities and assets are stated with their probable realization amounts.

Income and expenses

Net sales (revenues) and other operating income are recognized upon performance of the contract for goods/services or upon passage of risk to the customer. Operating expenses are recognized when caused or when the underlying service, etc. is used. The accrual basis of accounting is applied to interest income and expenses.

Derivative financial instruments

Within the Kolbenschmidt Pierburg Group, financial derivatives are solely used to hedge against currency and interest rate risks from operations.

Pursuant to IAS 39 Financial Instruments all financial derivatives are recognized at historical cost at the time of purchase and thereafter fair-valued as of the balance sheet date. Financial derivatives with a positive or negative fair value are disclosed as sundry assets or sundry liabilities, respectively.

Fundamentally, any changes in the fair value of financial derivatives are immediately recognized in net income unless an effective hedge exists that satisfies the criteria of IAS 39. If the derivative is a cash flow hedge (CFH) and hence used to effectively hedge expected future cash flows, changes in the financial derivative's fair value are recognized in equity only, under the other reserves. In this case, the changes in the derivative's value would not impact on net income until after the hedged underlying transaction has fallen due or been settled.

Changes in the value of financial derivatives used in fair value hedges (FVHs) to effectively hedge the fair value of recognized assets and liabilities are posted to net income as are any changes in the hedged assets or liabilities (where appropriate, by adjusting their book values), with the result that the compensatory effects are all reflected in the income statement.

The ineffective part of a hedge transaction is carried in the consolidated income statement under other financial income and/or expenses.

Notes
to the consolidated balance sheet

(6) Fixed asset analysis *€ million*

	Gross values			
	12/31/ 2002	Additions	Disposals	Book transfers
Intangible assets				
Development costs and other internally created intangibles	17.5	5.4	0.0	1.1
Concessions, franchises, industrial property rights and licenses	18.5	5.9	0.6	5.5
Goodwill	74.5	0.0	(1.7)	0.0
Badwill from consolidation	(6.0)	0.0	(6.0)	0.0
Prepayments on intangibles	4.7	1.0	0.0	(5.1)
	109.2	12.3	(7.1)	1.5
Tangible assets				
Land, equivalent titles, and buildings (incl. buildings on leased land)	320.9	5.9	1.2	3.6
Production plant and machinery	1,085.6	47.3	23.1	32.3
Other plant, factory and office equipment	276.6	11.9	20.1	12.0
Prepayments on tangibles	8.0	6.7	0.1	(6.7)
Construction in progress	48.8	42.4	0.9	(42.7)
	1,739.9	114.2	45.4	(1.5)
Financial assets				
Shares in joint ventures	12.7	9.0	0.0	8.0
Shares in associated affiliates	15.6	0.0	0.0	(8.0)
Other long-term securities	1.2	0.0	0.0	0.0
Sundry long-term loans	2.6	0.1	1.1	0.0
	32.1	9.1	1.1	0.0
Total	**1,881.2**	**135.6**	**39.4**	**0.0**
	12/31/ 2003	Additions	Disposals [1]	Book transfers
Intangible assets				
Development costs and other internally created intangibles	24.0	4.8	0.0	0.0
Concessions, franchises, industrial property rights and licenses	28.9	10.0	0.5	0.8
Goodwill	74.9	0.0	27.2	0.0
Prepayments on intangibles	0.6	0.0	0.0	(0.5)
	128.4	14.8	27.7	0.3
Tangible assets				
Land, equivalent titles, and buildings (incl. buildings on leased land)	323.1	4.7	4.5	2.0
Production plant and machinery	1,104.3	48.0	57.4	37.9
Other plant, factory and office equipment	278.4	17.7	24.8	9.5
Prepayments on tangibles	7.9	6.2	0.0	(4.5)
Construction in progress	45.0	41.3	0.3	(45.2)
	1,758.7	117.9	87.0	(0.3)
Financial assets				
Shares in joint ventures	29.7	0.0	0.1	0.0
Shares in associated affiliates	7.6	0.0	7.6	0.0
Other long-term securities	1.2	0.0	0.0	0.0
Sundry long-term loans	1.6	0.1	0.7	0.0
	40.1	0.1	8.4	0.0
Total	**1,927.2**	**132.8**	**123.1**	**0.0**

[1] *First-time application of IFRS 3; the historical costs of goodwill were reduced by the amount of accumulated amortization.*

		Amortization/depreciation/write-down						Net values	
Currency translation differences	**12/31/ 2003**	12/31/ 2002	Deprecia-tion during fiscal year	Disposals	Book transfers	Currency translation differences	**12/31/ 2003**	12/31/ 2002	**12/31/ 2003**
0.0	24.0	7.8	3.3	0.0	0.0	0.0	11.1	9.7	12.9
(0.4)	28.9	11.8	3.1	0.6	0.0	(0.3)	14.0	6.7	14.9
(1.3)	74.9	21.5	4.0	(1.7)	0.0	(1.0)	26.2	53.0	48.7
0.0	0.0	(6.0)	0.0	(6.0)	0.0	0.0	0.0	0.0	0.0
0.0	0.6	0.0	0.0	0.0	0.0	0.0	0.0	4.7	0.6
(1.7)	128.4	35.1	10.4	(7.1)	0.0	(1.3)	(51.3)	74.1	77.1
(6.1)	323.1	135.0	11.5	0.3	0.0	(2.2)	144.0	185.9	179.1
(37.8)	1,104.3	781.2	83.2	19.9	0.0	(26.1)	818.4	304.4	285.9
(2.0)	278.4	203.2	30.9	18.2	0.0	(1.7)	214.2	73.4	64.2
0.0	7.9	0.0	0.0	0.0	0.0	0.0	0.0	8.0	7.9
(2.6)	45.0	0.0	0.0	0.0	0.0	0.0	0.0	48.8	45.0
(48.5)	1,758.7	1,119.4	125.6	38.4	0.0	(30.0)	1,176.6	620.5	582.1
0.0	29.7	0.0	0.0	0.0	0.0	0.0	0.0	12.7	29.7
0.0	7.6	0.0	0.0	0.0	0.0	0.0	0.0	15.6	7.6
0.0	1.2	0.3	0.0	0.0	0.0	0.0	0.3	0.9	0.9
0.0	1.6	0.1	0.0	0.0	0.0	0.0	0.1	2.5	1.5
0.0	40.1	0.4	0.0	0.0	0.0	0.0	0.4	31.7	39.7
(50.2)	**1,927.2**	**1,154.9**	**136.0**	**31.3**	**0.0**	**(31.3)**	**1,228.3**	**726.3**	**698.9**

Currency translation differences	**12/31/ 2004**	12/31/ 2003	Deprecia-tion during fiscal year	Disposals	Book transfers	Currency translation differences	**12/31/ 2004**	12/31/ 2003	**12/31/ 2004**
0.0	28.8	11.1	2.7	0.0	0.0	0.0	13.8	12.9	15.0
(0.1)	39.1	14.0	5.6	0.5	0.0	(0.1)	19.0	14.9	20.1
(0.7)	47.0	26.2	0.0	25.6	0.0	(0.6)	0.0	48.7	47.0
0.0	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.6	0.1
(0.8)	115.0	51.3	8.3	26.1	0.0	(0.7)	32.8	77.1	82.2
(2.4)	322.9	144.0	10.4	2.6	0.0	(0.9)	150.9	179.1	172.0
(15.4)	1,117.4	818.4	75.9	53.5	0.0	(11.0)	829.8	285.9	287.6
(0.7)	280.1	214.2	27.2	23.5	0.0	(0.7)	217.2	64.2	62.9
0.0	9.6	0.0	0.0	0.0	0.0	0.0	0.0	7.9	9.6
(0.9)	39.9	0.0	0.0	0.0	0.0	0.0	0.0	45.0	39.9
(19.4)	1,769.9	1,176.6	113.5	79.6	0.0	(12.6)	1,197.9	582.1	572.0
0.0	29.6	0.0	0.0	0.0	0.0	0.0	0.0	29.7	29.6
0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	7.6	0.0
0.0	1.2	0.3	0.0	0.0	0.0	0.0	0.3	0.9	0.9
0.0	1.0	0.1	0.0	0.0	0.0	0.0	0.1	1.5	0.9
0.0	31.8	0.4	0.0	0.0	0.0	0.0	0.4	39.7	31.4
(20.2)	**1,916.7**	**1,228.3**	**121.8**	**105.7**	**0.0**	**(13.3)**	**1,231.1**	**698.9**	**685.6**

Notes
to the consolidated balance sheet

(7)
Intangible assets

The intangible assets mainly comprise goodwill from consolidation.

In the year under review, R&D costs of €102.0 million were incurred (up from €86.8 million), €4.8 million of which (down from €5.4 million) met the capitalization criteria as defined in the IFRS.

The following amounts were charged to other operating expenses:

Research and development costs chargeable as expenditure *€ million*

	2003	**2004**
Research costs and noncapitalized development costs	78.1	94.5
Amortization of capitalized development costs	3.3	2.7
R&D costs expensed	81.4	97.2

The total amortization of intangible assets amounted to €8.3 million (down from €10.4 million). Owing to the continuation of a project being cancelled, a special write-down amounting to €0.1 million occurred during the year under review (2003: €0.0 million). Along with netting of the cumulated amortization, also included in goodwill are disposals from a subsequent payment reimbursement of €1.1 million and the correction of goodwill from a subsequent captilization of loss carryovers of €0.5 million.

(8)
Tangible assets

Depreciation in 2004 amounted to €113.5 million, down from €125.6 million the previous year. The figure for 2004 contains €2.4 million in special write-downs (2003: €6.2 million), of which €1.5 million related to technical plant and equipment, and €0.9 million to production plant and machinery made redundant by cancelled orders.

Last year's encumbrances of €17.0 million on land and buildings to collateralize long-term investment loans, as well as the production plant and machinery worth €8.8 million assigned as security for an investment loan, were entirely eliminated due to repayment of the loan.

The property, plant & equipment capitalized under capital leases total €22.2 million (down from €31.1 million), of which €8.1 million (down from €8.7 million) is allocable to a long-term property lease; another €14.1 million (2003: €22.4 million) refers exclusively to capital leases for production plant and machinery used in current production. Lease terms vary between four and ten years. Depending on the local market and the contracting date, the interest rates underlying these leases range from 5.9 to 8.0 percent, just as in 2003.

Fixed Assets and Capital Leases *€ million*

	Gross book values			Depreciation				Net book values	
	12/31/2002	Disposals	**12/31/2003**	12/31 2002	Depreciation during fiscal year	Disposals	**12/31/2003**	12/31/2002	**12/31/2003**
Real property and equivalent rights and buildings	12.1	0.0	12.1	2.9	0.5	0.0	3.4	9.2	8.7
Technical equipment and machinery	89.8	1.6	88.2	57.2	9.0	0.4	65.8	32.6	22.4
Total	**101.9**	**1.6**	**100.3**	**60.1**	**9.5**	**0.4**	**69.2**	**41.8**	**31.1**
	12/31/2003	Disposals	**12/31/2004**	12/31 2003	Depreciation during fiscal year	Disposals	**12/31/2004**	12/31/2003	**12/31/2004**
Real property and equivalent rights and buildings	12.1	0.0	12.1	3.4	0.6	0.0	4.0	8.7	8.1
Technical equipment and machinery	88.2	0.9	87.3	65.8	7.9	0.5	73.2	22.4	14.1
Total	**100.3**	**0.9**	**99.4**	**69.2**	**8.5**	**0.5**	**77.2**	**31.1**	**22.2**

The future rents payable under capital leases, the interest portions therein included, as well as the present values of future rents (recognized at equal amounts as financial debts) are all shown in the table below:

Rents in subsequent years – Finance leasing *€ million*

	2003				**2004**			
	2004	2005–2008	from 2009	Total	2005	2006–2009	from 2010	Total
Rents	9.4	19.2	16.6	45.2	7.2	15.5	17.9	40.6
Discount	2.0	5.1	4.9	12.0	1.6	4.4	4.3	10.3
Present values	7.4	14.1	11.7	33.2	5.6	11.1	13.6	30.3

There are no subleases.

NOTES
TO THE CONSOLIDATED BALANCE SHEET

(9)
Financial assets

The share of assets and liabilities as well as income and expenses from joint ventures at the balance sheet date are as follows:

Joint Ventures *€ million*

	2003	**2004**
Assets [1]	35.4	32.3
of which long-term	*[20.9]*	*[16.8]*
Equity	23.1	21.1
Debts [2]	12.3	11.3
of which long-term	*[4.7]*	*[4.5]*
Income	50.0	50.3
Expenses	42.1	43.8
Net income	7.9	6.5

[1] *Including income tax and prepaid expenses and deferred charges*
[2] *Accruals, lliabilities, income tax and deferred income*

Participations in joint ventures and affiliated companies developed as follows:

Financial assets *€ million*

	Book value 12/31/ 2003	Disposals	P/L share	Dividend payments	**Book value 12/31/ 2004**
Joint Ventures					
Kolbenschmidt Pierburg Shanghai Nonferrous Components Co. Ltd.	16.2	0.0	4.2	4.1	16.3
Kolbenschmidt Shanghai Pistons Co. Ltd.	13.5	0.0	2.3	2.5	13.3
	29.7	**0.0**	**6.5**	**6.6**	**29.6**
Associated affiliates					
Pierburg Instruments GmbH	7.6	7.6	0.0	0.0	0.0
	7.6	**7.6**	**0.0**	**0.0**	**0.0**

The remaining other long-term securities at a total book value of €0.9 million (2003: €0.9 million), for which no quoted market price is available and whose fair value cannot reliably be determined are stated at amortized cost.

In accordance with IAS 39, other loans are carried at historical cost.

(10)
Inventories

Inventories *€ million*	2003	**2004**
Raw materials and supplies	65.0	72.4
Work in process	54.3	64.0
Finished products and merchandise	92.3	100.7
Prepayments made	0.8	1.6
	212.4	**238.7**
Prepayments received	(7.1)	(12.4)
	205.3	**226.3**

The book value of inventories stated at the lower NRV totals €18.3 million (down from €22.6 million in 2003). Write-downs in fiscal 2004 amounted to €1.7 million (2003: €1.2 million). In the year under review, €2.6 million (up from €2.2 million) of inventories previously written down was written up as their NRV had risen.
Inventories are not used to collateralize liabilities.

(11)
Receivables and sundry assets

Receivables and sundry assets *€ million*	2003	of which due >1 year	**2004**	of which due >1 year
Trade receivables of which due from	194.8	0.0	179.7	0.0
related parties	*[0.0]*	*[0.0]*	*[3.5]*	*[0.0]*
All other receivables and sundry assets	33.4	1.3	26.2	1.1
	228.2	**1.3**	**205.9**	**1.1**

The disclosed book values of the monetary assets covered by these items approximate their fair values.

Under an ABS program, the Kolbenschmidt Pierburg Group sells inter alia trade receivables on a revolving basis up to a maximum volume of €175.3 million (2003: €126.7 million). In accordance with IAS 39, the receivables are to be treated as sold, as the remaining risks to the company are insignificant. As of December 31, 2004, the receivables sold had a par value of €127.2 million (up from €93.1 million).

Notes
to the consolidated balance sheet

Sundry assets encompass:

Other receivables and sundry assets *€ million*	2003	of which due > 1 year	2004	of which due > 1 year
Accounts due for/from				
non-income taxes	13.0	0.8	9.5	1.1
financing	14.0	0.0	3.8	0.0
prepayments made	0.6	0.0	1.0	0.0
guaranty fund	1.1	0.0	4.1	0.0
investment grants/allowances	0.2	0.0	2.4	0.0
Other	4.5	0.5	5.4	0.0
	33.4	**1.3**	**26.2**	**1.1**

In 2004, allowances for doubtful receivables and sundry assets were charged at €2.1 million (2003: €2.6 million).

(12)
Cash and cash equivalents

Cash & cash equivalents *€ million*	2003	2004
Cash on hand and checks	2.3	0.7
Cash in banks	40.4	67.5
	42.7	**68.2**

As in the previous year, the availability of cash and cash equivalents was not subject to limitation.

(13)
Income tax assets

Income tax assets *€ million*	2003	2004	of which recognized in net income	of which not recognized in net income
Deferred taxes				
from temporary differences	21.7	20.2	20.5	(0.3)
from loss carryforward and tax credits	12.7	16.0	16.0	0.0
	34.4	36.2	36.5	(0.3)
Income tax refundable by the tax authorities	1.8	1.1	1.1	0.0
	36.2	**37.3**	37.6	(0.3)

At the end of the 2004, tax reduction claims of €16.0 million (2003: €12.7 million) were carried, deriving from the expected utilization of existing loss carry-overs and tax credits in subsequent years. Loss carry-overs are stated on the basis of corporate planning data at the amount of budgeted future taxable income.

Over and above the deferred tax assets from loss carryovers and tax credits, German and foreign tax loss carryovers exist at a total of €143.3 million (down from €165.9 million), and foreign tax credits of €1.8 million (down from €2.5 million), which were not recognizable. The loss carryovers amount to €59.9 million (2003: €59.1 million) in Germany, with an another €83.4 million (up from €106.8 million) existing abroad. Even after the introduction of minimum taxation, domestic loss carryovers are not subject to expiration. Of the foreign loss carryovers, €4.7 million (2003: €0.4 million) expire between 2005 and 2007; €78.7 million (2003: €104.5 million) expire between 2008 and 2024. The non-reported foreign loss carryovers contain tax credits of €1.8 million (2002: €2.5 million), and will not expire or expire between six and 25 years. Deferred taxes amounting to €4.2 million were written up (2003: €0.0 million) on loss carryovers not taken into account in prior periods. The change in the write-downs of activated deferred taxes in 2004 amounts to (€0.9 million), compared to €0.0 million the year before.

(14)
Equity/Minority interests

Kolbenschmidt Pierburg AG's capital stock amounts to €71.7 million and is divided into 28,003,395 no-par bearer shares of fully voting common stock. No unpaid capital is subscribed.

Unchanged from the previous year, the additional paid-in capital amounts to an unchanged €174.0 million.

The other reserves include, besides retained reserves, differences from currency translation, as well as hedge reserves. During fiscal 2004, these reserves developed along the following lines:

Plan assets at fair value *€ million*

	Hedge reserve
Balance at January 1, 2003	**(0.4)**
Exchange differences	0.2
Changes in fair value	1.2
Deferred taxes	(0.5)
Balance at January 1, 2004	**0.5**
Changes in fair value	0.2
Deferred taxes	(0.2)
Balance at December 31, 2004	**0.5**

The differences from the fair valuation of an interest rate swap transaction liquidated in October 2004 were transferred to the hedge reserve. Fair value at the time of the disposal amounted to €0.0 million (2003: €0.8 million). Furthermore, differences from the fair valuation of individual currency forward transactions concluded for hedging planned purchases of materials up until 2007 are carried here, and are neutral in their effect on profits. Valuation is at fair value.

Prepared in accordance with HGB standards, the individual financial statements of Kolbenschmidt Pierburg AG show net income for the year of €59.0 million (2003: €19.0 million), of which the Executive Board and Supervisory Board have resolved to appropriate €29.5 million to profit reserves (2003: €5.0 million). The profit shown on the balance sheet after the appropriation to reserves is €29.5 million (€14.0 million). Of this amount, €19.6 million will be disbursed (2003: €14.0 million), while €9.9 million will be appropriated to profit reserves (2003: €0.0 million). The dividend proposed amounts to €0.70 (2003: €0.50) per non-par share of stock.

Notes
to the consolidated balance sheet

(15)
Accruals for pensions

These accruals provide for obligations under vested rights and current pensions payable to eligible active and former employees and their surviving dependants. Such commitments primarily encompass pensions, both basic and supplementary. The individual confirmed pension entitlements are based on benefits that vary according to country and company and, as a rule, are measured according to service years and employee pay. Being a noncurrent provision for the accumulated postretirement benefit obligation, the accrued health care obligations to the retirees of some US group companies are also included in the pension accruals recognized hereunder.

The company pension system consists of both defined-contribution and defined-benefit plans. Under a DCP, the company incurs no obligations other than the payment of contributions to earmarked funds or appropriated plans. These pension expenses are shown within personnel expenses. In the year under review, a total €21.4 million (down from €24.3 million) was paid to DCPs.

Under defined benefit plans, a company is obligated to meet its confirmed commitments to active and former employees.

The following parameters underlay the actuarial calculation:

Pension accruals – calculation parameters *in %*

	12/31/2003		**12/31/2004**	
	Germany	USA	Germany	USA
Discount rate	5.50	6.00	4.75	5.60
General pay rise	3.00	4.00	3.00	4.00
Pay rise (firm commitment)	1.25	--	1.25–0.5	--
Pension rise	1.25	--	1.25	--
Health care cost rise	--	14.0–5.0	--	11.0–5.0
Expected return on plan assets	--	9.00	--	8.50

As a result of the downward drift of interest rates in the German capital market, the interest rate for German pension obligations was reduced by 0.75 percentage points. Adjustment of the US interest rate by 0.40 percentage points was undertaken in response to the lowering of the relevant capital market interest rates. Furthermore, the interest rate for the anticipated trend in the plan assets was lowered by 0.50 percentage points.

Pension accruals developed along the following lines:

Pension accruals *€ million*

	2003	**2004**
Balance at January 1	**272.9**	**256.5**
Pension payments and contributions to plan	(29.8)	(34.7)
Service cost	5.3	5.8
Effects of plan curtailments/settlements	(1.1)	0.0
Past service costs/revenue	(1.5)	(0.6)
Amortized insurance-related gains and losses	2.6	1.9
Compounding of expected pension obligations	19.9	18.6
Expected return on plan assets	(4.3)	(5.2)
Exchange differences/other	(7.5)	(1.1)
Balance at December 31	**256.5**	**241.2**

The pension accruals derive from the present value of the DBO as well as the plan assets:

Pension accruals – transition *€ million*

	2003			**2004**		
	Germany	Abroad	Total	Germany	Abroad	Total
Analysis of the DBO's present value						
Present value of DBO at January 1	217.9	151.5	369.4	220.0	123.5	343.5
Exchange differences	0.0	(22.8)	(22.8)	0.0	(9.0)	(9.0)
Service cost	3.6	1.7	5.3	4.4	1.5	5.9
Interest cost	11.7	8.2	19.9	11.8	6.8	18.6
Pension payments	(12.9)	(13.5)	(26.4)	(11.8)	(14.9)	(26.7)
Plan curtailment/settlements	(0.1)	(1.0)	(1.1)	0.0	0.0	0.0
Unrecognized past service returns/costs	0.0	(1.6)	(1.6)	0.0	0.0	0.0
Actuarial gains/losses	(0.2)	1.0	0.8	21.7	4.2	25.9
Plan assets at fair value at December 31	**220.0**	**123.5**	**343.5**	**246.1**	**112.1**	**358.2**
Development of plan assets						
Present value of DBO at Januar 1	0.0	53.9	53.9	0.0	58.2	58.2
Exchange differences	0.0	(9.6)	(9.6)	0.0	(5.7)	(5.7)
Expected return on plan assets	0.0	4.3	4.3	0.0	5.2	5.2
Contributions to plan	0.0	17.1	17.1	0.0	20.8	20.8
Pension payments of plan	0.0	(13.7)	(13.7)	0.0	(12.8)	(12.8)
Actuarial gains/losses	0.0	6.2	6.2	0.0	(0.7)	(0.7)
Present fair value of DBO at December 31	**0.0**	**58.2**	**58.2**	**0.0**	**65.0**	**65.0**
Unfunded pension obligations at December 31						
Unrecognized actuarial gains/losses	(3.7)	(28.5)	(32.2)	(25.4)	(29.2)	(54.6)
Unrecognized past service returns/costs	0.0	3.4	3.4	0.0	2.6	2.6
Pension accrual at December 31	**216.3**	**40.2**	**256.5**	**220.7**	**20.5**	**241.2**

The present value of funded pension obligations at December 31, 2004, came to €104.1 million (2003: €114.0 million). The unrecognized actuarial losses of €54.6 million (up from €32.2 million) are substantially the result of adjusted discount rates and of the deviating actual vs. expected return on plan assets. In 2004, actual investment income of the plan assets came to €4.5 million, (2003: €10.5 million), prior to a foreign currency loss with a neutral impact on earnings. Actuarial losses are expensed over the average residual service years if outside a corridor of 10 percent of total DBO, those proratable to the year under review amounting to €1.9 million (2003: €2.6 million).

Plan assets break down as follows:

Pension accruals – plan assets *€ million*

	2003	**2004**
Equities	37.1	35.5
Government and corporate bonds	18.3	18.3
Cash & cash equivalents	2.8	11.2
Plan assets	**58.2**	**65.0**

Notes
to the consolidated balance sheet

Pension expenses are structured as follows:

Pension expenses *€ million*

	2003	**2004**
Current service cost	5.3	5.8
Amortized actuarial gains/losses	2.6	1.9
Past service cost/revenue	(1.5)	(0.6)
Effects of plan curtailments/settlements	(1.1)	0.0
Expected return on assets	(4.3)	(5.2)
Compounding of expected pension obligations	19.9	18.6
	20.9	**20.5**

The interest portion in the 2004 pension provision, as well as the expected return on plan assets, are shown within net interest expense, the remaining items being included in personnel expenses.

(16)
Other accruals

Other accruals *€ million*

	Warranties	Identifiable losses	Outstanding costs [1]	Restructuring	Sales remuneration	Environmental risks	Personnel	Other	Total
Balance at January 1, 2003	**19.7**	**15.6**	**9.3**	**1.8**	**1.9**	**3.4**	**49.5**	**21.2**	**122.4**
Utilized	(4.0)	(8.1)	(8.5)	(0.4)	(1.6)	(0.3)	(37.7)	(7.2)	(67.8)
Released	(1.7)	(1.4)	0.0	(0.7)	(0.2)	0.0	(1.2)	(0.9)	(6.1)
Added/newly provided	10.8	5.7	11.2	3.6	2.0	1.6	49.4	7.4	91.7
Compounded	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.1	0.2
Exchange differences/other	(0.2)	(0.3)	0.7	(0.1)	0.0	(0.4)	(0.8)	(1.4)	(2.5)
Balance at January 1, 2004	**24.7**	**11.5**	**12.7**	**4.2**	**2.1**	**4.3**	**59.2**	**19.2**	**137.9**
Utilized	(3.3)	(4.7)	(11.4)	(0.5)	(1.9)	(0.6)	(38.8)	(11.2)	(72.4)
Released	(3.5)	(1.6)	(0.3)	(0.2)	0.0	(0.1)	(0.5)	(2.4)	(8.6)
Added/newly provided	6.3	2.9	0.6	0.7	3.0	0.9	55.4	10.9	80.7
Compounded	0.2	0.0	0.0	0.0	0.0	0.0	0.0	0.1	0.3
Exchange differences/other	0.0	0.0	0.0	0.0	0.0	(0.2)	(0.3)	(0.2)	(0.7)
Balance at December 31, 2004	**24.4**	**8.1**	**1.6**	**4.2**	**3.2**	**4.3**	**75.0**	**16.4**	**137.2**

[1] *Until 2003 including outstanding invoices, which were transferred to liabilities starting in 2004.*

Known specific warranty risks are accrued at the anticipated amount of the obligation. Accruals for identified losses provide for binding purchasing obligations. Any economic risks beyond are also adequately provided for.

Accruals for obligations to personnel essentially provide for accrued vacation, residual annual leave, overtime and flextime at a total €18.2 million (down from €18.7 million); for pre-retirement part-time work at €13.3 million (2003: €12.2 million); and for termination benefits at €11.1 million (up from €5.9 million).

As in 2003, no refunds are expected from accruals. The following cash outflows are predicted for each category of the discounted noncurrent accruals:

Payment outflow accruals *€ million*

	within 1 year	1–5 years	after 5 years	Total
Warranties	18.6	5.8	0.0	24.4
Identifiable losses	8.1	0.0	0.0	8.1
Outstanding costs	1.0	0.6	0.0	1.6
Restructuring	0.5	3.7	0.0	4.2
Sales remuneration	2.6	0.6	0.0	3.2
Environmental risks	3.1	0.8	0.4	4.3
Personnel	51.0	21.3	2.7	75.0
Other	12.5	3.8	0.1	16.4
	97.4	**36.6**	**3.2**	**137.2**

(17)
Liabilities

Liabilities *€ million*

	12/31/2003	of which due within <1 year	of which due within >5 years	**12/31/2004**	of which due within <1 year	of which due within >5 years
Financial liabilities						
due to banks	74.8	7.9	25.5	15.0	5.1	0.0
due to non-consolidated Group companies	10.9	10.9	0.0	0.0	0.0	0.0
under leases	59.4	8.5	11.7	47.1	5.9	10.4
other	2.2	0.5	0.0	2.3	0.5	0.8
	147.3	27.8	37.2	64.4	11.5	11.2
Trade payables	173.0	173.0	0.0	180.1	180.1	0.0
All other liabilities						
prepayments received on orders	9.6	9.6	0.0	16.5	16.5	0.0
notes payable (trade)	9.1	9.1	0.0	9.9	9.9	0.0
[1] Outstanding invoices	0.0	0.0	0.0	18.1	18.1	0.0
Sundry liabilities	79.7	77.6	0.0	85.8	82.4	0.0
	98.4	96.3	0.0	130.3	126.9	0.0
	418.7	**297.1**	**37.2**	**374.8**	**318.5**	**11.2**

[1] *Shown under Other accruals until 2003*

The financial debts under leases include accounts payable by the special-purpose leasing firms to banks at €21.5 million (down from €26.2 million). Debts owed to banks continue to contain no finance bill liabilities.

Out of the accounts due to banks, €0.0 million (2003: €17.0 million) is collateralized by land charges and similar encumbrances, another €0.5 million (€9.3 million) being secured by similar rights and interests.

Notes
to the consolidated balance sheet

Sundry liabilities break down as follows:

Sundry liabilities *€ million*

	12/31/2003	**12/31/2004**
Monies in transit	39.1	50.5
Non-income taxes	10.4	9.3
Social security	13.2	13.9
Due to employees	9.0	5.9
Other liabilities	8.0	6.2
	79.7	**85.8**

There were no liabilities to joint ventures or associated affiliates (2003: €0.3 million). The book values of trade payables and all other liabilities approximate their fair values.

The analysis below reflects the terms and book and fair values of financial debts:

Liabilities due to banks

Terms	Weighted rate *in %*	Currency	Book value 12/31/2003 *€ million*	Market value 12/31/2003 *€ million*	Rates fixed until	Book value **12/31/2004** *€ million*	Market value **12/31/2004** *€ million*
fixed	1.0	¥	2.3	2.3	2005	1.4	1.4
fixed	1.0	¥	1.2	1.2	2006	0.7	0.8
fixed	5.2	*€/Rs*	1.2	1.3	2007	8.1	8.4
fixed	3.0	*US$*	3.6	3.8	2008	2.6	2.3
Variable		*€/Rs*	2.9	2.9	2005	2.3	2.3

Liabilities due to banks of special-purpose leasing firms

Terms	Weighted rate *in %*	Currency	Book value 12/31/2003 *€ million*	Fair value 12/31/2003 *€ million*	Rates fixed until	Book value **12/31/2004** *€ million*	Market value **12/31/2004** *€ million*
fixed	4,9	€	26.2	27.4	2008	21.5	22.9

Due under capital leases

Terms	Weighted rate *in %*	Currency	Book value 12/31/2003 *€ million*	Fair value 12/31/2003 *€ million*	Rates fixed until	Book value **12/31/2004** *€ million*	Market value **12/31/2004** *€ million*
fixed	5.9	€	3.5	3.7	2005	1.9	1.9
fixed	5.9	€	5.2	5.5	2006	3.7	3.8
fixed	6.5	€	4.9	5.8	2008	4.2	5.0
fixed	6.5	€	3.6	3.9	2010	3.2	3.5
fixed	6.5	€	0.6	0.6	2011	0.5	0.5
fixed	6.5	€	1.7	1.8	2012	1.6	1.7
fixed	8.0	€	10.9	13.1	2020	10.7	13.2

The stated fair values were calculated on the basis of interest rates valid at December 31, 2004 for the respective maturities and redemption structures.

(18)
Income tax liabilities

Income tax liabilities *€ million*

	2003	**2004**
Deferred taxes	5.8	4.8
Current income taxes	24.2	30.3
	30.0	**35.1**

For temporary differences in the case of shares held in subsidiaries and associated companies amounting to €2.4 million, no deferred tax liabilities are reported, since the reverse effect can be controlled, and neither a disbursement nor a sale of the companies is likely within the foreseeable future.

The deferred tax assets and liabilities refer to the following:

Composition of deferred tax assets and liabilities *€ million*

	2003 assets	2003 liabilities	**2004** assets	**2004** liabilities
Loss carryforwards and tax credits	12.7	0.0	16.0	0.0
Tangible and intangible assets	9.4	(37.2)	2.6	(19.2)
Pension accruals	20.3	(0.5)	15.6	(0.5)
Other accruals [1]	13.3	0.0	12.1	(0.3)
Liabilities	19.1	(18.8)	1.3	(0.7)
Sundry	19.8	(9.5)	6.4	(1.7)
Subtotal	94.6	(66.0)	53.8	(22.4)
Offset	(60.2)	60.2	(17.6)	17.6
Consolidated balance sheet	**34.4**	**(5.8)**	**36.2**	**(4.8)**

[1] *of which (€0.3 million) carried as liabilities, but not affecting the income statement*

(19)
Deferred income

Deferred income *€ million*

	12/31/ 2003	of which >1 year	**12/31/ 2004**	of which >1 year
Customer grants	3.4	2.0	5.4	0.0
Public grants and subsidies	3.4	1.2	2.8	1.7
Other	1.2	0.9	0.1	0.0
	8.0	**4.1**	**8.3**	**1.7**

Notes
to the Consolidated income statement

(20)
Net sales

For a breakdown of the net sales of €1,940.8 million (up from €1,884.2 million in 2003) by divisions and regions, please see the segment reports.

(21)
Net inventory changes, other work and material capitalized

Net inventory changes, other work and material capitalized *€ million*

	2003	2004
Change in inventories of finished products and work in process	3.9	13.4
Other work and material capitalized	13.3	12.4
	17.2	**25.8**

(22)
Other operating income

Other operating income *€ million*

	2003	2004
Income from the disposal of plant and equipment	13.6	4.3
Income from the release of accruals	6.1	8.6
Income from investment grants and subsidies	4.1	4.7
Income from credit notes for prior periods	3.6	5.2
Income from customer reimbursements	8.5	5.8
Income from the reimbursement for prototypes and tools	6.0	7.2
Income from the sale of leftover material	1.4	3.0
Income from services	2.1	0.0
Income from the payment of bad debts charged off and the reversal of bad-debt allowances	2.1	1.9
Rental income	3.7	3.5
Income from damages/claims	0.9	0.6
Other income	10.6	7.5
	62.7	**52.3**

(23)
Cost of materials

Cost of materials *€ million*

	2003	2004
Cost of raw materials, supplies, and merchandise purchased	888.8	922.1
Cost of services purchased	81.8	88.5
	970.6	**1,010.6**

The Group's cost of materials decreased in 2004 as inventories were written up at €2.6 million (2003: €2.2 million).

(24)
Personnel expenses

Personnel expenses *€ million*	2003	**2004**
Wages and salaries	413.8	415.9
Social security contributions	71.0	71.9
Expenses for pensions and related employee benefits	30.4	33.0
	515.2	**520.8**

Pension expense primarily reflects the annual provision for accrued pension liabilities—cf. Note (15)—and the DCP contributions, as well as statutory pension contributions amounting to €24.9 million (2003: €24.5 million).

Annual average headcount

Annual average headcount	2003	**2004**
Pierburg	3,714	3,531
KS Pistons	5,530	5,563
KS Plain Bearings	1,006	1,010
KS Aluminum Technology	900	926
Motor Service	361	385
Other	34	38
	11,545	**11,453**

(25)
Amortization/depreciation/write-down

This encompasses amortization of other intangible and tangible assets. For a breakdown by amortization of intangible assets and depreciation of tangible assets, see the notes (6). During the period under review, special write-downs totaling €2.5 million were charged (2003: €6.2 million).

Notes
to the Consolidated income statement

(26)
Other operating expenses

Other operating expenses € million	2003	2004
Maintenance and repair	50.0	51.9
Data processing	24.2	26.9
Selling, promotion and advertising	24.0	23.3
Other general administration	15.1	17.2
Severance packages, termination benefits, pre-retirement part-time work	15.9	15.2
Rents	10.2	12.0
Other payroll incidentals	9.2	10.1
Legal and consultancy fees	10.2	9.1
Travel	8.8	8.8
Research and development	5.3	7.7
Non-income taxes	7.7	7.6
Insurances	7.1	6.6
Group allocations and service fees	5.8	5.8
Formation of other accruals	9.8	5.1
Outsourced support services	6.3	5.0
Project costs	2.3	4.3
Losses on fixed-asset disposal	1.0	3.1
Write-down of receivables	2.6	2.1
Warranties	7.1	2.0
Cleaning of Buildings	2.1	2.0
Physical security	1.7	1.8
Other expenses	16.4	15.6
	242.8	**243.2**

Income from the release of accruals was offset at €10.5 million (2003: €13.0 million) against other operating expenses.

(27)
Net interest expense

Net interest expense € million	2003	2004
Interest income		
return on plan assets	4.3	5.2
from long-term loans and financial receivables	0.2	0.1
other interest and similar income	2.9	2.1
	7.4	7.4
Interest expense		
from capital leases	(4.9)	(2.0)
compounding of pensions	(19.9)	(18.6)
compounding of other noncurrent accruals	(0.2)	(0.3)
other interest and similar expenses	(12.9)	(14.6)
	(37.9)	(35.5)
	(30.5)	**(28.1)**

(28)
Net investment income and other financial results

Net investment income and other financial results *€ million*

	2003	2004
Net investment income		
from joint ventures	7.6	6.5
from associated affiliates	0.0	8.5
	7.6	15.0
Other financial results		
from foreign exchange	(3.1)	(0.2)
from financial derivatives	0.5	1.8
Other financial expenses/income, net	(1.4)	(0.2)
	(4.0)	1.4
	3.6	**16.4**

The other financial results from foreign exchange includes €0.1 million (2003: €0.2 million), the loss from consolidating the Turkish subsidiary's annual accounts according to the rules for hyperinflationary economies.

(29)
Income taxes

Income taxes *€ million*

	2003	2004
Actual income tax expenses	28.9	30.5
Tax expenses not relating to the period	0.6	4.8
Deferred tax income	(0.1)	(3.9)
	29.4	**31.4**

The table below reconciles the expected to the recognized tax expense, which is determined by multiplying EBT by an unchanged tax rate of 40 percent. This tax expense comprises German corporate income tax, the solidarity surtax thereon, and municipal trade tax. Expected tax expenses are matched against the effective income tax burden.

Notes
to the Consolidated income statement

Reconciliation of expected to effective tax expenses *€ million*	2003	2004
EBT	72.6	110.8
Expected tax expense	**29.0**	**44.3**
Differences from German tax rates	(0.2)	0.3
Differences from foreign tax rates	(4.8)	(2.8)
Effects from loss carryovers and changes in provisions [1]	6.4	(10.3)
Tax-exempt income and nondeductible expenses	(0.7)	(6.0)
Nondeductible goodwill amortization	1.5	0.5
Adjustment for non-period income taxes	0.6	4.8
Reduction of deferred taxes due to tax rate change	0.3	0.1
Joint ventures and associated affiliates reported at equity	(2.8)	0.1
Other	0.1	0.4
Effective tax exense	**29.4**	**31.4**
Effective tax rate in %	40	28
Expected tax rate in %	40	40

[1] *of which a €4.2 million (2003: €0.0 million) reduction in actual tax expenses due to utilization of loss carryovers not previously applied.*

(30)
Minority interests

Minority interests in profit came to €1.3 million (2003: €0.9 million) and in loss to €0.0 million (down from €0.1 million).

(31)
Earnings per share (EpS)

EpS is obtained by dividing the weighted average number of shares issued and outstanding in the fiscal year into the Group's earnings. Neither at December 31, 2004 nor December 31, 2003 were any shares outstanding that could dilute earnings per share. Therefore, both in the year under review and the previous year, the undiluted EPS equals the diluted EPS.

Earnings per share (EpS)	2003	2004
Group earnings (after minority interests) €	42,398,238	78,079,571
Weight average number of shares	28,003,395	28,003,395
Earnings per share (EpS) €	1.51	2.79

The weighted average of the shares corresponds to the overall number shares, since there was no change in the number of shares in circulation.

Note
to the consolidated statement of cash flows

(32)
Cash flow statement

The cash flow statement conforms to IAS 7 and breaks down into the cash flows generated by operating, investing and financing activities. The effects of changes in the consolidation group are eliminated but they and parity changes, if impacting on cash & cash equivalents, are shown in separate lines.

Starting from the beginning-of-period (BoP) balance of cash & cash equivalents, this statement shows a cash flow above the previous year's level, amounting to €188.1 million, and net cash provided by operating activities of €221.9 million, representing a €47.5 million increase in cash inflow.

The net cash used in investing activities declined by €4.5 million to €102.0 million. The cash inflow derived from the disposal of tangible assets. The cash outflow from capital expenditure in the divisions relates to the acquisition of the engine parts activities of the companies E. Trost GmbH & Co. KG of Stuttgart, PV Autoteile GmbH of Duisburg, and Willy Konczewski GmbH & Co. KG of Berlin by MSD Motor Service Deutschland GmbH of Neckarsulm, which took over their assets and liabilities. Contained in the disinvestments of financial assets are the dividends of the associated companies and participations amounting to €6.6 million (2003: €1.7 million); the purchasing price from the sale of the interest in Pierburg Instrument GmbH of Neuss, as well as repayments from loans.

As a result from repaying financial debts and paying dividends, the net cash used in financing activities came to €94.2 million for the period under review (2003: €69.5 million).

Note
to the segment reports

(33)
Segment reports

In accordance with the Kolbenschmidt Pierburg Group's internal controlling organization, the Group breaks down into five primary divisions, viz.:

– Air Supply, Emission Controls and Pumps
– Large and Small Pistons
– Plain Bearings and Continuous Casting
– Aluminum Engine Blocks
– Aftermarket

The "Others/Consolidation" column includes, apart from the Group's parent (Kolbenschmidt Pierburg AG), further companies not allocable to any defined segment, including property companies and consolidations. It should be noted that, in 2004, the complete transfer of overhead costs of the holding companies is shown in the division results for the first time.

Responsibilities are clearly separated between the segments and Kolbenschmidt Pierburg AG, which performs the functions of a strategic management holding company. The management of the company and its internal reporting procedures have been structured accordingly. The companies belonging in each segment/division are listed on pages 90/91. In line with the Kolbenschmidt Pierburg Group's shareholder value concept, segment assets comprise the essential assets excluding cash & cash equivalents and income tax assets, while segment liabilities exclude financial debts and income tax liabilities. Net financial liabilities are contained in financial liabilities, minus cash and cash equivalents.

Capital employed (CE) is the sum total of equity (including minority interests), pension accruals, encompassing the net assets used to determine EBIT. The return on capital employed (ROCE) equals EBIT divided into average capital employed (average of the balances at December 31, 2003 and December 31, 2004.

The intersegment transfers principally indicate sales among divisions and are priced as if at arm's length.

EBITDA means earnings before interest, income taxes, depreciation and amortization on tangible and intangible assets. EBIT refers to earnings before interest and income taxes. The EBIT margin is defined as EBIT in relation to segment sales.

Capital expenditures and amortization/depreciation refer to tangible and intangible assets.

Additional notes

(34)
Contingent liabilities

Since 1998, a court of arbitration has been examining the appropriateness of the conversion ratio calculated with regard to the merger of Kolbenschmidt Pierburg (Rheinmetall participations). On the basis of preliminary figures, the expert appointed by the Heilbronn District Court has now submitted an interim report in 2003 that arrives at significantly deviating estimates of the worth of the two companies, which merged in January 1998. Kolbenschmidt Pierburg AG, however, after having read and considered this interim report, as well as the report by the expert of mergers, sees no grounds for distancing itself from the originally calculated value comparisons. At the time of the merger of the two companies, these value comparisons were calculated by two independent accounting companies and confirmed by a court-appointed merger and acquisitions expert. Kolbenschmidt Pierburg assumes that the value estimates, which were documented by three different experts, will be vindicated in the final ruling. So as not to prejudice the outcome of this process, we will desist from commenting further on this matter.

(35)
Other financial obligations

At December 31, 2004, the commitments to purchase tangible assets totaled €22.7 million (2003: €3.1 million), chiefly relating to orders of tangible assets. There were no purchasing price commitments in fiscal 2004 (2003: €7.9 million).

In succeeding years, the following disbursements for operating leases will be made:

The rents for land and buildings chiefly refer to a long-term property lease that neither includes a purchase option nor a firmly agreed passage of title and, therefore, is an operating lease.

In the year under review, €11.9 million (2003: €9.7 million) was paid under operating leases and recognized in net income. No subleases existed.

Rents in subsequent years – Finance leasing *€ million*

	2003			**2004**		
	2004	2005–2008	after 2008	2005	2006–2009	after 2009
Buildings	1.8	5.1	18.7	3.3	6.7	18.4
Production plant and machinery	1.5	1.9	0.0	1.9	3.7	0.0
Other leases	2.1	2.5	0.0	0.8	1.3	0.0
	5.4	9.5	18.7	6.0	11.7	18.4

(36)
Significant subsequent events

After the balance sheet date, KS Kolbenschmidt GmbH of Neckarsulm, the lead company of the KS Pistons division, increased its stake in the company Shriram Pistons & Rings Ltd. of India, held as securities under financial assets.

(37)
Stock Appreciation Rights (SAR)

During the period 1998 to 2001, the Kolbenschmidt Pierburg Group granted SARs to selected managerial staff, enabling them to participate in any stock appreciation. SAR-programs are basically phantom stock option plans under which participants receive a cash compensation upon exercise that equals the difference between the stock price at exercise date and the base (reference) price. The base price has been fixed at the arithmetic mean of the closing prices quoted on the 10 market days preceding plan commencement.

The SAR-program has an overall term of seven years: after a three-year qualifying period, SARs may be exercised during defined time windows during the residual four-year term. If not exercised during such period or when eligible staff leave the company for any reason other than retirement or death, the SARs become forfeited and lapse. SARs cannot be exercised unless and until the base price has been exceeded by 25 percent or more on the day of exercise.

Additional notes

Key parameters of the SAR-programs launched to date:

SAR-Program

SAR-Program	Exercisable until	Baseprice €	Number issued	of which settled/ exercised by 12/31/2003	of which forfeited in 2004	of which settled/ exercised in 2004	SAR as of **12/31/2004**
Executive Board							
2000	end-2003	11.22	60,000	40,000	0	20,000	0
2001	end-2004	14.19	50,000	30,000	0	0	20,000
							20,000

Obligations under SARs are fair-valued pro rata temporis by using an option price model. An accrual of €0.4 million (up from €0.3 million) provides for the obligations incurred up to December 31. 2004.

(38)
Hedging policy and financial derivatives

The operations and financial transactions of Kolbenschmidt Pierburg as an international group are exposed to financial risks, mainly from exchange rate volatility and interest rate changes. In accordance with the groupwide implemented risk management system of Kolbenschmidt Pierburg AG, such risks are not only identified, analyzed and measured but also managed through derivative financial instruments. No such derivatives may be acquired for speculation. Counterparties of Kolbenschmidt Pierburg Group companies for contracting financial derivatives are exclusively German and foreign banks of prime standing. By setting these high standards on counterparties the risk of uncollectible debts is minimized. All transactions involving financial derivatives are subject to stringent monitoring, which is particularly ensured by the strict segregation of the contracting. settlement and control functions.

Liquidity risk
The Kolbenschmidt Pierburg Group ensures sufficient liquidity at all times mainly through a liquidity forecast based on a fixed planning horizon as well as through existing, yet unutilized credit facilities.

Default risk
The Kolbenschmidt Pierburg Group primarily supplies customers of top standing meaning that bad debts or uncollectibles are extremely rare. Furthermore, lending guidelines exist which further reduce the risk of charge-offs. A dequate allowances have been made where this is a known risk of non-payment. Moreover, the Kolbenschmidt Pierburg Group has no significant loan concentration.

The default risk emanating from financial derivatives consists in a failure of the counterparty and is therefore limited to the instrument's positive fair value to the counterparty. Kolbenschmidt Pierburg companies contract financial derivatives solely with German and foreign banks of impeccable standing, thus minimizing default risks.

Raw materials price risk
Volatile prices for purchasing raw materials constitute a price risk for the Kolbenschmidt Pierburg Group. Thanks to a series of material price escalation agreements with customers, the risk from rising, but also the advantage of falling, metal prices has been largely shifted to the customers. For other metals for which agreements of this type could not be concluded, the use of long-term possibilities for procurement via suppliers is currently being investigated, as is the use of other instruments.

Currency risk
Due to the international nature of the Kolbenschmidt Pierburg Group's business, certain operational currency risks arise from the fluctuating parity of the euro to other currencies. Open positions exposed to a currency risk are principally hedged through financial derivatives, generally currency forwards or futures.

These hedges are contracted by the foreign subsidiaries on a decentralized basis.

In Germany the Kolbenschmidt Pierburg Group benefits to a large extent from a natural hedge. Remaining open currency positions, particularly in US dollars are hedged in additional currency forward transactions. All intercompany financing transactions are hedged by currency swaps. The lower limit of the hedging ratio amounts to 75 percent.

Interest rate risk
The Kolbenschmidt Pierburg Group's financing activities also use such funding tools as floating-rate facilities. Interest rate hedges such as caps/floors/collars and interest rate swaps contain the risks ensuing from market rate changes. These interest rate options are used to redesign variable-rate into fixed-rate agreements. These hedges are contracted centrally by Kolbenschmidt Pierburg AG, as well as by the individual divisions on a decentralized basis.

Participation in the ABS program of the Rheinmetall Group results in a risk of interest rate change. In order to limit this risk, interest rate caps (among other instruments) are employed. Currently, roughly half of these risks are covered; however, the ratio can vary depending on the volume of receivables sold.

As of December 31, 2004, the currency and interest rate hedges tabled below existed, their notional volumes being shown non-netted and thus reflecting the total amounts of all individual contracts. Being marked to the market at December 31, the fair values of financial derivatives correspond to prices in arm's length transactions.

Financial derivatives *€ million*

	Notional volume		Maturing after	Fair market values	
	12/31/2003	**12/31/2004**	(in months)	12/31/2003	**12/31/2004**
Currency hedges					
Currency forwards/futures	68.9	99.3	29	1.9	0.9
Interest rate hedges					
Swaps	10.3	11.4	57	(0.7)	1.4
Other derivatives	25.0	60.0	65	0.0	0.4

(39)
Related-party transactions

The subsidiaries consolidated by Kolbenschmidt Pierburg AG directly or indirectly maintain ordinary business relations with many non-consolidated group companies, as well as associated affiliates and joint ventures. Any and all trade transactions conducted in the scope of ordinary day-to-day business with unconsolidated related companies conform to the arm's length principle.

In addition, Rheinmetall AG as Kolbenschmidt Pierburg AG's majority stockholder as well as Rheinmetall service companies provide extensive services to companies of the Kolbenschmidt Pierburg Group, including (for example) legal, tax, and PR consultancy and support, and insurance services.

As apart of the cash management system of majority stockholder Rheinmetall AG, the Kolbenschmidt Pierburg Group invests and/or borrows cash & cash equivalents within the Rheinmetall Group. All cash management business is transacted as if at arm's length.

Additional notes

Volume of services provided to and/or by related companies:

Details of service transactions with related companies *€ million*

	Volume of services rendered		Volume of services utilized	
	2003	**2004**	2003	**2004**
Rheinmetall AG	0.0	0.0	5.2	5.7
Rheinmetall Service Gesellschaft mbH	0.0	0.0	0.4	0.5
Rheinmetall DeTec AG	0.0	0.0	0.0	0.2
Pierburg Instruments GmbH	1.0	0.0	0.4	0.0
Kolbenschmidt Shanghai Piston Co., Ltd.	0.4	2.0	1.7	1.6
Kolbenschmidt Pierburg Shanghai Nonferrous Components Co., Ltd.	0.6	1.1	0.0	0.2

(40)
Executive and Supervisory Boards

Executive Board
For their duties performed on behalf of the parent company and its subsidiaries, the Executive Board members received fixed remuneration €0.9 million (2003: €0.9 million), and €1.5 million in profit shares (2003: €2.1 million). Former members of the Executive Board still held 20,000 shares of phantom stock from the SAR program in 2001. Additional information concerning the SARS program can be found in Note (37) of this annual report. In addition, as a replacement for the terminated SAR program, a new incentive program has been instituted, which is oriented to the absolute increase in value of the Rheinmetall Group, with €0.4 million in bonus payments being disbursed in 2004. In addition, members of the Executive Board received compensation in kind worth €0.1 million, substantially in the form of company car privileges and grants for social security insurance.

In fiscal 2004, members of the Executive Board received compensation totaling €2.9 million (2003: 3.6 million).

Pensions paid to former members of the Executive Board and their survivors totaled €0.4 million (2003: €0.4 million) payments. Pension accruals for former members of the Executive Board and their survivors amounted to €5.2 million (2003: €5.1 million).

Supervisory Board
Supervisory Board fees amounted to €0.2 million in fiscal 2004 (2003: €0.2 million). No further compensation paid, nor were any benefits granted, to Supervisory Board members for personally rendered advisory or agency services in the year under review.

Shareholdings
As of December 31, 2004, none of Kolbenschmidt Pierburg AG's Supervisory or Executive Board members held any shares in the company.

(41)
Corporate Governance

Since January 2005, Kolbenschmidt Pierburg AG, pursuant to Art. 161 AktG, has published a declaration of conformity to the German Corporate Governance Code on the Internet at www.kolbenschmidt-pierburg.com, thus making it available to its stockholders.

Regarding the consolidated financial statements of Rheinmetall AG, a declaration of conformity under the terms of Art. 161 AktG has been published since December 2002 on the Internet at www.rheinmetall.de.

Düsseldorf, February 25, 2005

The Executive Board
Dr. Kleinert Dr. Merten Dr. Friedrich

Auditor's report and opinion

Kolbenschmidt Pierburg AG, Düsseldorf

Independent group auditor's report and opinion

We have audited the consolidated financial statements of Kolbenschmidt Pierburg Aktiengesellschaft, Düsseldorf, consisting of the balance sheet, the income statement and the statements of changes in equity and cash flows as well as the notes to the financial statements for the business year from January 1. to December 31, 2004. The preparation and the content of the consolidated financial statements according to the International Financial Reporting Standards of the IASB (IFRS) are the responsibility of the Company's Board of Managing Directors. Our responsibility is to express an opinion, based on our audit, whether the consolidated financial statements are in accordance with IFRS.

We conducted our audit of the consolidated financial statements in accordance with German auditing regulations and generally accepted standards for the audit of financial statements promulgated by the Institut der Wirtschaftsprüfer in Deutschland (IDW). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatements. Knowledge of the business activities and the economic and legal environment of the Group and evaluations of possible misstatements are taken into account in the determination of audit procedures. The evidence supporting the amounts and disclosures in the consolidated financial statements are examined on a test basis within the framework of the audit. The audit includes assessing the accounting principles used and significant estimates made by the Board of Managing Directors, as well as evaluating the overall presentation of the consolidated financial statements. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements give a true and fair view of the net assets, financial position, results of operations and cash flows of the Kolbenschmidt Pierburg Group for the business year in accordance with IFRS.

Our audit, which also extends to the group management report prepared by the Board of Managing Directors for the business year from January 1. to December 31, 2004, has not led to any reservations. In our opinion, on the whole the group management report, together with the other information of the consolidated financial statements, provides a suitable understanding of the Group's position and suitably presents the risks of future development. In addition, we confirm that the consolidated financial statements and the group management report for the business year from January 1. to December 31, 2004 satisfy the conditions required for the Company's exemption from its duty to prepare consolidated financial statements and the group management report in accordance with German accounting law.

Stuttgart, February 28, 2005

PwC Deutsche Revision
Aktiengesellschaft
Wirtschaftsprüfungsgesellschaft

Staudacher	Adamaszek
German Public Auditor	German Public Auditor

Group of consolidated companies at December 31, 2004

Group of consolidated companies at December 31, 2004

			IFRS Equity	Interest held (%) direct	indirect
	Kolbenschmidt Pierburg AG, Düsseldorf	€	331,324,036		
	Pierburg				
1	Pierburg GmbH, Neuss	€	112,384,098	100	
	Carbureibar S.A., Abadiano/Spain	€	29,913,586		100
	Pierburg S.à r.l., Basse-Ham (Thionville)/France	€	27,324,055		100
	Pierburg Inc., Fountain Inn (Greenville)/USA	*US$*	11,742,455		100
	Pierburg do Brasil Ind. e Comercio Ltda., Nova Odessa/Brazil	*Rs*	12,862,230		100
	Pierburg S.p.A., Lanciano/Italy	€	19,081,483		100
	Société Mosellane de Services S.C.I., Basse-Ham (Thionville)/France	€	10,174,010		100
2	Kolbenschmidt Pierburg Shanghai Nonferrous Components Co. Ltd., Shanghai/China	*Yuan*	237,397,021		50
3	Calor Grundstücksverwaltungsgesellschaft mbH & Co. KG, Grünwald	€	(1,962,824)		94
	Pierburg s.r.o., Usti, Czech Republic	*Čk*	(9,887,670)		100
	KS Pistons				
1	KS Kolbenschmidt GmbH, Neckarsulm	€	179,014,005	100	
	KS Pistões Ltda., Nova Odessa/Brazil	*Rs*	162,967,069		100
	KS International Investment Corp., Southfield/USA	*US$*	158,785,695		100
	Karl Schmidt Unisia Inc., Marinette/USA	*US$*	21,831,284		92
	KS Large Bore Pistons Inc., Marinette/USA	*US$*	6,216,961		100
	KUS Canada Inc., Leamington/Canada	*Can$*	9,886,977		92
	KS France S.A.S., Basse-Ham (Thionville)/France	€	18,070,134		100
	Société Mosellane de Pistons S.A.S., Basse-Ham (Thionville)/France	€	22,191,033		100
	Metal a.s., Usti/Czech Republic	*Čk*	678,094,000		95
2	Kolbenschmidt Shanghai Piston Co. Ltd., Shanghai/China	*Yuan*	237,152,832		50
3	Tiro Grundstücks-Verwaltungsgesellschaft mbH & Co. KG, Grünwald	€	(242,713)		0
	Kolbenschmidt K.K., Yokohama/Japan	¥	1,174,607,788		100
	KS Plain Bearings				
1	KS Gleitlager GmbH, St. Leon-Rot	€	19,659,952	100	
	KS Bearings Inc., Fountain Inn (Greenville)/USA	*US$*	(18,570,169)		100
	KS Bronzinas Ltda., Nova Odessa/Brazil	*Rs*	16,292,728		100
	KS Aluminum Technology				
1	KS ATAG GmbH, Neckarsulm	€	25,231,355	100	
1	KS Aluminium-Technologie AG, Neckarsulm	€	19,958,712		100
4	Werkzeugbau Walldürn GmbH, Walldürn	€	552,377		100
	KS Doehler-Jarvis GmbH, Neckarsulm	€	1,251,948		65
	KS Aluminium Beteiligungs-GmbH, Neckarsulm	€	(136,633)		100

			IFRS Equity	Interest held (%) direct	indirect
	Motor Service				
1	MSI Motor Service International GmbH, Neckarsulm	€	19,791,824	100	
	G. Krull GmbH, Neckarsulm	€	40,799		100
4	MSD Motor Service Deutschland GmbH, Neckarsulm	€	1,718,576		100
	KS Motorac S.A.S., Le Blanc Mesnil/France	€	2,960,051		100
	KS Winston Ltd., i.L. Purfleet/Great Britain	£	42,745		100
	Kolbenschmidt Istanbul Dis Ticaret ve Pazarlama A.S., Istanbul/Turkey	TL	7,039,856,607,000		51
	KS Produtos Automotivos Ltda., Nova Odessa/Brazil	Rs	16,086,981		92
	KS Motor Servis CZ s.r.o., Trmice/Czech Republic	Čk	14,608,944		66
3	Litos Grundstücks-Verwaltungsgesellschaft mbH & Co. KG, Grünwald	€	(501,560)		0
	Other				
	Kolbenschmidt Liegenschaftsverwaltung GmbH Berlin, Berlin	€	6,748,641	100	
	KS Grundstücksverwaltung Beteiligungs-GmbH, Neckarsulm	€	34,462	100	
	KS Grundstücksverwaltung GmbH & Co. KG, Neckarsulm	€	9,417,224		100
	GVN Grundstücksverwaltung Neuenstadt GmbH & Co. KG, Neckarsulm	€	73,723		100

1 *P&L transfer agreement with Kolbenschmidt Pierburg AG, application of the exemption clause under § 264 art 3 HGB*
2 *Included at equity*
3 *Special-purpose entity*
4 *Profit pooling agreement with controlling company of the division, application of the exemption clause under § 264 art 3 HGB*

Balance Sheet of Kolbenschmidt Pierburg AG as of December 31, 2004 (based on HGB)

Assets *€ million*	**12/31/2003**	**12/31/2004**
Assets		
Tangible assets	0.1	0.1
Financial assets	327.3	356.0
	327.4	**356.1**
Current assets		
Receivables and sundry assets		
Due from Group companies	77.6	114.2
Sundry assets	3.7	1.6
Cash & cash equivalents	16.1	32.1
	97.4	**147.9**
Prepaid expenses & deferred charges	0.1	0.1
Total assets	**424.9**	**504.1**

Equity & liabilities *€ million*	**12/31/2003**	**12/31/2004**
Equity & Liabilities		
Stockholders' equity	71.7	71.7
Capital stock	174.0	174.0
Reserves retained from earnings	27.4	56.9
Net earnings	14.0	29.5
	287.1	**332.1**
Untaxed/special reserves	**0.0**	**0.0**
Accruals		
Accruals for pensions and similar obligations	11.8	12.7
Other accruals	17.1	23.3
	28.9	**36.0**
Liabilities		
Due to banks	8.5	7.5
Trade payables	0.2	0.1
Due to Group companies	100.0	128,2
Sundry liabilities	0.2	0.2
	108.9	**136.0**
Total equity & liabilities	**424.9**	**504.1**

Income statement of Kolbenschmidt Pierburg AG for the year ended December 31, 2004 (based on HGB)

€ million	2003	2004
Income from investments	44.5	78.6
Net interest income	(2.6)	(3.0)
Net financial result	**41.9**	**75.6**
Other operating income	17.7	37.5
Personnel expenses	(9.0)	(12.3)
Amortization/depreciation/write-down	(0.1)	(0.1)
Other operating expenses	(22.2)	(25.9)
Earnings before taxes (EBT)	**28.3**	**74.8**
Income taxes	(9.3)	(15.8)
Net income	**19.0**	**59.0**
Transfer to reserves retained from earnings	(5.0)	(29.5)
Net earnings	**14.0**	**29.5**

*You can access the complete separate accounts of Kolbenschmidt-Pierburg AG (including the notes) at our website **www.kolbenschmidt-pierburg.com**, or by writing to us at Kolbenschmidt-Pierburg AG, Rheinmetall Allee 1, 40476 Düsseldorf.*

Supervisory and Executive Boards
Membership in other supervisory and comparable boards

Supervisory Board

Klaus Eberhardt
Düsseldorf

Chairman

Chairman of the Executive Board
Rheinmetall AG, Düsseldorf

Member of further supervisory boards:

Rheinmetall Defence Electronics GmbH, Bremen
(from March 1, 2004, Chairman from March 16, 2004)

Rheinmetall DeTec AG, Ratingen
(Chairman, until February 29, 2004)

Rheinmetall Landsysteme GmbH, Kiel
(from March 1, 2004, Chairman from August 3, 2004)

Rheinmetall W&M GmbH, Unterlüss
(March 1, 2004 to May 11, 2004)

Rheinmetall Waffe und Munition GmbH, Ratingen
(from November 4, 2004, Chairman from December 2, 2004)

Oerlikon Contraves AG, Zurich, Switzerland
(from March 26, 2004,
President of the Administrative Board from March 27, 2004)

Nitrochemie AG, Wimmis, Switzerland
(President, from March 24, 2004)

Nitrochemie Wimmis AG, Wimmis, Switzerland
(President, from March 24, 2004)

Dr. Rudolf Luz *
Weinsberg

Vice-Chairman

1st Delegate of the German Metalworkers Union ("IG Metall"),
Heilbronn/Neckarsulm office, Neckarsulm

Member of further supervisory boards:

Rheinmetall AG, Düsseldorf
(from June 1, 2004)

Bechtle AG, Neckarsulm
(Member of the supervisory board)

Member of a further German and foreign supervisory board:

Wirtschaftsfördergesellschaft Raum Heilbronn GmbH, Heilbronn
(Member of the supervisory board)

Dr. Andreas Beyer
Sindelfingen

Director with general power to represent the company
Rheinmetall AG, Düsseldorf

Member of further supervisory boards:

Pierburg GmbH, Neuss

Jagenberg AG, Neuss

Bachofen + Meier AG, Bülach, Switzerland

Dr. Herbert Müller
Essen

Member of the Executive Board
Rheinmetall AG, Düsseldorf
Finance

Member of a further supervisory board:

Rheinmetall DeTec AG, Ratingen

Dr. Bernd M. Hönle
Weisenheim a.S.

Managing Director
Röchling Industrie Verwaltung GmbH, Mannheim

Member of further supervisory boards:

Rheinmetall AG, Düsseldorf

Rheinmetall DeTec AG, Ratingen

BEA Holding AG, Düsseldorf

DeTeWe - Deutsche Telephonwerke Beteiligungs AG, Berlin

Francotyp-Postalia Beteiligungs AG, Birkenwerder

PFEIFFER & MAY Großhandel AG, Karlsruhe

Seeber Beteiligungs AG, Mannheim

* Staff representative

Burkhard Leffers
Bad Homburg v.d.H

Member of the Regional Executive Board
Commerzbank AG

Member of further supervisory boards:

AFFINE S.A., Paris, France
(Membre du Conseil d'Administration)

Goodyear Dunlop Tires Germany GmbH, Hanau
(Member of the supervisory board from January 1, 2004)

Prof. Dr. Dirk Zumkeller
Munich,

Full Professor of Transport & Traffic
Technical University of Karlsruhe

Member of a further supervisory board:

Rheinmetall AG, Düsseldorf

Dr. Ludwig Dammer *
Düsseldorf

Pierburg GmbH, Neuss

Member of a further supervisory board:

Rheinmetall AG, Düsseldorf

Heinrich Kmett *
Fahrenbach/Robern

Works Council Chairman
KS Kolbenschmidt GmbH, Neckarsulm

Member of a further supervisory board:

Rheinmetall AG, Düsseldorf

Erich Hüskes *
Nettetal

Member of the Works Council
Nettetal plant of Pierburg GmbH, Neuss

Dietrich Termöhlen *
Hinte

1st Delegate of IG Metall
Neuss Office

Member of further supervisory boards:

Aluminium Norf GmbH, Neuss

Pierburg GmbH, Neuss (Deputy chairman)

Gerhard Grasmeier *
Waghäusel

Chairmain of the Works Council of the St. Leon-Rot plant
of KS Gleitlager GmbH, St. Leon-Rot

Member of a further supervisory board:

KS Gleitlager GmbH, St. Leon-Rot

Supervisory and Executive Boards
Membership in other supervisory and comparable boards

Executive Board of Kolbenschmidt Pierburg AG 2004

Dr. Gerd Kleinert
Gottmadingen

Chairman
Strategy, Marketing, Operations

Member of the following supervisory boards:

Pierburg GmbH, Neuss
(Chairman)

KS Kolbenschmidt GmbH, Neckarsulm
(Chairman)

KS Gleitlager GmbH, St. Leon-Rot
(Chairman)

KS Aluminium-Technologie AG, Neckarsulm
(Chairman)

KS ATAG GmbH, Neckarsulm
(from March 22, 2004, Chairman from November 08, 2004)

Läpple AG, Heilbronn
(Member of the supervisory board, from December 10, 2004)

Läpple Holding AG, Heilbronn
(Member of the supervisory board, from December 10, 2004)

Member of the following comparable German and foreign supervisory boards:

KS International Investment Corp., Southfield, USA

Kolbenschmidt Pierburg Shanghai Nonferrous Components Co. Ltd, Shanghai, China (KPSNC)
(Vice Chairman)

KS Pistons Shanghai Co. Ltd, Shanghai, China (KSSP)
(from March 22, 2004)

Dr. Peter P. Merten
Herrsching

Finance/Controlling, IT

Member of the following supervisory board:

Pierburg GmbH, Neuss

KS Kolbenschmidt GmbH, Neckarsulm

KS Gleitlager GmbH, St. Leon-Rot

KS Aluminium-Technologie AG, Neckarsulm

KS ATAG GmbH, Neckarsulm
(from March 22, 2004)

Member of the following comparable German and foreign supervisory boards:

KS International Investment Corp., Southfield, USA

Dr. Jörg-Martin Friedrich
Ludwigsburg

Human Resources, Legal Affairs

Member of the following supervisory boards:

Pierburg GmbH, Neuss

KS Kolbenschmidt GmbH, Neckarsulm

KS Gleitlager GmbH, St. Leon-Rot

KS Aluminium-Technologie AG, Neckarsulm

KS ATAG GmbH, Neckarsulm
(from March 22, 2004)

Member of the following comparable German and foreign supervisory board:

KS International Investment Corp., Southfield, USA

List of addresses

Kolbenschmidt Pierburg AG

Kolbenschmidt Pierburg AG
Karl-Schmidt-Strasse
74172 Neckarsulm, Germany
Phone (+49-71 32) 33 0
Fax (+49-71 32) 33 28 89
www.kolbenschmidt-pierburg.com

Kolbenschmidt Pierburg AG
Rheinmetall Allee 1
40476 Düsseldorf, Germany
Phone (+49-2 11) 473 47 18
Fax (+49-2 11) 473 41 57
www.kolbenschmidt-pierburg.com

Pierburg division

Pierburg GmbH
Alfred-Pierburg-Strasse 1
41460 Neuss, Germany
Phone (+49-21 31) 52 01
Fax (+49-21 31) 52 06 45
info-airmanagement@kolbenschmidt-pierburg.com
info-pumps@kolbenschmidt-pierburg.com

KS Pistons division

KS Kolbenschmidt GmbH
Karl-Schmidt-Strasse
74172 Neckarsulm, Germany
Phone (+49-71 32) 33 0
Fax (+49-71 32) 33 27 96
info-pistons@kolbenschmidt-pierburg.com

KS Plain Bearings division

KS Gleitlager GmbH
Am Bahnhof 14
68789 St. Leon-Rot, Germany
Phone (+49-62 27) 56 0
Fax (+49-62 27) 56 302
info-bearings@kolbenschmidt-pierburg.com

KS Aluminum Technology division

KS Aluminium-Technologie AG
Hafenstrasse 25
74172 Neckarsulm, Germany
Phone (+49-71 32) 33 1
Fax (+49-71 32) 33 43 57
info-alucasting@kolbenschmidt-pierburg.com

Motor Service division

MSI Motor-Service International GmbH
Untere Neckarstrasse
74172 Neckarsulm, Germany
Phone (+49-71 32) 33 33 33
Fax (+49-71 32) 33 28 64
info@msi-motor-service.com

Imprint

© 2005
Kolbenschmidt Pierburg Aktiengesellschaft
Rheinmetall Allee 1
40476 Düsseldorf, Germany

Production
Schmitz-Design, Düsseldorf, Germany

Printer
Druckerei Dehl, Düsseldorf, Germany

Contacts

Corporate Communications Automotive
Folke Heyer
Telephone (+49-21 31) 520-30 10
Telefax (+49-21 31) 520-20 14
folke.heyer@kolbenschmidt-pierburg.com

Investor Relations
Franz-Bernd Reich
Telephone (+49-2 11) 4 73-47 77
Telefax (+49-2 11) 4 73-41 57
franz-bernd.reich@rheinmetall-ag.com

Copies of this annual report, which is also available in a German version, can be obtained by contacting the company; or can be downloaded at www.Kolbenschmidt-pierburg.com.

In cases of doubt, the German version takes precedence.

Kolbenschmidt Pierburg AG
Rheinmetall Allee 1
40476 Düsseldorf, Germany
Phone (+49-2 11) 473-47 18
Fax (+49-2 11) 473-41 57
www.kolbenschmidt-pierburg.com

KOLBENSCHMIDT
PIERBURG

Annual Report 2004 Kolbenschmidt Pierburg AG