www.gildemeister.com

ANNUAL REPORT 2005

Know.how.

GILDEMEISTER

COVER PICTURE:
Workpiece: steel mould making element used in the production of PET bottle bases (plastic industry), made on the DMC 64 V *linear* vertical machining centre

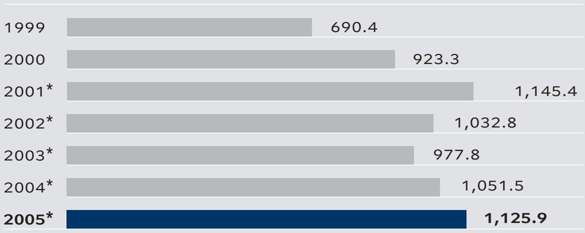
Key figures

The Consolidated Financial Statements of GILDEMEISTER Aktiengesellschaft for the year ended 31 December 2005 were prepared in accordance with the International Financial Reporting Standards (IFRS).

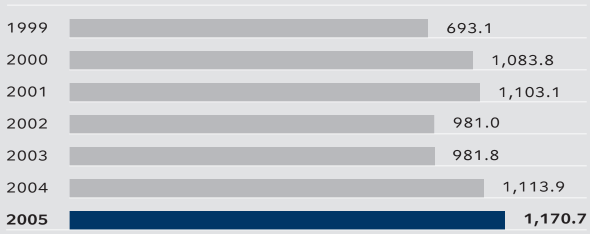
GILDEMEISTER group	2005	2004	Changes 2005 against 2004	
	€ M	€ M	€ M	%
Sales revenues				
Total	**1,125.9**	1,051.5	74.4	7
Domestic	**501.9**	502.9	-1.0	0
International	**624.0**	548.6	75.4	14
% International	**55**	52		
Order intake				
Total	**1,170.7**	1,113.9	56.8	5
Domestic	**520.7**	508.8	11.9	2
International	**650.0**	605.1	44.9	7
% International	**56**	54		
Order backlog*				
Total	**346.8**	321.8	25.0	8
Domestic	**129.3**	113.6	15.7	14
International	**217.5**	208.2	9.3	4
% International	**63**	65		
Investments	**26.8**	21.8	5.0	23
Personnel costs	**295.9**	282.5	13.4	5
Employees	**5,083**	4,984	99	2
plus trainees	**189**	190	-1	-1
Total employees*	**5,272**	5,174	98	2
EBITDA	**87.8**	71.2	16.6	
EBIT	**56.4**	41.9	14.5	
EBT	**25.4**	12.0	13.4	
Annual result	**13.5**	5.6	7.9	

* Reporting date 31 December

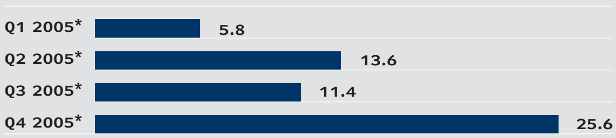
Sales revenues
in € million



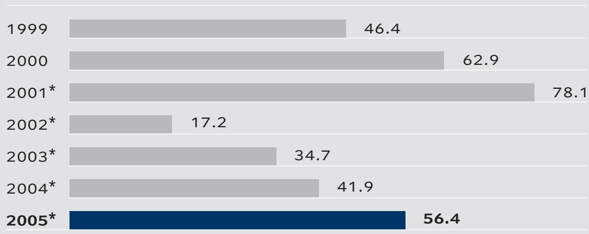
Order intake
in € million



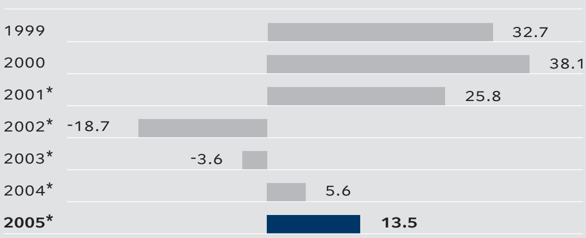
Quarterly results (EBIT)
in € million



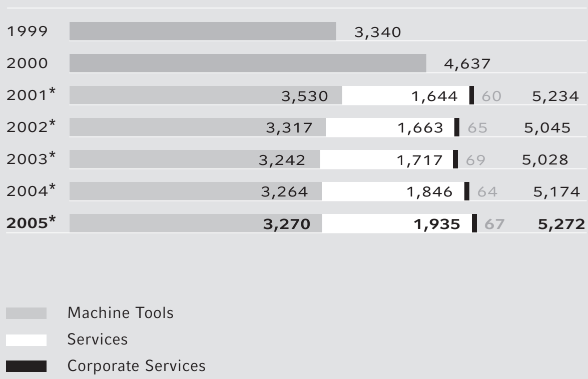
EBIT
in € million



Annual result
in € million



Number of Employees
incl. trainees



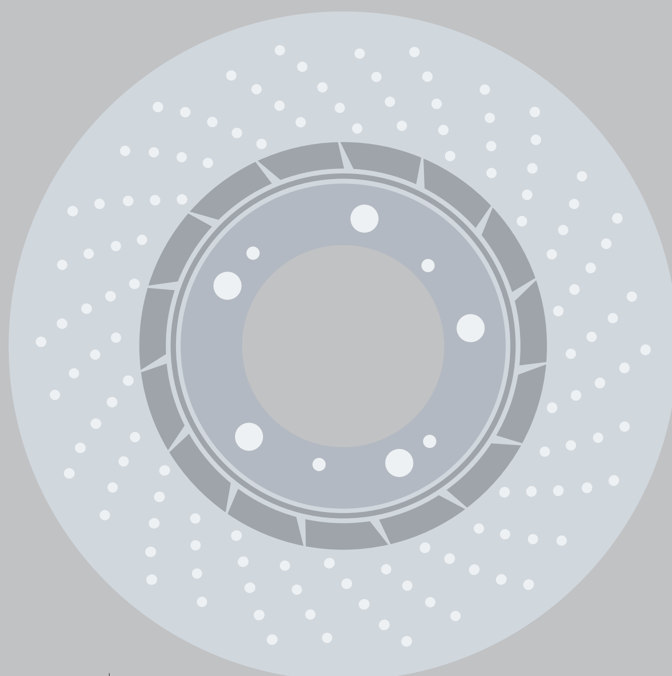
*in accordance with IFRS

Know.how.

Technology. Service. Performance.

At GILDEMEISTER the motto for 2006 is "technology, service and performance". In machine tool technology and the services area, GILDEMEISTER's know-how is unequalled in the industry. We combine our technology in the core competencies: "turning", "milling", "ultrasonic" and "laser". With our service know-how we develop service products for all aspects of the machine tool beyond its entire life-cycle. Our customers can rely on maximum quality, skilled services and state-of-the-art software products. Throughout the world from one source. Seven days a week, 24 hours a day. Our great power of innovation originates from this environment. Performance: Reinforcing our earning power and increasing the value of our company form the basis of our activities.


Know.how: With our expertise you will safely reach your
destination.



BRAKE DISK MADE
OF HARDENED STEEL

The production of a car is based on smooth processes, high accuracy and efficiency. An innovative concept and design point the way ahead. The automotive and component supplier industries therefore rely on GILDEMEISTER technology and use our complete machining solutions in many areas, such as the production of brake disks. So that you will always reach your destination safely. Maximum safety requires maximum expertise. We know how.

Know.how: Our expertise gets you into

shape.

SPINNING MOULD
FOR CHOCOLATE BUNNIES

No lasting quality without reliability and security; this principle applies particularly to food. The food processing industry therefore uses our expertise for its specific requirements in the flexible 5-sided-/5-axis machining area. All year round, but particularly in the seasonal trade. That's why GILDEMEISTER machines play a crucial part in getting chocolate bunnies into shape in time for Easter. Maximum quality requires maximum expertise. We know how.


Know.how: Our expertise lets you
smile.

TOOTH BRIDGE MADE OF SPECIAL CERAMICS (ZIRCONIUM OXIDE)

Precision and innovative technologies play a crucial role in the dental equipment industry. The specific properties of new materials require state-of-the-art machining technologies. The dental equipment industry therefore relies on the innovative ultrasonic technology of GILDEMEISTER. Our machines help you fulfil your hopes and so put a beaming smile on your face. Maximum precision requires maximum expertise. We know how.

GILDEMEISTER is the leading manufacturer of cutting machine tools worldwide. Our business includes the "Machine Tools" and the "Services" segments, along with the "Corporate Services" segment, which functions as the management holding company for the group. The "Machine Tools" segment covers the group's new machines business including the "turning", "milling", "ultrasonic" and "laser" technologies. GILDEMEISTER combines its expertise in development and technology at five product facilities with ten

Group Structure*

GILDEMEISTER Aktiengesellschaft
Bielefeld

Production Plants

GILDEMEISTER Drehmaschinen GmbH, Bielefeld

GILDEMEISTER Italiana S.p.A. Bergamo

GRAZIANO Tortona S.r.l.

DECKEL MAHO Pfronten GmbH

DECKEL MAHO Geretsried GmbH

DECKEL MAHO Seebach GmbH

FAMOT Pleszew S.A.

SAUER GmbH Idar-Oberstein, Kempten

DECKEL MAHO GILDEMEISTER (Shanghai) Machine Tools Co., Ltd.

Sales and Service organization

DMG Vertriebs und Service GmbH DECKEL MAHO GILDEMEISTER, Bielefeld

"Machine Tools"
"Services"

* Simplified organisational structure in accordance to lead management criteria (Reporting date: March 2006). The legal corporate structure is illustrated in the notes starting on page 154.

production sites. The “Services” segment is operated by DMG Vertriebs und Service GmbH and its subsidiaries. They offer services for all aspects of our machines across all areas. GILDEMEISTER is represented in 28 countries with 59 national and international sales and service sites. A total of 5,272 committed employees attend to our innovative machine technologies, excellent services and state-of-the-art software products. It is our principal aim to reinforce the earning power and to raise the value of our company.

DMG Deutschland Stuttgart	DMG Europe Klaus / Austria	DMG America Chicago	DMG Asia Shanghai	DMG Services Bielefeld, Pfronten
			DMG China	
DMG Stuttgart Vertriebs und Service GmbH	DMG Italia S.r.l. Bergamo, Tortona	DMG Chicago Inc. Chicago / Schaumburg	DMG Shanghai Co. Ltd. Shanghai	DMG Service Fräsen Pfronten Pfronten, Geretsried
DMG München Vertriebs und Service GmbH	DMG France S.a.r.l. Les Ulis, Lyon, Scionzier	DMG Charlotte Inc. Charlotte	DMG Beijing Sales Office Beijing	DMG Service Fräsen Seebach Seebach, Geretsried
DMG Hilden Vertriebs und Service GmbH	DMG Austria GmbH Klaus, Wiener Neudorf	DMG Los Angeles Inc. Los Angeles	DMG Guangdong Sales Office Guangdong	DMG Service Drehen GmbH Bielefeld
DMG Bielefeld Vertriebs und Service GmbH	DMG (Schweiz) AG Zürich / Dübendorf	DMG Canada Inc. Toronto	DMG Chongquing Sales Office Chongquing	DMG Trainings-Akademie GmbH Bielefeld, Pfronten, Stuttgart
DMG Berlin V. u. S. GmbH Berlin, Chemnitz	DMG Russland o.o.o. Moscow	DMG México S.A. de C.V. Monterrey	DMG Shenyang Sales Office Shenyang	DMG MICROSET GmbH Bielefeld
DMG Frankfurt Vertriebs und Service GmbH	DMG Czech s.r.o. Brno, Trenčin	DMG Brasil Ltda. São Paulo	DMG Xian Sales Office Xian	SACO S.p.A. Castelleone
	DMG Benelux Veenendaal, Zaventem		DMG Nippon K.K. Yokohama, Nagoya	a & f Stahl- und Maschinenbau Würzburg
	DMG (UK) Ltd. Luton		DMG Korea Ltd. Seoul	DMG Gebrauchtmaschinen Geretsried, Bielefeld, Zlin
	DMG Ibérica S.L. Barcelona, Bilbao		DMG India Pvt. Ltd. Bangalore, New Delhi	
	DMG Polska Sp.z.o.o. Pleszew		DMG Taiwan Ltd. Taichung	
	DMG Danmark Kvistgård		DMG Asia Pacific	
	DMG Istanbul Ltd. Istanbul		DMG Asia Pacific Pte. Ltd. Singapore	
			DMG Australia Pty. Ltd. Melbourne, Sydney	
			DMG Malaysia SDN BHD Kuala Lumpur	
			DMG (Thailand) Co. Ltd. Bangkok	
			DMG Vietnam Sales Office Hanoi	

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"Preserving traditional values"

The work of the Supervisory Board and its committees aims to permanently secure and cultivate GILDEMEISTER's success. We undertake to meet these aims with shareholders and investors and with our customers, employees and other business partners. What this means to us is that we preserve traditional values and manage the company in accordance with an exemplary Corporate Governance policy and modern principles.

Hans Henning Offen (65)
has been Chairman of the Supervisory Board since May 2004 and a member of it since 1994. Following master's degree in business administration (Dipl.-Kaufmann) at universities in Cologne and Hamburg, he started his career at the Citibank in Hamburg, New York and Frankfurt. In 1979 he became a member of the Executive Board at the Handelsbank in Lübeck AG and in 1985 spokesman for the Executive Board at the Deutsche Bank Asia AG. Both of these institutes are subsidiaries of the Deutsche Bank AG. In 1990, Offen was appointed member of the Executive Board at the Westdeutsche Landesbank Girozentrale and was Deputy Chairman of the Executive Board between 1992 and 2002.

In the past financial year, the Supervisory Board advised the Executive Board and supervised its management. It was therefore part of all the major decision-making processes. There were five meetings of the Supervisory Board in the reporting year. Together with the Executive Board, the Supervisory Board discussed issues of corporate planning and strategy, corporate policy, the course of business, risk status and risk management. The Executive Board also prepared written comprehensive and timely reports on all processes of particular importance and on the development of key financial indicators.

The main point on the agenda of the **annual accounts meeting** that took place on **29 March 2005** was the adoption of the Annual Consolidated Financial Statements, the Group Management Report, the Annual Financial Statements and the Management Report of GILDEMEISTER Aktiengesellschaft for the year ended 31 December 2004. The meeting was attended by twelve members of the Supervisory Board and the auditors.

The main point on the agenda of the second **meeting of the Supervisory Board,** which took place on **19 May 2005**, was the preparation for the general meeting of shareholders. Other points on the agenda included the strengthening of the sales and service activities in the Asian market. The meeting was attended by eleven members.

At the meeting following the **general meeting of shareholders on 20 May 2005,** the Supervisory Board elected Günther Berger as a member of the Finance and Auditing Committee. He was also elected Chair of the Committee. Ulrich Hocker was elected as member of the Personnel and Conciliation Committee. This meeting was attended by ten members of the Supervisory Board.

Intensification of committee work

Main points on the agenda of the fourth **Supervisory Board meeting on 8 September 2005** included, along with the present business development, the development of the "Services" division. All twelve members were present at this meeting. At the **planning meeting of 30 November** the Supervisory Board discussed the group strategy and approved of the planning for the financial year 2006. An efficiency audit of the Supervisory Board and its committees was initiated. In addition, the Supervisory Board adopted alterations to its rules of internal procedures. The former Personnel and Conciliation Committee has been split into two committees. The newly introduced Personnel, Nomination and Remuneration Committee will focus on nomination and remuneration issues. The Conciliation Committee will exclusively perform its role as described by law. Moreover, the auditors of KPMG informed about new developments of the reporting standards according to IFRS. The meeting was attended by eleven members of the Supervisory Board.

In the reporting year, the **Finance and Auditing Committee** and the Committees that were responsible at the time for staff matters, prepared the work of the Supervisory Board. The Finance and Auditing Committee met four times in total. Main points on the agenda were the auditing of the Annual Financial Statements and Annual Consolidated Financial Statements, corporate planning for 2006, the finance and tax strategy and risk management. Further points included the independence and remuneration of the auditor and preparations for, and the awarding of, the audit assignment.

The **Personnel and Conciliation Committee** that existed in this form until 30 November 2005, met three times in 2005. The adequacy audit regarding the remuneration of the Supervisory Board and the Executive Board was carried out in all meetings. Following its introduction, the **Personnel, Nomination and Remuneration Committee** met for the first time on 30 November 2005. A Conciliation Committee meeting in accordance with section 27 para. 3 of the German codetermination law (Mitbestimmungsgesetz) was not called. The committee members regularly submitted detailed reports on the committees' work to all members of the Supervisory Board.

Recommendations of the code of Corporate Governace completely achieved

At its meeting on 8 September 2005, the Supervisory Board and Executive Board adopted the **2005 Declaration of Compliance** regarding the German Code of Corporate Governance. In future, GILDEMEISTER will achieve all recommendations as set out in the German Code of Corporate Governance. The joint report of the Supervisory Board and the Executive Board on "Corporate Governance" starts on page 65.

The audit report issued by the auditors and the entire reporting package were submitted to the members of the Supervisory Board in time for the Supervisory Board meeting on the financial statements on 28 March 2006. The year-end audit 2005 focused on the treatment and valuation of inventories and the accrued deferral of sales. Prior to the balance sheet meeting of the Supervisory Board, the Supervisory Board's Finance and Auditing Committee obtained detailed information on the corporate situation by inspecting and checking all relevant documents. The financial statements, management reports and audit reports were all discussed in detail.

During the meetings, the auditors informed the Finance and Auditing Committee and the plenum of the Supervisory Board on the development and results of their audit and were available for questions and additional information. They also confirmed that GILDEMEISTER has in place a functional early risk recognition system as required by Section 92 paragraph 2 German Companies Act (AktG). The detailed Risk Report starts on page 92.

The accounts auditor issued an unqualified audit opinion

The Executive Board prepared the Annual Financial Statements and the Management Report 2005 of GILDEMEISTER Aktiengesellschaft in accordance with the provisions of the German Commercial Code (HGB). The Consolidated Financial Statements of GILDEMEISTER Aktiengesellschaft were prepared in accordance with International Financial Reporting Standards (IFRS). In accordance with the exemption provision in Section 315a HGB, Consolidated Financial Statements in accordance with HGB were not prepared. The auditor, KPMG Deutsche Treuhand-Gesellschaft Aktiengesellschaft, Wirtschaftsprüfungsgesellschaft, Berlin/Frankfurt am Main, issued an unqualified audit certificate to both Financial Statements and the Management Reports.

The Annual Financial Statements have been adopted in accordance with § 172 of the Stock Corporation Act (AktG)

On the basis of its own audit of the Annual Financial Statements, the Management Report, the Consolidated Financial Statements and the Group Management Report, the Supervisory Board, at its meeting on 28 March 2006, approved of the results of the audit. The Supervisory Board approved the Annual Financial Statements and the Consolidated Financial Statements for the financial year 2005. The Annual Financial Statements of GILDEMEISTER Aktiengesellschaft have therefore been certified in accordance with Section 172 of the German Companies Act (AktG). The Supervisory Board endorses the Executive Board's proposal for the appropriation of retained profits.

Dr.-Ing. Manfred Lennings resigned his Supervisory Board seat with effect from 20 May 2005. On the same day, the members of the general meeting of shareholders elected Prof. Dr.-Ing. Uwe Loos as a member of the Supervisory Board. Peter Oxfart, staff representative, and Alfred Geißler, senior executives' representative, resigned from the Supervisory Board on 31 January 2005 and 1 June 2005 respectively. Their successors on the Supervisory Board are Rainer Stritzke since 1 February 2005 and Norbert Zweng since 2 June 2005.

The Supervisory Board would like to thank all retired members for their work, and would like to express special thanks to former Supervisory Board member Dr.-Ing. Manfred Lennings for his dedication and commitment over many years. We also thank the Executive Board and all our employees for their continued commitment and hard work throughout the year.

Bielefeld, 28 March 2006

THE SUPERVISORY BOARD

Hans Henning Offen
Chairman

“Develop and implement strategies”

GILDEMEISTER meets global market requirements, and as a result the requirements of its customers, with innovative products and services. To continue setting international standards, we will pursue the development and implementation of our innovation-based strategies. Along with further investments in the expansion of our technological lead, this includes the expansion of our presence in all major industrial countries. Increasing the value of our company forms the basis of our entrepreneurial activities.

Dr. Rüdiger Kapitza (51)
Has been Chairman of the Executive Board since April 1996. He was appointed to the Executive Board of GILDEMEISTER Aktiengesellschaft in 1992. Following his training as a machinist and industrial clerk at GILDEMEISTER, he studied Economics in Paderborn and obtained his Doctorate at the Johannes Gutenberg University in Mainz. Dr. Rüdiger Kapitza takes responsibility for Corporate Strategy, Product Development, Sales and Services, Purchasing, Personnel and Public/Investor Relations.

Prof. Dr.-Ing. Raimund Klinkner (41)

Studied Mechanical Engineering at the Munich University of Technology and has been a member of the Executive Board since May 1998; from 1 January 2003 as Deputy Chairman of the Executive Board. His areas of responsibility include Procurement, Production, Logistics and Investments as well as projects covering various areas, such as the development of the production site in Shanghai. Prof. Dr.-Ing. Raimund Klinkner is honorary professor of Production Logistics at Berlin Technical University, Faculty for Technology and Management. Before his appointment to the GILDEMEISTER Executive Board, Dr. Raimund Klinkner worked in the car industry.

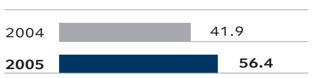
Michael Welt (51)

Has been a member of the Executive Board since January 2003. He is responsible for Controlling, Finances and Information Technology (IT). Michael Welt holds a degree in business administration (Dipl.-Kaufmann) and has been Commercial Director at DECKEL MAHO Pfronten GmbH since 1996. This appointment is in addition to his other responsibilities. Before he joined GILDEMEISTER, Michael Welt was a manager in the mechanical and plant engineering area.

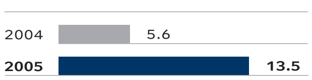
Order intake
in € million

Sales revenues
in € million

EBIT
in € million



Profit for the year
in € million



Employees
(incl. trainees)

Dear Shareholders,

GILDEMEISTER has reached its targets for 2005! We have continued to increase sales revenues, order intake and income – despite strong global competition. At € 1,170.7 million we have achieved the highest order intake in the 135-year history of the company. At € 1,125.9 million, sales revenues came close to the record figure for 2001. Profitability continued to improve also: EBITDA amounted to € 87.8 million; and EBIT to € 56.4 million. EBT was € 25.4 million and has therefore doubled. The group has recorded an annual profit of € 13.5 million. Earnings per share rose to € 0.32. The conclusion is: GILDEMEISTER has returned to solid growth.

The Executive Board and Supervisory Board will propose to the general meeting of shareholders, to be held on 19 May 2006, to distribute a dividend of € 0.10 for the financial year 2005. The course of business for 2005 is set out in more detail in the “Results of Operations, Net Worth and Financial Position” chapter starting on page 36.

Basis of this good business development in 2005 was the fact that our products and services were in more demand than ever before. We sold 5,114 machine tools worldwide and thereby maintained world market leadership. Our success was supported by the right strategy and the high motivation of our employees. We have not yet relocated any high-tech jobs abroad and do not intend to do so either, even though competitive pressure remains high, costs of material and energy have risen noticeably and we continue to fight against the weak dollar. This Annual Report presents to you the details of this development in the usual form and communicates an authentic and detailed image of your company.

At GILDEMEISTER the motto for 2006 is “technology, service and performance”. In the segments “Machine Tools” and “Services” GILDEMEISTER disposes of an exemplary know-how in the industry. Our complete entrepreneurial activities continue to focus on our customers’ requirements. Your success is our success! The start of the new year has shown that we are heading in the right direction. Growth stimuli came again from Asia – particularly China and Japan – and from the USA. In the past years GILDEMEISTER has – besides the development of new products – invested significantly in the expansion of its international distribution and service organisations; we will begin to harvest these fruits.

The **international market** demands machines with ever higher precision and more performance in less time at nearly the same price and level of energy consumption. The customer demands a reliable service and technology support – worldwide around the clock. In the past years, GILDEMEISTER has set standards. To us, research and development continue to be our top priority. We employ more than 400 construction engineers and have invested about € 220 million in innovations in the past five years. It is this commitment that secures our technological competitive edge. Thanks to our target-oriented innovation policy, we have created the basis for tomorrow’s corporate success.

Our objectives for the year 2006 are ambitious again: Following the optimisation of our production and logistics and of our position in the European market, we will now focus on the lasting improvement of our presence in the world markets, by first realigning our sales and service network in Asia and in America. Our range of products remains innovative and trendsetting.

For 2006 we expect, for the first time, order intake to exeed € 1.2 billion

GILDEMEISTER has become more profitable and more efficient again. We will continue to pursue this positive developments at a higher level. For the year as a whole we expect, for the first time, order intake to exceed € 1.2 billion. We intend to increase our sales revenues according to the order intake. It remains GILDEMEISTER's ambition to further increase and sustain the group's earning power. For the financial year 2006 we aim for an improvement in EBT and in the annual profit of more than 30%. Also for the current financial year a dividend shall be distributed.

Furthermore we intend to improve the other financial key indicators: Particularly free cash flow shall be increased to more than € 30 million. We intend to increase the return on capital employed (ROCE) to about 10%. We will continue to reduce net indebtedness. We aim at an equity ratio of about 30% by the end of the year. With these targets we will increase our company's market value and highlight the shareholder-value approach as major components of our corporate governance. We will continue this value and growth oriented strategy in the **financial year 2007.**

We will continue our value and growth oriented strategy

To be successful, we need the trust of our customers and suppliers, the trust of our investors and employees as well as the trust of you, our owners. The basis for this is transparent communication. A long-term-value-oriented management – in the sense of Corporate Governance – reflects GILDEMEISTER's core values, the foundations of which are our virtues: speed in innovation and a strong global presence in all the major industrial countries of the world. Ladies and gentlemen, my colleagues and I would like to thank you for your commitment to GILDEMEISTER. We hope to have your continued support!

Yours sincerely,

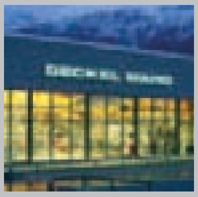
Rüdiger Kapitza

Dr. Rüdiger Kapitza
Chairman of the Executive Board
Bielefeld, 28 March 2006

January

In the financial year 2005 GILDEMEISTER has once again confirmed its innovative power. 22 product developments have been presented at a total of 67 national and international trade fairs and exhibitions throughout the year.

February



The traditional highlight at the start of the year: The DECKEL MAHO in-house exhibition in Pfronten began on 22 February and ended with the positive balance of 161 sold machines and an order intake of € 40.3 million.

March

16 March saw the opening of the in-house exhibition at DMG Italia in Bergamo. 700 visitors and orders to the value of € 9.2 million exceeded all our expectations.

At GILDEMEISTER the first quarter developed according to plan. Compared to the previous year order intake was up by 17%. The good level of international transactions has contributed to this development.

April

With 71 machines sold and an order intake of € 16.1 million, the in-house exhibition at DECKEL MAHO Seebach was a success.

May

Grand Opening on 27 May: To benefit long-term from the fast-track growth in Turkey, DMG Istanbul was set up. Within a few weeks the new DMG generated an impressive percentage of orders in the Turkish machine tool market.

On 20 May the 103rd general meeting of shareholders took place, which was attended by more than 1,000 shareholders. For the first time, Hans Henning Offen as the new chairman of the Supervisory Board presided over the meeting.

June

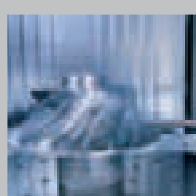
With the opening of DMG Russia on 21 June, GILDEMEISTER reinforced its presence in East Europe. Once more, this market offers good growth potentials for machine tools. DMG Russia intensifies this historically good relationship.

In the first six months of 2005 GILDEMEISTER increased order intake, sales revenues and performance, thereby building on the positive trends of the first quarter. Sales were up to € 517.8 million (+6%). Order intake increased to € 574.2 million (+6%).

July

In 2005 GILDEMEISTER employed overall 189 trainees. Groupwide we took on 64 trainees, demonstrating the importance of in-company training.

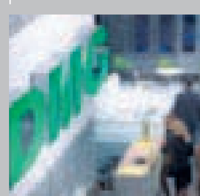
August



For the sixth successive time, the GILDEMEISTER Annual Report took top position in the annual ranking by the “manager magazin”. The honour extended to the quarterly report, which the jury praised as being exemplary.

September

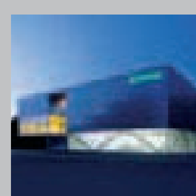
At the EMO 2005 in Hanover, the industry’s mood indicator, GILDEMEISTER exhibited 65 high-tech machines, 9 of which are world premieres. A business volume of € 87.4 million and 451 sold machines resulted in GILDEMEISTER’s highest order intake ever achieved at a trade fair.



In the third quarter GILDEMEISTER continued the good business development of the first six months of the financial year. Both order intake and sales increased by 8%.

October

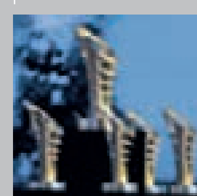
On 1 October 2005 GILDEMEISTER celebrated its 135th anniversary. Further anniversaries were celebrated at the following production sites: GILDEMEISTER Italiana S.p.A. (30 years), GRAZIANO Tortona S.p.A. (65 years) and DECKEL MAHO Seebach GmbH (15 years).



On 19 October 2005, GILDEMEISTER set up DMG Europe Holding GmbH at the heart of Europe – in Klaus, Vorarlberg/Austria. From here, the sales and service activities of all European DMG companies are controlled. The domestic market (Germany) is still controlled from Stuttgart.

November

For the first time, the “Manufacturing Excellence Award” (MX Award) was presented at the initiative of GILDEMEISTER. In six categories, German medium-sized enterprises were honoured for “best-practice solutions”.



December

At € 1,170.7 million, GILDEMEISTER has achieved the highest order intake in the 135-year history of the company thereby exceeding the high figures of the previous year. Sales revenues were up 7% to € 1,125.9 million. Profitability of the group further improved.

Business Environment

In 2005 global economy expanded despite the sharp increase in the prices of crude oil and energy. Along with the USA, China was the driving force of worldwide economic activity. The Japanese economy also picked up noticeably. Economic recovery in the European Union on the other hand was less apparent. In Germany particularly, economic progress was subdued.

Overall Economic Development

In 2005 the **global economy** experienced another strong surge. In the USA particularly, growth experienced another rapid increase over the year. Fresh stimulus for this positive economic development also came from Asia, particularly China. The revival experienced in the European Union was comparatively moderate, however an upward trend became apparent during the second half of the year. This applies to Germany as well. According to provisional calculations by the Institute for World Economics (IfW) based at Kiel University, aggregate output rose globally by 4.3% (previous year: 5.1%).

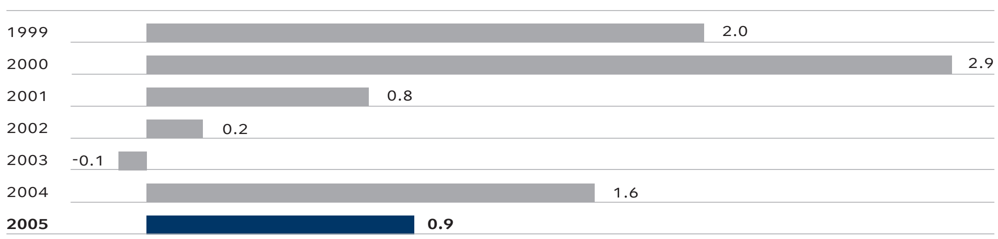
In **Asia** growth continued to be the order of the day. Economic activity in Japan picked up noticeably in 2005, with reduced vigour however during the second half of the year. Here the main buoyant force was domestic demand. Exports increased mainly as a result of stronger demand from the remaining regions in Asia. Once more China proved to be one of the major driving forces of global economic activity. Here, the rate of growth remained at its high level. The gross domestic product in China was up 9.2% (previous year: 9.0%) and in Japan 2.3% (previous year: 2.7%).

In the **USA** economic recovery also continued. This was mainly due to the strong increase in private consumption. The vigour of capital investment on the other hand decreased slightly. Exchange rate trends also had a slow down effect. Exports were on the rise, whilst the development of imports slowed down. Over the entire year, gross domestic product increased by 3.6% (previous year: 4.2%).

Overall, the economic situation in **Europe** picked up only slowly, although this varied hugely from country to country. Following a weak expansion in production during the first six months, slowed down by the increased oil price and the previous upward revaluation of the Euro, signs of an economic revival became evident from the middle of the year. In this respect, fresh stimulus was triggered mainly from international demand. Investment activity also picked up. However, no positive effects were felt by the job market. According to provisional figures, gross domestic product in the Euro states was up by 1.4% (previous year: 2.1%). The EU, with its 25 member states, recorded a 1.6% increase (previous year: 2,4%).

Gross domestic product of Germany
Real changes against the previous year in %

Source: Statistisches Bundesamt (Federal Statistical Office), Wiesbaden

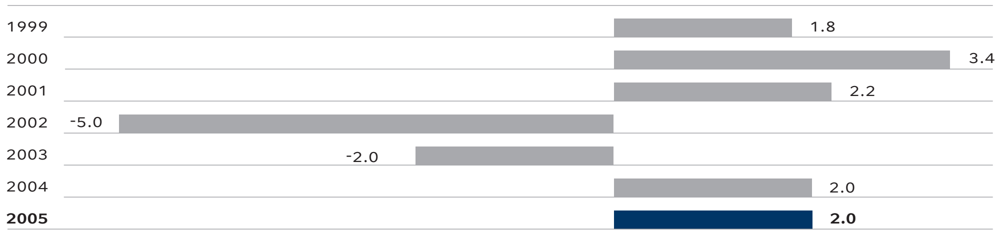


Economic trends in **Germany** were subdued. According to provisional figures from the Federal Statistical Office in Wiesbaden, the gross domestic product increased by 0.9% (previous year: 1.6%). Fresh stimulus was triggered from exports, recording an increase of 6.2%. Increasing growth was noted in investments in plant and equipment. This increase was about 4.0% (previous year: 1.2%). The situation in the job market continued to be tight. At the end of 2005 4.6 million people were out of work, more than in the previous year (4.5 million). At almost 38,000 the number of insolvencies decreased slightly by about 2,000 in comparison with the previous year. Cost of living rose sharply and the rate of inflation was 2.3% (previous year: 1.6%). The situation in public spending remained critical over the reporting year. The slightly reduced deficit quota of 3.5% again missed the reference value provided in the Maastricht treaty for the fourth time in succession.

Sources: Federal Statistical Office, Wiesbaden; Institute for World Economics (IfW), Kiel; ifo Institute, Munich

Investments in the German manufacturing sector
Nominal changes against the previous year in %

Source: ifo Institute (Economic Research Institute), Munich



The movement of foreign **exchange rates** in this period has to be evaluated in different ways. Over the year, the US dollar has gained in value in relation to the Euro, with the average market price remaining at the previous year's level ($ 1.24). On 3 January 2005 the US dollar reached its annual high of $ 1.35. From then on it fluctuated between $ 1.20 and $ 1.25, reaching its lowest value of $ 1.17 on 15 November 2005. In July 2005 the exclusive linking of the Chinese currency Renminbi to the US dollar was cancelled. Following an upward revaluation of 2% in July, the Chinese renminbi initially developed in parallel with the US dollar. Compared to the Renminbi the Euro fell slightly by 1% in the annual average. In the fourth quarter, the Chinese currency rose again by about 1% in relation to the US currency. The Japanese yen maintained its position and was up against the Euro in the second half of the year. Following its lowest value of ¥ 130.9 on 7 June 2005, the yen climbed to its ¥ 143.3 peak on 13 December 2005. This resulted in an annual average rate of exchange in relation to the Euro of ¥ 137.1. More detailed explanatory notes on the movements of the Euro in comparison with selected currencies are set out on page 31.

In the reporting year **GILDEMEISTER** benefited from an expanding global economy and maintained its leading market position. Against the current industry trend, we continued to increase our order intake in Germany. As planned, growth in Europe was stable. Orders from America and Asia continued to perform well and were up again.

Development of the Machine Tool Building Industry

International Development

In 2005 the global market for machine tools developed positively and reached a high level. According to calculations by the Association of German Machine Tool Factories (VDW) **global output** was € 41.7 billion. This represents another rise against 2004 of 14% (previous year: € 36.6 billion). As in the previous years, Japan was again the largest producer of machine tools. With an output to the value of € 10.7 billion, Japan has expanded its global market share to 26% (previous year: 23%). The global market share of Germany (output: € 7.8 billion), placed second, decreased by one percentage point to 19%. With an output of € 4.0 billion, China increased its global market share to 10% (previous year: 9%) and for the first time pushed Italy (output: € 3.9 billion, global market share: 9%) from place three. They were followed by Taiwan (output: € 2.7 billion, global market share: 6%) and USA (output: € 2.5 billion, global market share: 6%). The above six nations together produced 76% of machine tools worldwide (previous year: 75%).

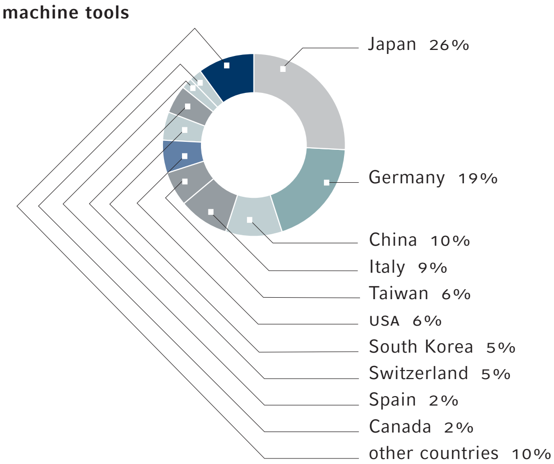
The individual world regions' shares in international production*

Shares in worldwide production	2005 in %	2004 in %
Europe	43	46
(of which Germany)	(19)	(20)
Pacific Region	48	44
(of which Japan)	(26)	(23)
America	9	10

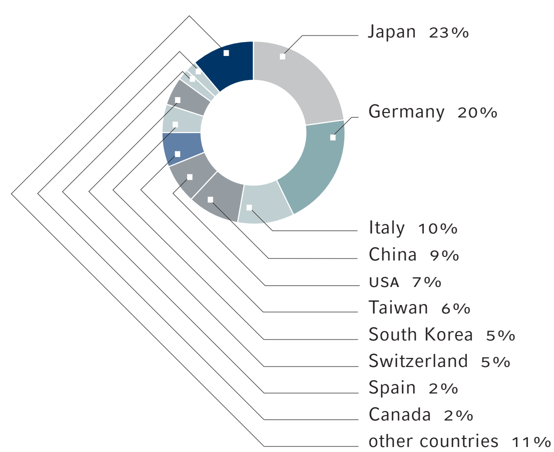
* Provisional figures for 2005; revised values 2004

Worldwide production of machine tools

2005: Total of € 41.7 billion



2004: Total of € 36.6 billion



In the reporting year 56% of global production was exported (previous year: 55%). In respect of **exports**, there was further confirmation of the leading role of Germany with its export share of 66% (previous year: 63%) and Japan with an export share of 49% (previous year: also 49%). Both countries together accounted for 44% by value of world exports (previous year: 43%). They were followed, at some distance, by Italy, Taiwan, Switzerland, South Korea and the USA. Each of their shares – like the shares of the remaining countries – was below 10%.

Global consumption also rose by 14% to € 41.7 billion (previous year: € 36.6 billion). An overview of the chronological development of worldwide consumption of machine tools over the previous ten years is included in the Forecast Report on page 97. With a consumption of € 8.8 billion, China confirmed its position as the world's largest market for the fourth successive year; consuming 21% of all machine tools (previous year: 21%). It was followed, by noticeable distance, by Japan (€ 6.1 billion). The USA came third (€ 4.7 billion), followed by Germany (€ 4.3 billion). The Indian market experienced a particularly strong increase (+78%).

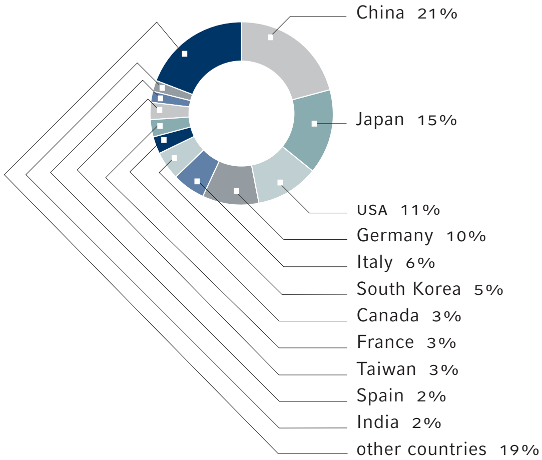
Worldwide consumption of machine tools*

Shares in worldwide consumption	2005 in %	2004 in %
Europe	**33**	35
(of which Germany)	**(10)**	(11)
Pazific Region	**49**	47
(of which Japan)	**(15)**	(13)
America	**17**	17
Rest of the world	**1**	1

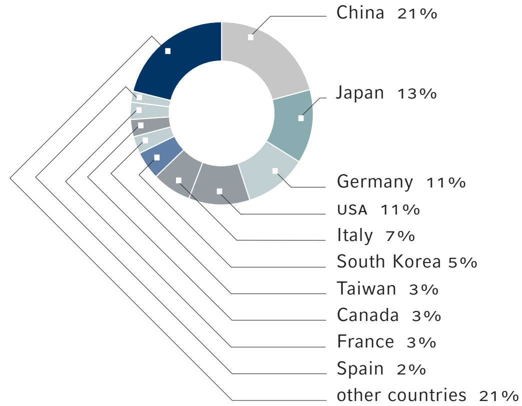
* provisional values 2005; revised values 2004

Shares in worldwide consumption

2005: Total of € 41.7 billion



2004: Total of € 36.6 billion



With respect to the **import** of machine tools, China with a growth of 13% to € 5.4 billion, took the lead in 2005, as it had done in the previous four years (€ 4.8 billion). The USA increased their imports from € 2.5 billion in 2004 to € 3.0 billion (20%). The two major importing nations were responsible for 36% of worldwide imports (previous year: 36%). Based on total consumption, China's import share decreased by two percentage points to 61% (previous year: 63%), whilst the USA had to import 65% of its consumption in the reporting year (previous year: 62%). In the reporting year Germany's import share was 38% (previous year: 36%). It was followed by Italy with an import share of 37% (previous year: 33%) and South Korea with 41% (previous year: 41%).

Sources: The basis of the world machine tool statistics is the data published by the VDW (German Machine Tool Builders' Association) (excluding parts and accessories). This data is requested by the national producers' associations of each individual country and is based on the current actual values or, for the remainder of the year, on careful estimations based on the updated values of the preceding year.

Explanatory notes on the problem of exchange rates

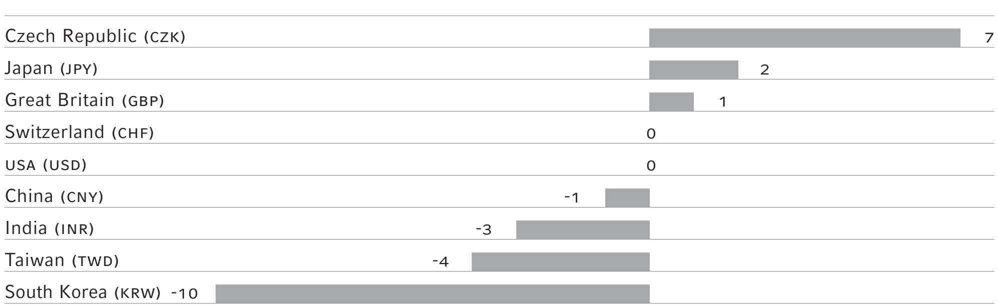
World Machine Tools Statistics

With the introduction of the common currency, possible exchange rate distortions ceased to play a role within the Euro countries, but remain relevant with regard to third currencies, for example in respect of the US dollar, Renminbi or Yen. As the chart of the movements of the Euro in relation to selected currencies demonstrates, the shifts in purchasing power remained moderate in comparison to 2004: Due to an upward revaluation of 7% against the previous year, the rise in the price of the Euro was felt mostly by customers from the Czech Republic. There were none or hardly any changes for Japan (2%), Great Britain (1%) and Switzerland (0%). The US dollar remained at a weak level (0%) with the result that the Euro continues to have a strong negative impact on products invoiced in dollars. In Asian countries, for the first time since 1999 the price of the Euro has become more attractive again: in China by 1%, in India by 3%, in Taiwan by 4% and in South Korea by 10%. However, the above industrial nations used to record the highest revaluation rates in the past – sometimes up to 20%.

Changes in the Euro 2005 compared with 2004 against the individual national currencies

in %

Source: Deutsche Bundesbank



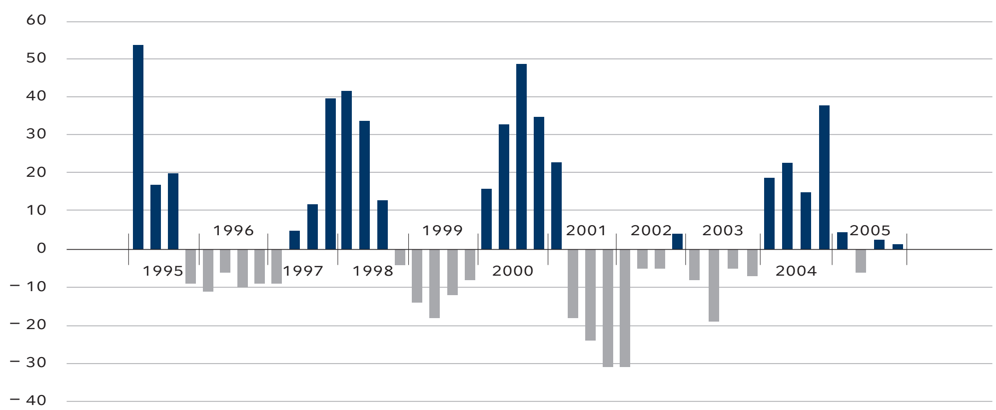
German Machine Tool Industry

For the German machine tool industry the year 2005 was dominated by a high level of stagnating order books and increases in production and exports.

Incoming orders were up only slightly by 1% to € 10.4 billion (previous year: € 10.3 billion). International demand increased by 2% (previous year: 24%), whilst domestic orders remained at the previous year's level (previous year: 10%).

The business climate index of the Munich-based ifo Institute reflected this development on a high level in their estimates for the principal purchaser industries: General engineering, automotive industry and electrical engineering did not record any positive trends before the second half of the year.

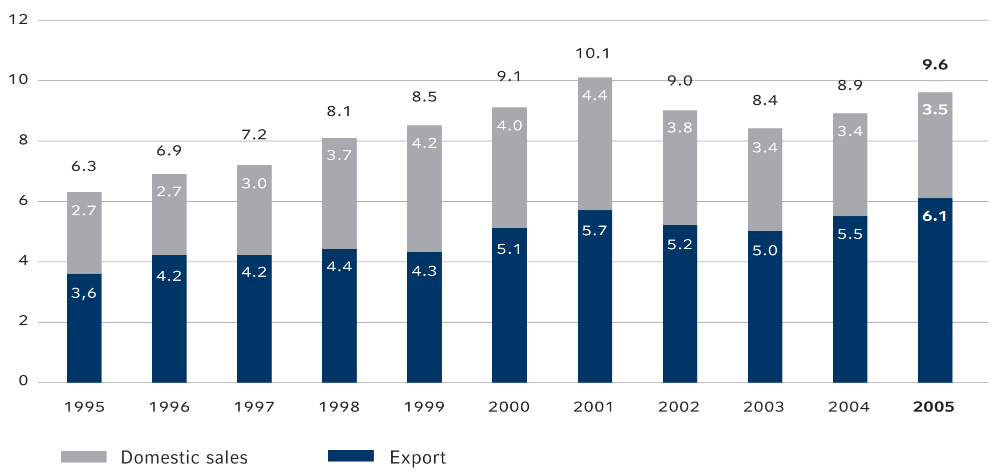
Machine Tool order intake in Germany
Real changes against the previous year in %



Production continued to rise in the reporting year: At € 9.6 billion it exceeded the corresponding figure for the previous year by € 0.7 billion or 8% (previous year: € 8.9 billion). This increase was more evident in the first six months of the year than in the second half of the year.

Machines to the value of almost € 6.1 billion (previous year: € 5.5 billion) went into **exports**, thereby exceeding the previous record result from 2001 by € 0.4 billion or 7%. The export share increased to 64% (previous year: 62%) – the highest value in ten years. China remained the most important market for German machine tools for the second successive year. Exports to China were up by 22.3 million or 3% to € 792.4 million (previous year: € 770.1 million). This represents 13% of German exports (previous year: 14%). The Chinese market therefore retained its leading position curtly against the USA, to whom machines to the value of € 790.7 million were delivered (previous year: € 714.4 million). As in the previous year, an increase of € 76.3 million or 11% resulted in a 13% share in German exports. They were followed, by a noticeable distance, by France with a 6% share in exports (previous year: 6%), Italy with 5% (previous year: 5%) and Switzerland also with 5% (previous year: 5%).

Machine tool production in Germany
in € billion



In the reporting period, the **import** of machine tools rose by € 0.2 billion or 10% to € 2.2 billion (previous year: € 2.0 billion). Domestic sales generated by the German machine tool industry increased by € 0.1 billion or 3% to € 3.5 billion, representing 61% of domestic consumption (previous year: 64%). **Domestic consumption** amounted to € 5.7 billion, thereby exceeding the previous year's figure by € 0.4 billion or 8% (previous year: € 5.3 billion). As in the previous years, most imports originated from the following five countries: Switzerland, Japan, Italy, Czech Republic and the USA. Switzerland again exported about twice as many machines by value to Germany as Japan.

Capacity utilisation at the German machine tool factories increased over the year. On average it amounted to 91% and was two percentage points above the previous year (89%). The annual average of capacity utilisation in cutting machine tool production was approximately 94% (previous year: 91%).

As in the previous year, the average **order backlog** covered 6.2 production months. This range of coverage, which is based on calculations, represents an average value for the industry sector and can only be a rough indicator of the order backlog due to its compilation. Along with standard machines with extremely short delivery times, it includes special machines and large non-cutting machine tools with long delivery times. At the beginning of the reporting year, the range of coverage was 6.6 months and was reduced to 5.9 months over the year.

The number of **employees** in German machine tool companies remained unchanged at 65,000.

Reliable statements on the **profitability** of the German machine tool industry are not readily available, as only a few companies publicise their figures. The Association therefore has to rely on estimates. It has to be said, though, that overall and in view of current economic trends, the industry's profitability is unsatisfactory. In the reporting year the tight earnings situation of some machine tool manufacturers resulted in a concentration process with major takeovers, which in turn led to major structural changes in the industry sector.

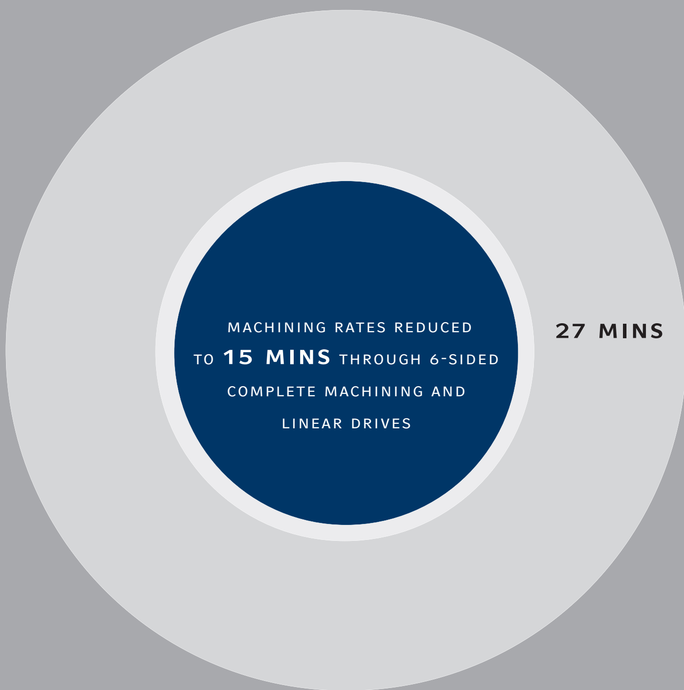
Sources: VDW; VDMA – Trade Association for Machine Tools and Production Systems (Figures include parts and supplies and exclude service and installation; some figures pertaining to the previous year were updated)


40%

Shorter machining rates thanks to a **100% Know.how** in turning.

UP TO 40% TIME SAVING THANKS TO STATE-OF-THE-ART TURNING TECHNOLOGY AND 6-SIDED COMPLETE MACHINING

WORKPIECE:
STAINLESS STEEL DRIVING COMPONENT USED IN MACHINE CONSTRUCTION, MACHINED ON THE GMX 400 *linear* TURNING AND MILLING CENTRE



MACHINING RATE OF A UNIVERSAL LATHE AND A MILLING MACHINE NOT EQUIPPED WITH 6-SIDED COMPLETE MACHINING FACILITIES AND LINEAR DRIVES

With 8 product lines GILDEMEISTER provides its customers with the highest quality lathes and a production programme that is unique throughout the world of turning, offering a perfect solution for every requirement. The GMX 400 *linear*, for example, combines state-of-the-art turning and milling technologies and provides highest performance for 6-sided complete machining tasks. The freely interpolatable 5-axis programming enables machining of complex workpieces. The linear drive on the z-axis and high-performance milling spindle combine power and speed at highest precision. The simultaneous machining at the main spindle and counter spindle saves time and increases productivity.

Results of Operations, Net Worth and Financial Position

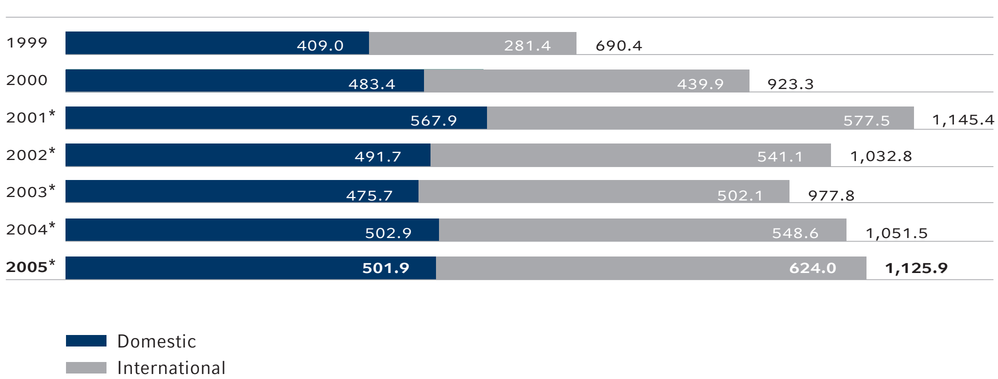
Overall and against a background of worldwide economic growth, 2005 was a satisfactory financial year for GILDEMEISTER. We have reached our budget estimates and slightly exceeded our targets published in the previous Interim Report. Sales revenues amounted to € 1,125.9 million; we had planned for an increase to about € 1.1 billion. With an order intake of € 1,170.7 million, we have confirmed our target of more than € 1,150 million. EBT amounted to € 25.4 million and was therefore in line with our reported targets. At € 13.5 million, annual profit exceeded our published target of more than € 10 million. Our objective of distributing dividend was accomplished.

Sales Revenues

The increased demand for machine tools had a positive impact on our sales revenues development. The trend towards complex and customer-specific machines has continued. Concurrently we could achieve significant increases in pieces with our entry-machines also because of the ramp up of new products as for example the NEF 400 and the DMC 635 V. Sales revenues increased by € 74.4 million or 7% to € 1,125.9 million (previous year: € 1,051.5 million). In the fourth quarter, sales revenues amounted to € 333.3 million, thereby exceeding the figure for the previous year (€ 316.4 million) by 5%. International sales revenues increased by 14% to € 624.0 million. At € 501.9 million, domestic sales revenues were in line with the previous year. The export share was 55% (previous year: 52%).

You will find detailed information on sales revenues development in each segment in the chapter "Segmental Reporting" starting on page 52.

GILDEMEISTER group –
sales revenues
in € million



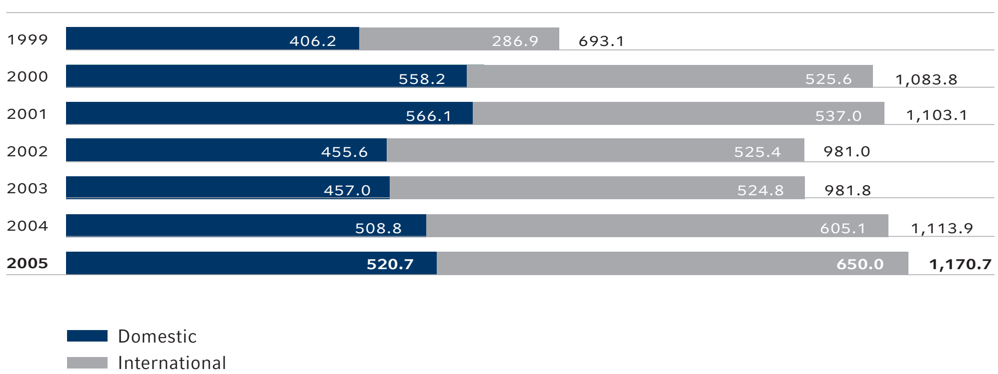
* in acc. with IFRS

Order Intake

In the financial year 2005, at € 1,170.7 million, GILDEMEISTER has achieved the highest order intake in the 135 year history of the company (previous year: € 1,113.9 million), representing a rise of € 56.8 million or 5% compared to the previous year. This was mainly due to the impressive success achieved at the EMO, the world's major trade fair for machine tools. With 451 sold machines at a value of € 87.4 million we accomplished the best trade fair result in the history of the company. In the fourth quarter, order intake of € 296.9 million remained roughly in line with the corresponding quarter of the previous year (€ 302.1 million). International orders increased by € 44.9 million or 7% to € 650.0 million (previous year: € 605.1 million). This resulted in a 56% rise in the international share (previous year: 54%). Domestic orders amounted to € 520.7 million (previous year. € 508.8 million), which is € 11.9 million or 2% more than the figure for the corresponding period of the previous year.

More detailed information on the order intake in each segment is included in the "Segmental Reporting" chapter starting on page 52.

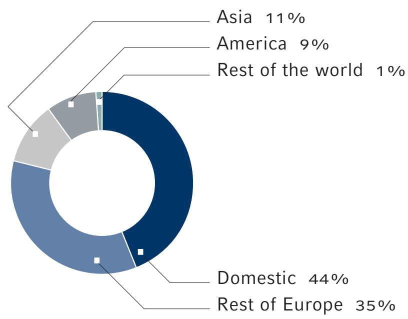
GILDEMEISTER group – order intake
in € million



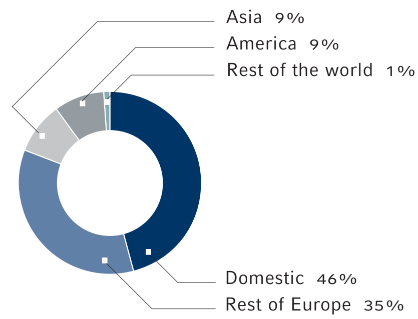
Thanks to our full-line products and worldwide presence we succeeded in reinforcing and extending our competitive position in all market regions: against the current industry's sector trend, we continued to increase the value of our order intake in **Germany.** As planned, growth in **Europe** was stable. Orders from **America** and **Asia** continued to perform well and were up again. In Asia, which has experienced continuous growth for years and is now responsible for nearly half of worldwide demand for machine tools, our business has noticeably increased.

GILDEMEISTER group – order intake by regions

2005: Total € 1,170.7 million



2004: Total € 1,113.9 million



In 2005, GILDEMEISTER sold a total of 5,114 turning, milling, ultrasonic/laser and used machines to 3,749 different customers. The **sales volume** rose by 8% when compared to the previous year. As especially demand for our successfully introduced entry-machines increased, the average value per machine only rose by 1%. Throughout the year, **selling prices** were raised by 2% to 6% depending on market conditions and each particular product.

A major contribution to the order intake again came from **key accounting**. Our support of international **major customers** is geared to their specific requirements. We were therefore able to secure orders to the value of € 96.3 million (previous year: € 114.4 million).

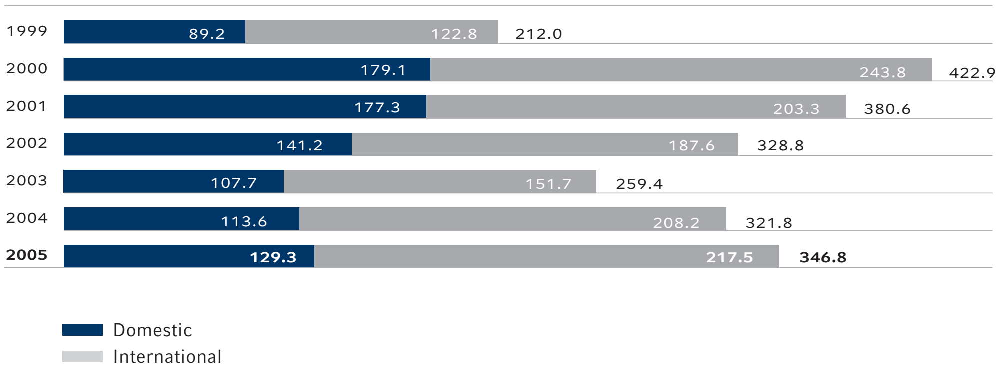
Order Backlog

On 31 December 2005, the group's order backlog amounted to € 346.8 million, thereby exceeding the figure for the previous year (€ 321.8 million) by € 25.0 million or 8%. 63% of these orders were attributed to international orders (previous year: 65%). Compared to the previous year, international order backlog increased by € 9.3 million (+4%) to € 217.5 million (previous year: € 208.2 million). Domestic order backlog increased by € 15.7 million (+14%) to € 129.3 million (previous year: € 113.6 million).

For computing purposes, this corresponds to a production capacity utilisation of about four months, representing a good basic capacity utilisation for the current financial year.

You will find detailed information regarding the order backlog of the single segments in the chapter "Segmental Reporting" starting on page 52.

GILDEMEISTER group – order backlog
in € million



Profitability

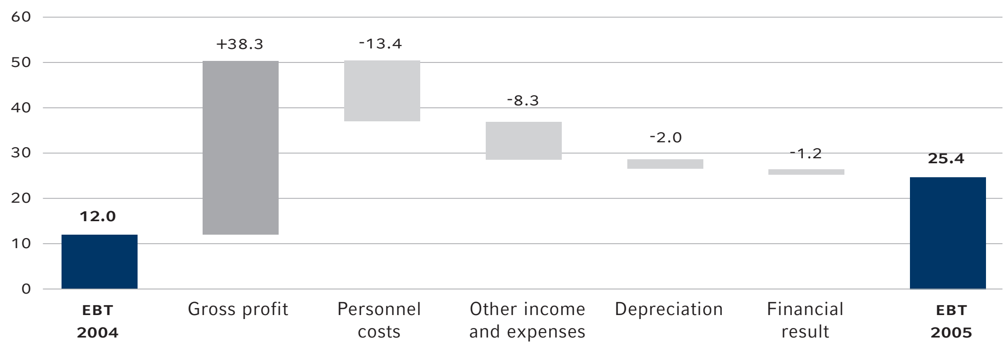
In the financial year 2005, profitability of the GILDEMEISTER group has improved as planned. **EBITDA** amounted to € 87.8 million (previous year: € 71.2 million), **EBIT** to € 56.4 million (previous year: € 41.9 million) and **EBT** to € 25.4 million (previous year: € 12.0 million). **Annual profit** was up to € 13.5 million (previous year: € 5.6 million). Both EBT and the annual profit therefore doubled in comparison with the previous year.

GILDEMEISTER group – Income Statement

	2005		2004		Changes against previous year	
	€ K	%	€ K	%	€ K	%
Total work done	**1,146,233**	**100.0**	**1,053,143**	**100.0**	**93,090**	**8.8**
Cost of materials	-608,541	-53.1	-553,716	-52.6	-54,825	9.9
Gross profit	**537,692**	**46.9**	**499,427**	**47.4**	**38,265**	**7.7**
Personnel costs	-295,926	-25.8	-282,524	-26.8	-13,402	4.7
Other income and expenses	-153,963	-13.4	-145,711	-13.8	-8,252	5.7
EBITDA	**87,803**	**7.7**	**71,192**	**6.8**	**16,611**	**23.3**
Depreciation	-31,369	-2.7	-29,339	-2.8	-2,030	6.9
EBIT	**56,434**	**4.9**	**41,853**	**4.0**	**14,581**	**34.8**
Financial result	-31,069	-2.7	-29,833	-2.8	-1,236	4.1
EBT	**25,365**	**2.2**	**12,020**	**1.1**	**13,345**	**111.0**
Taxes on profit	-11,835	-1.0	-6,444	-0.6	-5,391	83.7
Annual profit	**13,530**	**1.2**	**5,576**	**0.5**	**7,954**	**142.6**

Total work done reached € 1,146.2 million and was therefore € 93.1 million or 8.8% above the figure for the previous year (€ 1,053.1 million). The materials quota increased slightly from 52.6% to 53.1%. At € 537.7 million, gross profit was € 38.3 million or 7.7% above the figure for the previous year (€ 499.4 million). The gross profit margin was 46.9% (previous year: 47.4%).

GILDEMEISTER group – development of profitability (EBT) 2004 against 2005
in € million



The personnel quota decreased to 25.8% (previous year: 26.8%). Personnel costs amounted to € 295.9 million (previous year: € 282.5 million), which is an increase of € 13.4 million or 4.7%. This rise in costs is mainly due to higher customer requirements. Staff numbers in the "Services" segment therefore had to be increased. The balance from other income and expenses rose by € 8.3 million to € 154.0 million. Apart from sales-related rises in costs, additional costs were incurred by rental and lease expenses. Leasing and rental expenditure amounted to € 21.9 million in the reporting year (previous year: € 19.9 million). As at 31 December 2005 leasing and rental obligations for the financial year 2006 stood at € 17.1 million.

Depreciation/amortisation increased by € 2.0 million to € 31.4 million (previous year: € 29.4 million). This is mainly due to an increase in depreciation of capitalised development costs.

The financial result of € -31.0 million increased by € 1.2 million in comparison with the previous year (€ -29.8 million). The rise in interest paid is due to a higher level of the commitment of funds for business-related reasons.

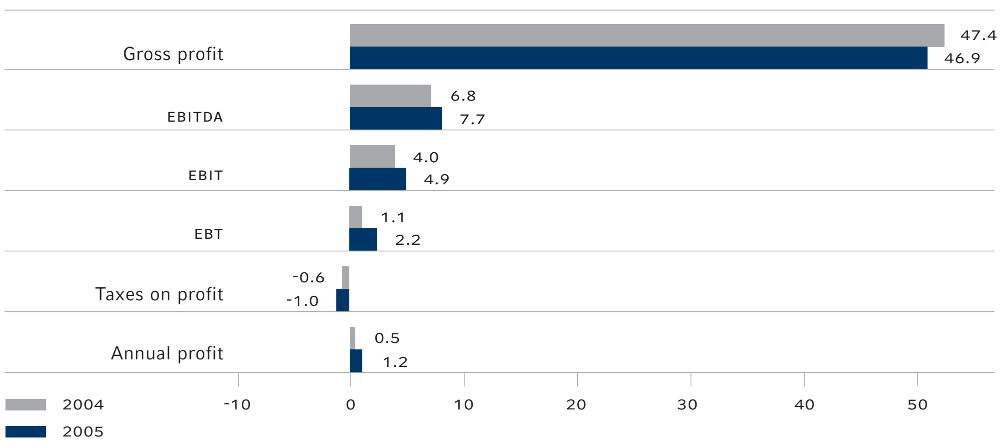
Tax expenditure was at € 11.8 million which is an absolute increase of € 5.4 million compared to the previous year (€ 6.4 million). The tax load ratio was 46.7% and decreased by 6.9 percentage points in comparison with the previous year (53.6 %), which was mainly due to the additional use of losses carried forward.

In the financial year we recorded an annual profit of € 13.5 million. The annual profit has therefore more than doubled compared to the previous year (€ 5.6 million).

The movement of margins, which are determined on the basis of total work done, has differed from that of the previous year. Whilst the gross profit margin decreased slightly by 0.5 percentage points to 46.9 %, the EBITDA, EBIT and EBT margin improved in comparison with the previous year. The EBITDA margin improved by 0.9 percentage points to 7.7% (previous year: 6.8%). The EBIT margin also increased by 0.9 percentage points to 4.9% (previous year: 4.0%). The percentage of personnel costs and for the balance of other income and expenses that decreased in comparison with the previous year, has had a positive impact on the improved earnings margins. In line with the EBT improvement, the EBT margin doubled by 1.1 percentage points to 2.2%. Taking into account tax expenditure, the annual profit margin more than doubled by 0.7 percentage points to 1.2% (previous year: 0.5%).

Further explanatory notes on our most important internal target and key performance indicators are set out in the "Organisation, Management and Legal Corporate Structure" chapter starting on page 70 as well as in the "Forecast" chapter on page 103.

GILDEMEISTER group – Changes in margins
in %



The **value added statement** demonstrates the difference between the company's output and the consumption of products and services in terms of value. The distribution statement shows the contribution of those participating in value-added activities – employees, company, lenders, shareholders/minority interests and government.

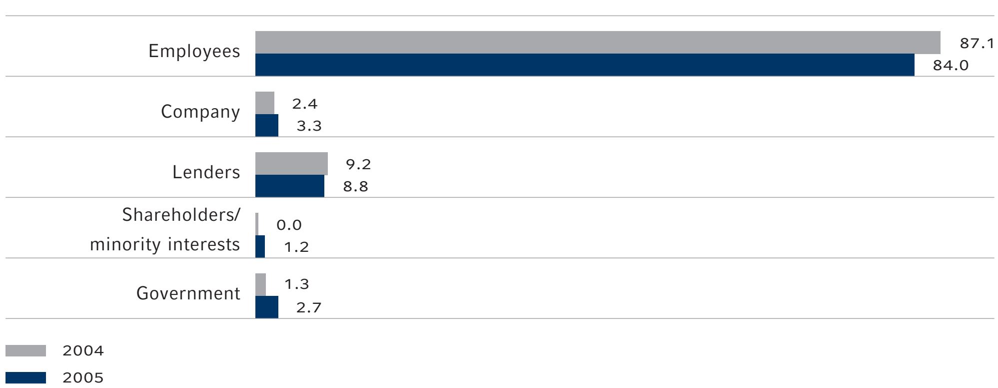
In the financial year 2005, the value added achieved by the GILDEMEISTER group amounted to € 352.5 million (previous year: € 324.5 million), representing a rise of 8.6% or € 28.0 million. Following the distribution of the contributions to the value added, the company is left with a positive share of € 11.5 million (previous year: € 7.8 million). The following table shows the value added statement in detail.

GILDEMEISTER group – Value added statement

	2005		2004		Changes against previous year	
	€ M	%	€ M	%	€ M	%
SOURCE						
Sales revenues	1,125.9	95.3	1,051.5	97.4	74.4	7.1
Other revenues	54.9	4.7	27.8	2.6	27.1	97.5
Operating performance	**1,180.8**	**100.0**	**1,079.3**	**100.0**	**101.5**	**9.4**
Cost of materials	608.5	51.5	553.7	51.3	54.8	9.9
Depreciation	31.4	2.7	29.4	2.7	2.0	6.8
Other expenses	188.4	16.0	171.7	15.9	16.7	9.7
Purchased materials and services	**828.3**	**70.2**	**754.8**	**69.9**	**73.5**	**9.7**
Value added	**352.5**	**29.9**	**324.5**	**30.1**	**28.0**	**8.6**

	2005		2004		Changes against previous year	
	€ M	%	€ M	%	€ M	%
DISTRIBUTION						
Employees	296.1	84.0	282.7	87.1	13.4	4.7
Company	11.5	3.3	7.8	2.4	3.7	47.4
Lenders	31.1	8.8	29.8	9.2	1.3	4.4
Shareholders/minority interests	4.3	1.2	0.0	0.0	4.3	0.0
Government	9.5	2.7	4.2	1.3	5.3	126.2
Value added	**352.5**	**100.0**	**324.5**	**100.0**	**28.0**	**8.6**

GILDEMEISTER group – Distribution of value added
in %



Net Worth and Financial Position

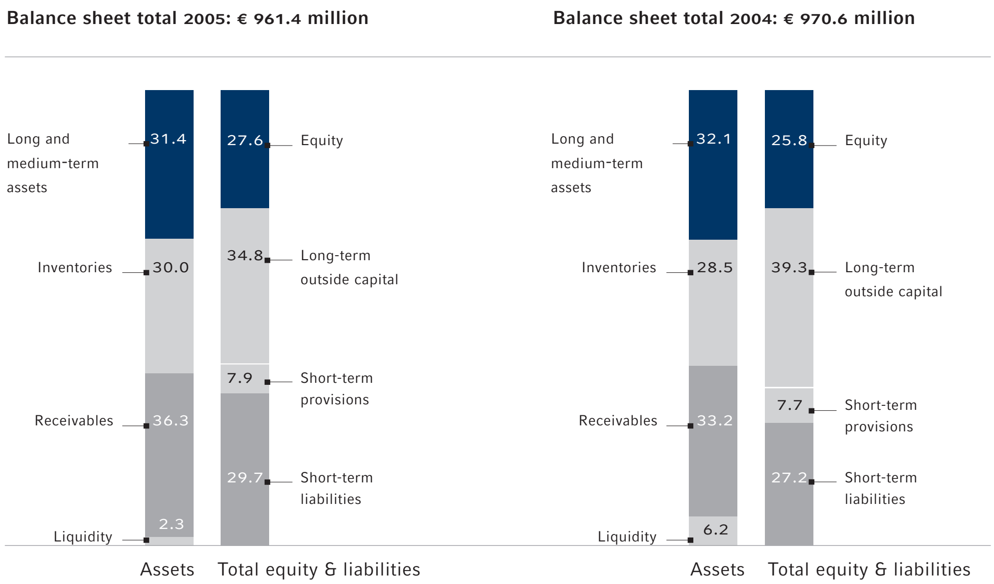
GILDEMEISTER group – balance sheet

	31 Dec. 2005		31 Dec 2004 [1]		Changes against previous year	
	€ K	%	€ K	%	€ K	%
Assets						
Long and medium-term assets						
Fixed assets	**262,353**	**27.3**	262,500	27.0	-147	-0.1
Current assets	**39,845**	**4.1**	49,449	5.1	-9,604	-19.4
	302,198	**31.4**	311,949	32.1	-9,751	-3.1
Short term assets						
Inventories	**288,777**	**30.0**	276,565	28.5	12,212	4.4
Receiveables and other assets	**348,521**	**36.3**	321,836	33.2	26,685	8.3
Liquid funds	**21,920**	**2.3**	60,297	6.2	-38,377	-63.6
	659,218	**68.6**	658,698	67.9	520	0.1
Balance sheet total	**961,416**	**100.0**	970,647	100.0	-9,231	-1.0
Total equity & liabilities						
Long and medium-term financing resources						
Equity	**265,782**	**27.6**	250,540	25.8	15,242	6.1
Outside capital						
Provisions	**49,796**	**5.2**	48,558	5.0	1,238	2.5
Liabilities	**284,412**	**29.6**	333,259	34.3	-48,847	-14.7
	334,208	**34.8**	381,817	39.3	-47,609	-12.5
	599,990	**62.4**	632,357	65.1	-32,367	-5.1
Short term financing resources						
Provisions	**75,611**	**7.9**	74,898	7.7	713	1.0
Liabilities	**285,815**	**29.7**	263,392	27.2	22,423	8.5
	361,426	**37.6**	338,290	34.9	23,136	6.8
Balance sheet total	**961,416**	**100.0**	970,647	100.0	-9,231	-1.0

[1] Adjusted data due to the application of IAS 39.

Compared with the previous year, the balance sheet total of the GILDEMEISTER group decreased by € 9.2 million or 1.0% to € 961.4 million (previous year: € 970.6 million).

Assets and capital structure of the GILDEMEISTER group in %



The **fixed assets** on the **assets side** decreased by € 0.1 million or 0.1% to € 262.4 million (previous year: € 262.5 million). In this respect, intangible assets increased by € 2.0 million , whilst tangible fixed assets decreased by € 2.1 million. The asset additions are set out in more detail in the “Investments” chapter on page 51. **Long and medium-term current assets** decreased by € 9.6 million or 19.4% to € 39.8 million (previous year: € 49.4 million). In this respect, deferred taxes increased by € 2.9 million, whilst other assets decreased by € 11.5 million. Other assets include the statement of discounted customers’ bills in an amount of 6.9 million (previous year: € 19.9 million). This was due to the application of the new IAS 39 derecognition regulations, amended with effect from 1 January 2005. In accordance with the amended IAS 39 the company continues to bear the material risks (risk of default) and rewards arising from discounted customers’ bills. Therefore a derecognition is not permitted before the bill has been fully paid back at the due date. Due to the revised accounting rule, the figures for the preceding years were adjusted accordingly.

In the reporting year **inventories** showed an increase of € 12.2 million or 4.4% to € 288.8 million (previous year: € 276.6 million). Whilst the inventory of raw materials and consumables decreased by € 0.2 million to € 92.3 million (previous year: € 92.5 million), the work-in-progress inventory increased by € 1.7 million to € 89.1 million (previous year: € 87.4 million) and the inventory of finished goods by € 9.7 million to € 104.9 million (previous year: € 95.2 million). The total inventories share in the balance sheet was 30.0% (previous year: 28.5%). In relation to the sales volume the turnover rate of inventories increased from 3.8 to 3.9.

Compared to the previous year, **short-term receivables and other assets** increased by 8.3% or € 26.7 million to € 348.5 million. In this respect, trade receivables increased by € 7.4 million to € 286.8 million due to higher sales figures at the end of the year. Other assets increased by € 19.3 million to € 61.6 million. Other assets include the statement of discounted customers' bills in an amount of € 18.3 million (previous year: € 10.8 million). Compared to the previous year, the ratio of trade receivables to sales remained unchanged at 4.2.

At the balance sheet date, **liquid funds** amounted to € 21.9 million (previous year: € 60.3 million). Thanks to our stringent financial management, the relative share in the balance sheet total dropped from 6.2% to 2.3%.

In the assets structure, the relative share of long and medium-term assets increased by 0.7 percentage points to 31.4% (previous year: 32.1%).

Structure of the assets

In **total equity and liabilities,** the annual profit particularly resulted in an increase in **equity** of € 15.3 million or 6.1% to € 265.8 million (previous year: € 250.5 million). The equity ratio therefore increased by 1.8% percentage points to 27.6% (previous year: 25.8%).

Net indebtedness decreased by € 8.9 million to € 305.1 million (previous year: € 314.0 million). Therefore the ratio of average net indebtedness to average equity (gearing) improved from 125.9% to 114.7% when compared to the previous year.

Long and medium-term borrowed funds decreased by € 47.6 million or 12.5% to € 334.2 million. Their share in the balance sheet total decreased by 4.5 percentage points to 34.8% (previous year: 39.3%). The percentage of **long and medium-term provisions** was 5.2% (previous year: 5.0%). An amount of € 27.5 million (previous year: € 27.7 million) included in long and medium-term provisions pertains to company pension provisions, and an amount of € 22.3 million (previous year: € 20.8 million) to other long and medium-term provisions for obligations arising from personnel. An amount of € 6.9 million (previous year: € 19.9 million) included in long and medium-term liabilities pertains to discounted customers' bills.

Long and medium-term financing resources decreased by € 32.4 million or 5.1% to € 600.0 million in the reporting year. Long and medium-term fixed assets are 198.5% financed (previous year: 202.7%) by funds that are available on a long and medium-term basis.

Short-term financing resources increased by € 23.1 million or 6.8% to € 361.4 million. In this respect, short-term provisions increased slightly by € 0.7 million or 1.0% to € 75.6 million (previous year: € 74.9 million). This includes provisions for risks arising from warranties and retrofittings that decreased by € 0.5 million to € 24.8 million in the reporting year. Short-term liabilities increased by € 22.4 million or 8.5% to € 285.8 million (previous year: € 263.4 million). In this respect, discounted customers' bill increased by € 7.5 million or 69.4% to € 18.3 million.

The total of fixed assets and inventories of € 551.1 million (previous year: € 539.1 million) is 108.9% covered (previous year: 117.3%) by long and medium-term financing resources. When compared to the previous year, the structure of total equity and liabilities showed a 1.8 percentage points increase in equity ratio and an increase in provisions; the liabilities ratio decreased by 2.2 percentage points to 59.3% (previous year: 61,5%).

Structure of total equity and liabilities

Material off-balance sheet financing instruments and future financial obligations are set out in the Notes in the "Liabilities" section starting on page 144 and under "Contingencies and Other Financial Obligations" starting on page 148.

For an illustration of our risk management targets and methods for the hedging of all major types of transactions that are recorded in the accounting of hedging transactions, and of risks arising from price fluctuations, risks of default, liquidity risks and risks arising from fluctuations in the cash flow, each in relation to the use of financial instruments, we refer to the section on risks arising from financing and evaluation included in the Risk Report starting on page 93, and the explanatory notes on "Derivative Financial Instruments" starting on page 149 included in the Notes.

We will continue to pursue our efforts to **reduce indebtedness**, particularly financial liabilities. With a consistent financial management and the expansion of the agency work in the customer financing area, we expect a reduction in trade payables. We are currently also looking into various options to reduce interest expenditure. With the increasing standardisation in the materials area and further globalisation efforts of our procurement we intend to achieve a lasting release of funds in inventories in medium term.

Cash flow

In the evaluation of the **financial position**, great significance is attached to the flow of funds analysis. At € 3.2 million the free cash flow (balance of cash flow from running operations and of cash flow from investment activities) – excluding investments in financial assets – was positive in the reporting year (previous year: € -6.4 million) and improved by € 9.6 million against the previous year.

Cash flow	**2005** € M	2004 € M
Cash flow from current operations	**27.2**	12.8
Cash flow from investment activity	**-24.4**	-20.1
Cash flow from financing activity	**-41.7**	57.0
Changes in cash and cash equivalents	**-38.4**	48.9
Liquid funds as at 1 January	**60.3**	11.4
Liquid funds as at 31 December	**21.9**	60.3

The detailed flow of funds analysis is set out on page 108. Key figures pertaining to the analysis of the financial position are included in the "Group Overview" chapter starting on page 162.

The **flow of funds analysis (cash flow statement)** records the payment flow in a financial year and represents the inflow and outflow of the company's liquid funds. In this process, the use of cash is compared with its source.

Based on the Annual profit for the year, the **cash flow from running operations is indirectly deduced.** It is calculated by adding to the annual profit those expenses that are not set off against any payments, and subtracting from it income that did not result from the receipt of monies. Changes taken into account in this process are adjusted for changes due to foreign currency conversion and changes in the consolidated group. The **cash flow from investment activity** and the **cash flow from financing activity** are each calculated in terms of actual sums paid. Therefore the cash flow cannot be directly deduced from the Consolidated Balance Sheet.

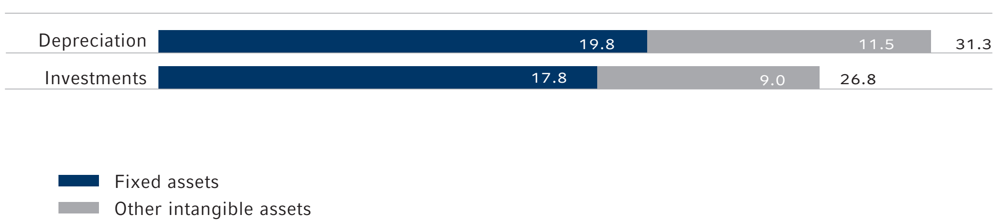
At € 27.2 million, **cash flow from running operations (cash received)** was positive in the reporting year, and exceeded the figure for the previous year by € 14.4 million (€ 12.8 million). Based on earnings before taxes (EBT) of € 25.4 million (previous year: € 12.0 million), depreciation/amortisation of € 31.3 million, net interest expense of € 31.1 million and the increase in trade payables of € 4.1 million all had a positive impact on the cash flow. A further positive effect was achieved by the changes in long-term provisions (€ 1.2 million), in other equity and liabilities, (€ 9.2 million) and by interest received (€ 1.4 million). In the financial year 2005, the changes in inventories (€ 17.2 million), in trade receivables (€ 3.4 million), in other assets (€ 14.6 million) and in short-term provisions (€ 1.7 million) all had a negative impact on the cash flow. Taxes on earnings paid of € 8.9 million and interest paid of € 31.0 million also had a negative impact on the cash flow.

Due to an investment volume that has increased when compared to the preceding year, the **cash flow (outflow of funds) from investment activity** increased by € 4.3 million compared to the previous year. Net investments excluding financial leases increased by 21.4%, amounting to € 24.4 million over the reporting year compared to € 20.1 million in the previous year. Amounts paid out for investments in tangible fixed assets were around € 17.6 million, therefore exceeding the preceding year's figure by 38.6%. Further details are set out in the "Investments" chapter on page 51.

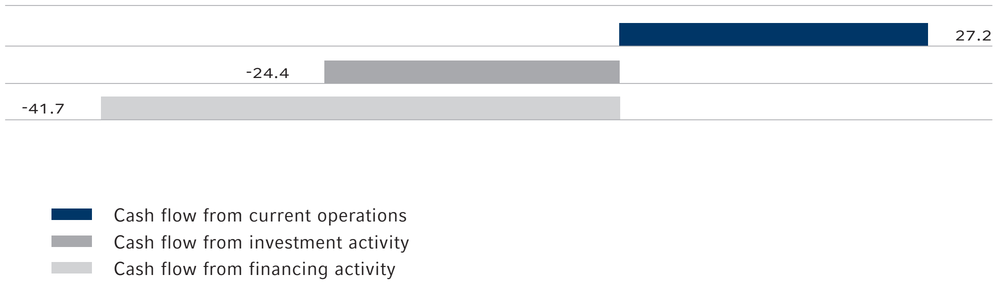
Amounts to the value of € 9.0 million paid out for investments in intangible fixed assets were mainly development services capitalised in the reporting year. There were no sales of companies or other business units during the reporting year.

The **cash flow (outflow of funds) from financing activity** was mainly affected by the payment of short-term financial liabilities of € 41.5 million. With regard to the principal terms of financial liabilities we refer to the explanatory notes on "Financial Liabilities" starting on page 144 of the Notes. Liquid funds at the balance sheet date decreased to € 21.9 million, when compared to the previous year (€ 60.3 million). Our capital requirements are covered by our liquid funds, open cash lines of € 76.6 million and further open credit lines (guaranteed bills outstanding, bills of exchange, factoring) of € 29.9 million.

Flow funds analysis (cash flow statement)
in € million



Composition of the cash flow statement
in € million



The following tables show the Annual Financial Statements of **GILDEMEISTER Aktiengesellschaft** in abbreviated form. The complete Annual Financial Statements and Management Report are set out in a separate document.

Balance sheet of GILDEMEISTER Aktiengesellschaft (HGB)

	2005	2004
	€K	€K
Assets		
Fixed assets		
Shares in affiliated companies	297,202	297,202
Other fixed assets	16,206	16,561
	313,408	**313,763**
Current assets		
Receivables from affiliated companies	281,655	231,445
Other current assets	14,228	48,613
	295,883	**280,058**
Balance sheet total	**609,291**	**593,821**
Total equity & liabilities		
Equity	**313,337**	**286,498**
Provisions	**19,860**	**19,328**
Liabilities		
Financial liablilities	234,684	265,070
Liabilities to affiliated companies	26,651	10,170
Other liabilities	14,759	12,756
	276,094	**287,996**
Balance sheet total	**609,291**	**593,821**

Income Statement GILDEMEISTER Aktiengesellschaft (HGB)

	2005	2004
	€ K	€ K
Sales revenues	16,939	16,921
Other operating income	4,956	11,988
Other income and expenses	-35,781	-49,335
Income from dividend distribution	50,349	34,958
Financial result	-4,671	-5,629
Write down of financial assets	0	-40,367
Profit/loss on ordinary activities	31,792	-31,464
Taxes on corporate income & business	-4,953	-225
Annual result	**26,839**	**-31,689**
Transfer to revenue provisions	-13,400	0
Withdrawals from revenue provisions	0	31,689
Net profit	**13,439**	**0**

In the financial year 2005, the result of GILDEMEISTER Aktiengesellschaft was dominated primarily by income from financial assets, including transfers of profits (€ 48.9 million) and income from investments (€ 1.5 million). No depreciation of financial assets was carried out in the reporting year (previous year: € 40.4 million). The financial result of € -4.7 million improved by € 0.9 million in comparison with the previous year (€ -5.6 million). Tax expenditure of € 5.0 million (previous year: € 0.2 million) is due mainly to corporate income and trade tax expenditure. Current tax losses carried forward were set off in line with legally permitted limits.

GILDEMEISTER Aktiengesellschaft closes the financial year 2005 with an annual profit € 26.8 million (previous year: € -31.7 million). € 13.4 million of which were transferred to revenue reserves. After a balanced net result for the financial year 2004 net profit increased to € 13.4 million.

The Executive Board and Supervisory Board will propose to the general meeting of shareholders, to be held on 19 May 2006, to distribute a **dividend** of € 0.10 per share for the financial year 2005. This equals an amount of € 4.3 million. Moreover, it will be proposed to the general meeting of shareholders to carry forward the remaining balance of retained profits of GILDEMEISTER Aktiengesellschaft amounting to € 9.1 million to new account.

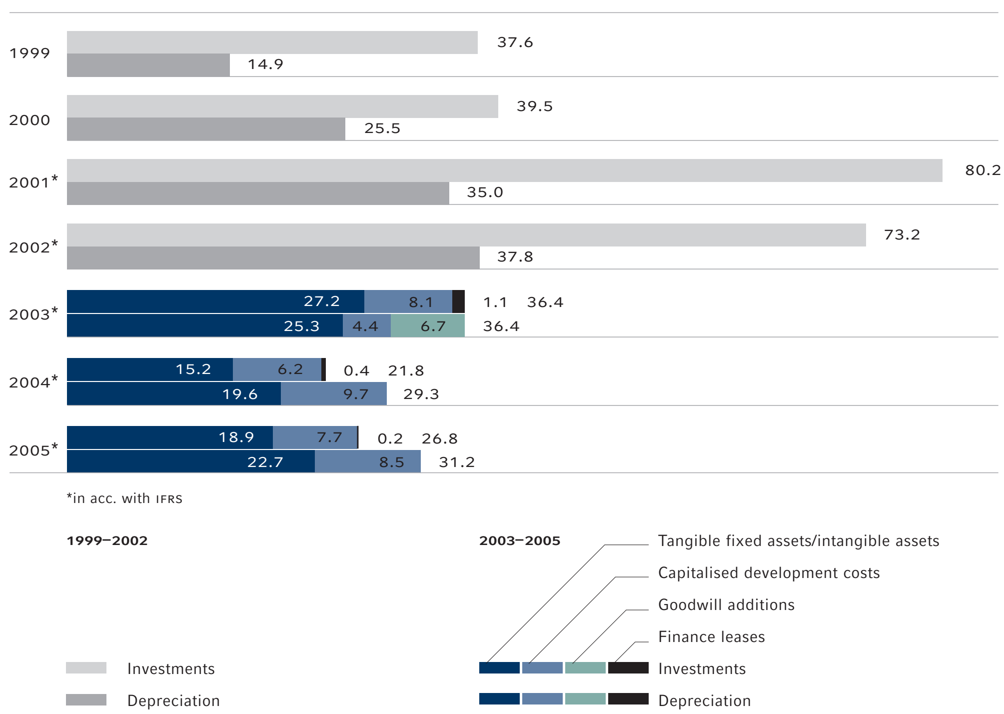
Investments

With regard to investments, we stayed below the planned investment volume of € 30.0 million thanks to a consistent cost management. In the reporting year, investments amounted to € 26.8 million (previous year: € 21.8 million). € 18.9 million of this amount were spent on tangible fixed assets and intangible assets. In accordance with our planning, capitalised development costs amounted to € 7.7 million (previous year: € 6.2 million). Furthermore, assets amounting to the volume of € 0.2 million have been leased (Finance Lease).

In the reporting period, depreciation of fixed assets, including capitalised development costs and finance leases, amounted to € 31.2 million, which is in line with the preceding year's figure of € 29.3 million and as expected. We have continued our consolidation course of the previous years and approximated our IFRS investments to the amount of investments carried out in the reporting year. Amounts invested related primarily to investments in tools and fixtures and to capitalised development costs.

More detailed information on investments in each segment is included in the "Segmental Reporting" chapter starting on page 52.

Investments and depreciation in the GILDEMEISTER group
in € million



Segmental Reporting

"Machine Tools" segment

The "Machine Tools" segment includes the group's business with new machines. It includes the "Turning", "Milling" and "Ultrasonic/Lasertec" divisions. Our range of products consists of 17 lines. Our product range is included in a supplement at the back cover page. We have focused our development and technology expertise from the Turning and Milling divisions in two product facilities respectively. The technological lead at the Turning division is taken by the two product facilities at GILDEMEISTER Drehmaschinen GmbH in Bielefeld, and GILDEMEISTER Italiana S.p.A. in Bergamo. Our full-line product range is divided into eight product lines, ranging from universal and vertical lathes to two-spindle turning centres and multi-spindle automatic lathes through to turning-milling centres for 6-sided complete machining.

DECKEL MAHO Pfronten GmbH and DECKEL MAHO Seebach GmbH are responsible for products in the Milling division. Our range of milling machines and machining centres is combined in seven product lines for CNC universal milling machines, CNC machining centres and milling machines for 5-axis machining, vertical and horizontal machining centres as well as traversing column machines and milling-turning centres.

Also included in the "Machine Tools" segment are the new technologies. The Ultrasonic/Lasertec division is managed by SAUER GmbH. The ultrasonic and lasertec product lines complement our range of new machines.

More detailed notes on products and services in the "Machine Tools" segment are included in the "Production and Logistics, Products and Services" chapter starting on page 78.

Key figures

"MACHINE TOOL" SEGMENT

	2005	2004	Changes 2005 against 2004	
	€ M	€ M	€ M	%
Sales revenues				
Total	**788.1**	743.3	44.8	6
Domestic	**329.3**	344.5	-15.2	-4
International	**458.8**	398.8	60.0	15
% International	**58**	54		
Order intake				
Total	**831.9**	801.8	30.1	4
Domestic	**339.3**	344.0	-4.7	-1
International	**492.6**	457.8	34.8	8
% International	**59**	57		
Order backlog*				
Total	**299.9**	284.4	15.5	5
Domestic	**89.9**	90.0	-0.1	0
International	**210.0**	194.4	15.6	8
% International	**70**	68		
Investments	**18.9**	15.2	3.7	24
Employees	**3,081**	3,074	7	0
plus trainees	**189**	190	-1	-1
Total employees*	**3,270**	3,264	6	0
EBITDA	**54.5**	50.3	4.2	
EBIT	**30.3**	28.3	2.0	
EBT	**18.2**	16.6	1.6	

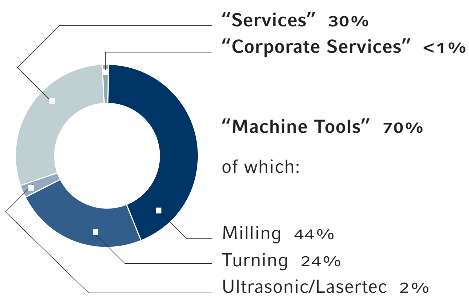
* Reporting date 31 Dec.

The successful product policy in the "Machine Tools" segment has once again contributed to an overall positive business development. **Sales revenues** increased by € 44.8 million or 6% to € 788.1 million (previous year: € 743.3 million). The export rose by 15% to € 458.8 million (previous year: € 398.8 million). The international quota was 58% (previous year: 54%). Domestic sales revenues decreased by € 15.2 million to € 329.3 million (previous year: € 344.5 million). The "Machine Tools" segment contributed 70% to total sales revenues (previous year: 71%). The DECKEL MAHO milling technology represented 44% of total sales revenues (previous year: 41%), whilst the GILDEMEISTER turning technology represented 24% (previous year: 28%). The SAUER ultrasonic and lasertec technologies contributed 2% (previous year: 2%). The **sales volume** also exceeded the figure for the preceding year.

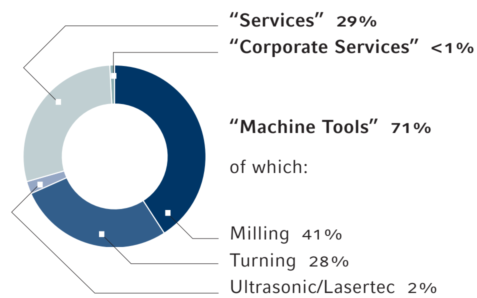
Relating to the total sales revenues of the group the "Machine Tools" as well as the "Services" and "Corporate Services" contributed as follows:

GILDEMEISTER group – sales revenues by segments/divisions

2005: € 1,125.9 million



2004: € 1.051,5 million



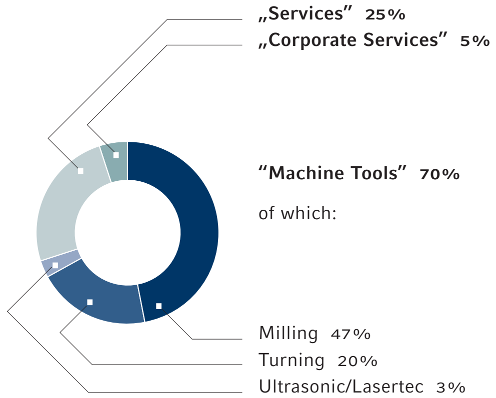
In the reporting year **order intake** increased by € 30.1 million or 4% to € 831.9 million (previous year: € 801.8 million). International orders increased by € 34.8 million or 8% to € 492.6 million (previous year: € 457.8 million). The international share therefore amounted to 59% (previous year: 57%). The intake of domestic order amounted to € 339.3 million (previous year: € 344.0 million). 71% of total orders were attributed to the "Machine Tools" segment (previous year: 72%).

On 31 December 2005, **order backlog** amounted to € 299.9 million (previous year: € 284.4 million), representing a 5% increase. The majority of the order backlog was made up of international orders. Their percentage increased to 70% (previous year: 68%). The absolute increase in the level of orders from abroad was € 15.6 million or 8% to € 210.0 million (previous year: € 194.4 million). Domestic order backlog of € 89.9 million remained in line with the preceding year's figure (€ 90.0 million).

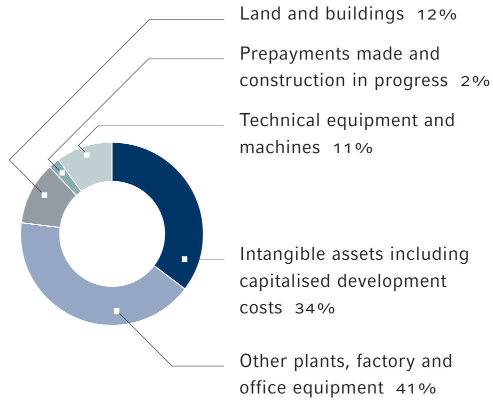
Earnings were up slightly. In line with the increase in sales, **EBITDA** was up 8% or € 4.2 million to € 54.5 million (previous year: € 50.3 million). **EBIT** amounted to € 30.3 million (previous year: € 28.3 million). **EBT** increased to € 18.2 million (previous year: € 16.6 million). In the "Machine Tools" segment depreciation increased by € 2.1 million when compared to the previous year.

The following graphics show the amount and the contribution of investments in each segment and division:

Contribution of each segment/ division to investments in %
2005: € 26.8 million



Investment volume broken down by investment types in %
2005: € 26.8 million



In the **Turning division** investments carried out by GILDEMEISTER Drehmaschinen GmbH amounted to € 0.9 million. The focus was the production ramp up of new machine types. € 0.3 million of the above amount was spent on models and fixtures. GRAZIANO Tortona S.p.A. invested € 0.5 million, which was used primarily to maintain the group companies' operational readiness. GILDEMEISTER Italiana S.p.A. invested € 1.2 million in the reporting year. This includes € 0.4 million for fixtures and models. FAMOT Pleszew S.A. invested € 1.0 million. Focal points of these investment activities were the modernisation and expansion of capacities in mechanical production, funded primarily through an operating lease and supplemented by investments of € 0.4 million. In the Turning division development costs of € 1.8 million were capitalised.

In the **Milling division**, DECKEL MAHO Pfronten GmbH invested € 3.9 million. Focal points were the production ramp up of new machine types and thereof investments in models and fixtures. This required an amount of € 1.5 million. A further € 1.1 million was spent on the modernisation of factory and office equipment. € 0.3 million were spent on the extension of buildings. DECKEL MAHO Seebach GmbH invested € 2.9 million. At € 1.0 million, the focal point was the production ramp up of new machine types and the investment in fixtures and models.

A further € 1.2 million was invested in the expansion and modernisation of mechanical production at the Seebach site, which primarily serves downstream assembly. DECKEL MAHO GILDEMEISTER (Shanghai) Machine Tools Co.,Ltd., invested € 0.9 million in the reporting period. € 0.3 million of this was spent on quality assurance and € 0.5 million on plant and equipment, tools and measuring equipment. In the Milling division development costs of € 5.1 million were capitalised.

In the **Ultrasonic/Lasertec division**, SAUER GmbH invested € 0.5 million. Focal points included selective measures to improve productivity and office equipment and to maintain operational readiness. Capitalised development costs in the Ultrasonic/Lasertec division amounted to € 0.2 million.

At the end of the year, 3,270 **employees** (previous year: 3,264) worked in the "Machine Tools" segment. This represents 62% of total staff at the GILDEMEISTER group. Compared to the corresponding time of the previous year the number of staff remained almost unchanged. Whilst staff levels at FAMOT Pleszew S.A. and the Ultrasonic/Lasertec areas of SAUER GmbH were systematically reinforced, staff numbers at the Bergamo productions site were adapted to business trends. In 2005 the average personnel expense per capita in the "Machine Tools" segment at the domestic production facilities amounted to € 58.5 K (previous year: € 57.3 K). Added to the figure for the international production facilities, this amounts to € 47.6 K (previous year: € 46.7 K).

The "Services" Segment

The "Services" segment is operated by DMG Vertriebs und Service GmbH DECKEL MAHO GILDEMEISTER and its subsidiaries. With its service products and technical services it represents an independent operating area. We offer our customers a comprehensive range of high-quality services and service products from a "one-stop shop" across the entire lifespan of their machine tool. The **Service Support** offers services provided by our highly qualified service staff. Their worldwide network ensures direct contact with the customer and prompt availability. It includes introduction and consulting services for our customers, the traditional maintenance and service activities, the installations and initial training, the vocational and further training provided by DMG Training Akademie GmbH as well as the retrofitting of machines and the used machines business. We continually strive to improve our service provision times and capacities to provide our customers with maximum productivity through a high degree of availability. This is also achieved by our **Service Products** that complete the range of products provided by DMG Vertriebs und Service GmbH. They comprise the DMG spare parts, the innovative software solutions of DMG Powertools, the machine tool components of SACO S.p.A., the setting equipment and tool management of DMG Microset GmbH and the procurement services provided by a & f Stahl- und Maschinenbau GmbH.

Key figures

THE "SERVICES" SEGMENT

	2005	2004	Changes 2005 against 2004	
	€ M	€ M	€ M	%
Sales revenues				
Total	**337.4**	307.6	29.8	10
Domestic	**172.2**	157.8	14.4	9
International	**165.2**	149.8	15.4	10
% International	**49**	49		
Order intake				
Total	**338.3**	311.5	26.8	9
Domestic	**180.9**	164.2	16.7	10
International	**157.4**	147.3	10.1	7
% International	**47**	47		
Order backlog*				
Total	**46.9**	37.4	9.5	25
Domestic	**39.4**	23.5	15.9	68
International	**7.5**	13.9	-6.4	-46
% International	**16**	37		
Investments	**6.7**	4.5	2.2	49
Employees*	**1,935**	1,846	89	5
EBITDA	**46.7**	34.7	12.0	
EBIT	**41.6**	29.6	12.0	
EBT	**28.0**	18.1	9.9	

* Reporting date 31 Dec.

GROUP ANNUAL REPORT: BUSINESS REPORT

The "Services" segment continued to perform as planned and contributed a major share of the GILDEMEISTER group's positive business development. **Sales revenues** increased by € 29.8 million or 10% to € 337.4 million (previous year: € 307.6 million). International sales revenues from services were up € 15.4 million or 10% to € 165.2 million; as in the previous year this represents a 49% contribution to total sales revenues. Sales revenues generated in Germany also increased noticeably: following € 157.8 million in 2004, sales in the reporting year amounted to € 172.2 million, representing an increase of 9% or € 14.4 million. In all, the "Services" segment contributed 30% to the group's total sales revenues (previous year: 29%).

Order intake also performed well, increasing by € 26.8 million or 9% to € 338.3 million (previous year: € 311.5 million). 47% of these were international orders, which totalled € 157.4 million, representing a 7% increase in comparison with the previous year (€ 147.3 million). Domestic orders increased by € 16.7 million or 10% to € 180.9 million (previous year: € 164.2 million). 29% of total orders were attributed to the "Services" segment (previous year: 28%).

On 31 December 2005, **order backlog** amounted to € 46.9 million, again exceeding the figure for the previous year of € 37.4 million.

In the reporting year, the earnings achieved in the "Services" segment were proportionally higher than the rate of growth in sales revnues. **EBITDA** was up € 12.0 million or 35% to € 46.7 million (previous year: € 34.7 million). **EBIT** amounted to € 41.6 million (previous year: € 29.6 million). **EBT** increased to € 28.0 million (previous year: € 18.1 million).

Investments of DMG distribution and service organisations amounted to € 6.1 million in the reporting year (previous year: € 4.4 million); € 2.9 million of this amount were spent on new office equipment. Focal points of this investment activity included an investment of € 0.8 million in the implementation of the first step of our new DMG showroom concept. A further € 1.2 million were invested in the ongoing upgrading and restocking of tools and measuring equipment used by our service staff. In the reporting year DMG Berlin moved into a new technology centre. € 1.1 million were invested in its acquisition and extension. In the reporting year, investments by SACO S.p.A. amounted to € 0.3 million. a & f Stahl- und Maschinenbau GmbH invested € 0.3 million. In the "Services" segment development costs of € 0.6 million were capitalised.

The number of **employees** increased by 89 to 1,935 (previous year: 1,846). Particularly our regional service capacities in Europe and Asia particularly were increased with the aim of better meeting the requirements of our customers. In addition, we specifically reinforced our distribution. Thus, the percentage of staff in this segment was 37% (previous year: 36%). The average personnel expense per capita in the "Services" segment amounted to € 70.1 K (previous year: € 68.6 K).

The "Corporate Services" segment

The "Corporate Services" segment includes GILDEMEISTER Aktiengesellschaft with its groupwide holding functions, such as group strategy, development and purchasing co-ordination, management of overall projects in the logistics and production areas, funding, corporate controlling and corporate personnel management as well as group-standardised IT.

Key Figures

THE "CORPORATE SERVICES" SEGMENT

	2005	2004	Changes 2005 against 2004	
	€ M	€ M	€ M	%
Sales revenues	**0.5**	0.6	-0.1	-9
Order intake	**0.5**	0.6	-0.1	-9
Investments	**1.2**	1.2	0.0	0
Employees*	**67**	64	3	5
EBITDA	**-13.1**	-5.1	-8.0	
EBIT	**-15.2**	-7.4	-7.8	
EBT	**-20.4**	-14.1	-6.3	

* Reporting date 31 Dec.

Sales revenues and **order intake** in the "Corporate Services" segment of € 0.5 million each consist mainly of income from rents. Less than 0.1% of the group's new orders were again attributed to "Corporate Services" (previous year: <0.1%).

EBIT amounted to € -15.2 million (previous year: € -7.4 million). This change in the result is due primarily to the profit arising from contributing the investment of GILDEMEISTER Aktiengesellschaft in DECKEL MAHO Geretsried GmbH to GILDEMEISTER Beteiligungen AG carried out in the previous year. This effect is offset at group level; its corresponding adjustment is shown in the reconciliation column of the Segmental Reporting (starting on page 112).

In the reporting year **investments** totalled € 1.2 million. € 0.5 million of this amount were spent on new office equipment.

On 31 December 2005, 67 **employees** (previous year: 64 employees) were working in this segment, representing an unchanged 1% of the group's staff.

Corporate Situation

GILDEMEISTER faces the global markets' requirements with innovative products and services. In the reporting year, spending on research and development increased by 21% to € 45.7 million. We have introduced an integrated value-added system to all our product and production facilities. The basis of our success is our highly qualified and very committed staff. This is supported by our good personnel training standards and flexitime models.

The GILDEMEISTER Share and Bond

The trading year 2005

Overall, the trading year 2005 in the international and national **stock markets** was good. The European Dow Jones EUROSTOXX 50 index (+21.3%), the British FTSE -100 index (+16.7%), the Japanese NIKKEI 225 index (+42.3%) and the American S&P 500 index (+2.9%) were up. The American Dow Jones Industrial index was down 0.6%. The German stock market indexes closed the trading year 2005 positively. The DAX 30 was up 27.1%, the MDAX was up 36.0% and the SDAX was up 35.2%.

Stock market listing, trading volume and market capitalisation

The SDAX listed GILDEMEISTER share is quoted in official trading at the stock exchanges in Frankfurt, Berlin-Bremen and Düsseldorf and also in unofficial dealing at the stock exchanges in Hamburg, Munich and Stuttgart. The security is registered in the "Prime Standard" segment, which means it meets international transparency requirements.

The average **trading volume** at all the German stock exchanges increased in comparison with the previous year by 46%. In the reporting year the daily volume was around 159,000 shares per day (previous year: 109,000), representing a trading volume of the GILDEMEISTER share at the year-end of around 40.9 million shares (previous year: 28.0 million shares). Based on the total share number of 43.3 million shares this represents an annual volume of 0.9 times (previous year: 0.6 times).

On 5 September 2005 WestLB AG sold their share in GILDEMEISTER Aktiengesellschaft of slightly more than 5%. The GILDEMEISTER shares are now exclusively in portfolio investment **(100% Free Float).**

At the end of 2005, **market capitalisation** amounted to € 253.8 million (previous year: € 225.2 million). A comparison of market capitalisation over several years is shown in the chapter "Group overview/Multiple year overview" on page 163.

Performance of the GILDEMEISTER share

The GILDEMEISTER share gained in value over the year 2005. It started the trading year 2005 at € 5.20 (3 January 2005). Its annual low of € 4.83 was recorded on 6 January. It reached its annual high of € 6.39 on 22 August. Its annual closing price was at € 5.86 (30 December 2005). It is currently quoted at € 7.25 (27 March 2006). The share is analysed by various banks. These are the latest assessments on our share: “Hold” (Bayerische Landesbank, (16 Feb. 2006), “Hold” (Berenberg Bank, 15 Feb. 2006), “Sell” (BHF Bank, 15 Feb. 2006), “Neutral” (HSBC, 15 Feb. 2006) “Outperform” (HVB, 14 Feb. 2006), “Hold” (Bankhaus Lampe, 14 Feb. 2006), “Hold” (WestLB, 09 Feb. 2006) and “Hold” (LBBW, 9 Nov. 2005). Up-to-date studies can be viewed on the Internet or requested from our Investor Relations Team.

The GILDEMEISTER share in comparison with the SDAX January 2005 to March 2006

in %

*01 Jan. 2005 = 100

price trends indexed

Source: Deutsche Börse

Earnings per share

In accordance with IAS 33, earnings per share are determined by dividing the consolidated earnings by the average weighted number of shares, as follows:

Determination of earnings

		2005
Result for the year excluding minority interests	€	13,719,056
Average weighted number of shares	shares	43,302,503
Earnings per share in acc. with IAS 33	€	**0.32**

Earnings resulted from continued business only. There were no dilution effects in the shown reporting period.

Dividend

The Executive Board and Supervisory Board will propose to the general meeting of shareholders, to be held on 19 May 2006, to distribute a dividend of € 0.10 per share for the financial year 2005. With regard to the 43.3 million of voting shares, distribution totals € 4.3 million. In accordance with the "50% exemption" system (Halbeinkünfteverfahren) pursuant to Section 3 no. 40 sentence 1 EStG (German Income Tax Law), only half of the dividends and taxable gains from the sale of capital interests received by private investors (individuals) are subject to tax.

Master data of the GILDEMEISTER share

Security code number		**(ISIN Code)**	**DE0005878003**
		(SCN – Security Code Number)	**587800**
Stock symbol			
Stock exchange			GIL
Reuters	Frankfurt stock exchange		GILG.F
	Xetra		GILG.DE
Bloomberg			GIL GR

Movement of the GILDEMEISTER share

		1999	2000	2001	2002	2003	2004	2005
Registered capital	€ M	56.4	75.1	75.1	75.1	75.1	112.6	**112.6**
Number of shares [1]	M shares	21.7	28.7	28.9	28.9	28.9	43.3	**43.3**
Year-end price [2]	€	6.80	8.20	9.32	3.78	8.22	5.20	**5.86**
Annual high [2) 3]	€	7.30	10.30	9.90	12.07	8.25	8.94	**6.49**
Annual low [2) 3]	€	5.05	6.65	6.20	3.21	2.83	5.00	**4.65**
Annual average market price [2) 4]	€	6.20	8.66	8.78	8.24	5.25	6.52	**5.68**
Dividend	€	0.50	0.60	0.60	-	-	-	**0.10**
Dividend total	€ M	10.9	17.2	17.3	-	-	-	**4.3**
Dividend yield	%	7.4	7.3	6.4	-	-	-	**1.7**
Earnings per share [5]	€	0.76	0.91	0.85	-0.66	-0.13	0.15	**0.32**

1) Share capital was split 1:10 in 1999
2) Prices since 1999 Frankfurt
3) Highest/lowest prices based on variable prices
4) Annual average price based on closing prices
5) Since 2001 pursuant to IAS 33

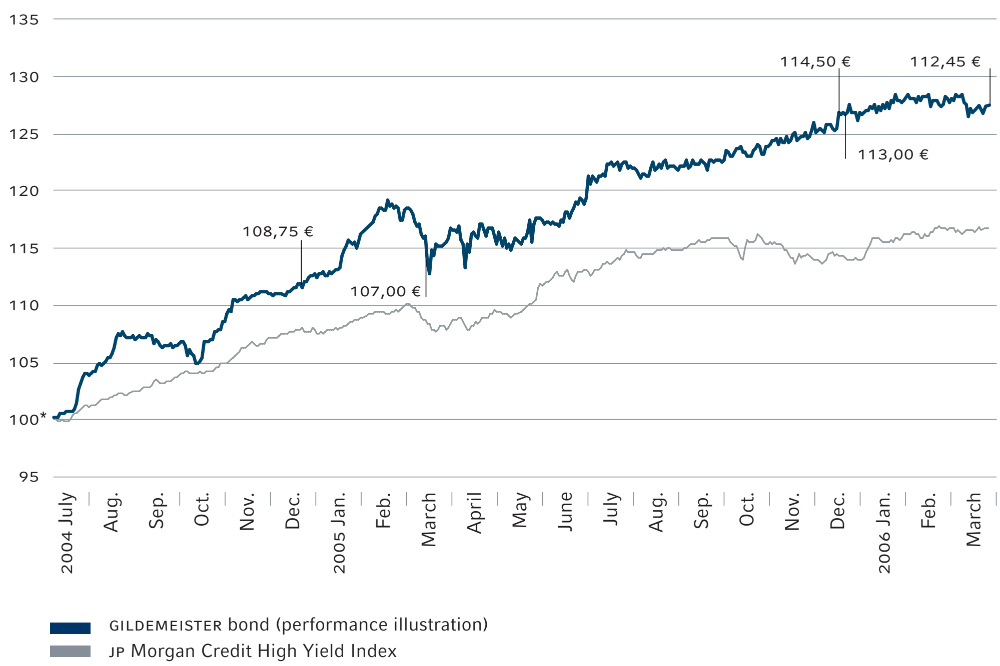
Bond and rating

In July 2004 GILDEMEISTER Aktiengesellschaft issued a secondary bond at a volume of € 175 million. The nominal interest rate (coupon rate) is 9.75% per annum. The bond will mature on 19 July 2011. The corporate rating of GILDEMEISTER was rated Ba3 by MOODY'S and B+ by STANDARD & POOR'S. Taking into account its secondary structure, the credit standing of the bond was rated B2 and B- respectively. The bond is continually observed by bond analysts.

Bond performance

The bond price was quoted above its initial offering price of € 100.00 over the entire year. On 3 January the bond started trading at € 108.75. It reached its lowest annual price of € 107.00 on 23 March. Over the last nine months of the year the price performed well and reached its annual peak of € 114.50 on 23 December. The GILDEMEISTER bond closed the year at a price of € 113.00 (30 December 2005). Our bond is currently traded at € 112.45 (as at: 27 March 2006).

The GILDEMEISTER bond July 2004 bis March 2006
in %



*19 July 2004 = 100
price trends indexed
Source: Deutsche Börse, Bloomberg

Master data of the GILDEMEISTER bond

Security code number	Europe	USA
ISIN	XS0196635402	XS0196669724
WKN	A0BVFC	A0BVFD
Common	19663540	19666972

Key data of the GILDEMEISTER bond

		2005	2004
Month-end price [1]	€	**113,00**	108,45
Monthly high [1,2]	€	**114,50**	108,45
Monthly low [1,2]	€	**106,30**	100,00
Monthly average market [1,3]	€	**111,37**	105,72

1) Bloomberg prices
2) Highest/lowest prices based on variable prices
3) Monthly average price based on closing prices

Investor and Public Relations

Investor Relations work signifies for us an open and continuing exchange of information with the participants of the capital markets. We have continued to increase our activities in the area of financial communication. We presented GILDEMEISTER to institutional investors at many road shows in all the important financial centres in Europe, broadening our investor base further. We used participation at several capital market conferences to groom existing investor circles and to increasingly win new investors in shares and bonds. Following the publication of our quarterly figures, we also explained the business situation and prospects for the industry and the company at presentations and telephone conferences. We once again welcomed more than 1,000 shareholders to our general meeting of share-holders, held on 20 May 2005. This meeting is an important forum for keeping in touch with our shareholders. Once more we have posted the speech made by the Chairman of the Executive Board on our website (“Live-Stream”). Our internet platform is a major component of our financial communication. In the past financial year, 29,331 annual and quarterly reports – including 14,200 in English – were accessed from our website at **www.gildemeister.com.**

Our **Public Relations** activities are a further important part of our corporate communication strategy, which is based on a long-term communication concept, shaping and strengthening GILDEMEISTER's good public image. Our public relations work informs the media and all other interested target groups in a competent, quick, open and reliable way about the current position of the group and its companies. We place a lot of value on a continuing and open dialogue with the national and international economic and trade press, with investors and financial experts as well as with the associations, institutions and decision makers who are important to us. The corresponding budget is set up efficiently, measures are carefully thought out and coordinated with each other, ensuring that an optimal result is attained. In the reporting year, five trade press conferences alone took place, in which 200 journalists took part. They reported worldwide about GILDEMEISTER in more than 950 pages of print. Due to the increased needs on the capital market expenditure in the Investor and Public Relations sector was € 2.1 million (previous year: € 1.7 million).

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Corporate Governance

To the Executive Board and the Supervisory Board, corporate governance is an essential element of management, which is geared towards the lasting increase in company value to the benefit of our shareholders. In accordance with Clause 3.10 of the German Code of Corporate Governance, the Executive Board, also on behalf of the Supervisory Board, reports on Corporate Governance at GILDEMEISTER as follows:

At GILDEMEISTER, corporate governance has, for a long time, represented responsible and transparent management and control of the company. It is a central element of our corporate policy covering all areas of the company. Our Code of Practice includes the standards and rules of responsible corporate management and control.

The Declaration of Compliance regarding the German Code of Corporate Governance pursuant to Section 161 German Companies Act (AktG) was adopted in September 2005. For the first time, the Supervisory Board and the Executive Board were jointly able to make the Declaration of Compliance announcing full recommendation of the guidelines included in the German Code of Corporate Governance as amended on 2 June 2005. Following full compliance with the above guidelines, the Executive Board and Supervisory Board have emphasised their joint commitment to good corporate governance at GILDEMEISTER. Moreover, the chairman of the Supervisory Board has reported on Executive Board members' remuneration 2004 detailed and specifically at the general meeting of shareholders on 20 May 2005.

Adequate remuneration of Executive Board and Supervisory Board

Pursuant to clause 5.4.7. of the German Code of Corporate Governance we report on the remuneration of Supervisory Board members, individually and broken down in components. Pursuant to clause 4.2.4. of the Code the remuneration of Executive Board members is set out in the Notes to the Consolidated Financial Statements starting on page 127 f.

Remuneration for the Supervisory Board of GILDEMEISTER Aktiengesellschaft

The remuneration for the Supervisory Board was defined at the general meeting of shareholders and is regulated under section 12 of the Articles of Association of GILDEMEISTER Aktiengesellschaft.

In the financial year 2005 the fixed remuneration was € 10,000 for each member of the Supervisory Board, € 20,000 for the chairman and € 15,000 for the deputy chairman. The annual fixed remuneration therefore totalled € 135,000 (previous year: € 135,000). Remuneration for committee work in the Finance and Auditing Committee (F&A) totalled € 37,500 (previous year: € 37,500). Each member received € 5,000, the chairman of the committee € 10,000 and the deputy chairman € 7,500. The Personnel Committee and Conciliation Committee were split with effect from 30 November 2005. The reason for this division was the continually increasing work load of the Supervisory Board committees with regard to personnel issues. Pursuant to section 12 of the Articles of Association, the remuneration for members of the new Personnel, Nomination and Remuneration Committee (PNR) equals that for the Finance and Auditing Committee. In 2005 the pro rata temporis remuneration was € 2,410.

In 2005, the direct remuneration of the Supervisory Board was made up as follows:

Remuneration of the Supervisory Board of GILDEMEISTER Aktiengesellschaft

	Fixed remuneration	Committee remuneration Finance and Auditing Committee	Committee remuneration Personnel, Nomination and Remuneration Committee	**Total**
	in €	in €	in €	in €
Hans Henning Offen Chairman SB, Chairman PNR from 30 Nov. 05	20,000	5,000	877	**25,877**
Dr.-Ing. Manfred Lennings Chairman F&A until 20 May 05 (resigned from SB 20 May 05)	3,836	3,836	0	**7,672**
Prof. Dr.-Ing. Uwe Loos (member SB since 20 May 05)	6,164	0	0	**6,164**
Günther Berger Chairman F&A from 20 May 05	10,000	6,164	0	**16,164**
Dr.-Ing. Jürgen Harnisch	10,000	0	0	**10,000**
Ulrich Hocker	10,000	0	438	**10,438**
Prof. Dr.-Ing. Walter Kunerth	10,000	5,000	0	**15,000**
Gerhard Dirr Deputy chairman SB, Deputy chairman PNR from 30 Nov. 05	15,000	5,000	657	**20,657**
Wulf Bantelmann	10,000	0	0	**10,000**
Harry Domnik Deputy chairman F&A	10,000	7,500	438	**17,938**
Alfred Geißler (resigned 1 June 05)	4,164	2,082	0	**6,246**
Norbet Zweng (member since 2 June 05)	5,836	2,918	0	**8,754**
Günther Johann Schachner	10,000	0	0	**10,000**
Peter Oxfart (resigned 31 Jan. 05)	849	0	0	**849**
Rainer Stritzke (member since 1 Feb. 05)	9,151	0	0	**9,151**
Total	**135,000**	**37,500**	**2,410**	**174,910**

Therefore, in the financial year 2005, € 174,910 (previous year: € 172,500) were transferred to reserves for Supervisory Board members' remuneration. Provisions for the long-term variable components were also set up. In accordance with the Articles of Association, the long-term variable component amongst others is based on the future performance of the company and cannot be paid out before the underlying objectives have been accomplished.

Notices by members of the company's Supervisory Board or by other persons subject to reporting requirements, on the acquisition or disposal of shares or related rights of purchase or disposal, such as options, or rights that are directly dependent on the company's stock exchange price, were not received.

Insurances for Supervisory and Executive Board members of the GILDEMEISTER group
GILDEMEISTER has directors' & officers' liability insurances (D&O) and legal expense insurances. Insured persons include all worldwide Supervisory Board members, Executive Board members and managers of the GILDEMEISTER group. Senior members of staff are also insured as far as they can be held liable in accordance with directors' and officers' liability principles. The D&O insurance provides for a reasonable retention amount.

Responsible management of risks
Another element of good corporate governance is the company's responsible management of risks. The GILDEMEISTER early risk management system is subject of the annual audit. Our risk management enables us to systematically identify, assess and control risks and chances. Further details are included in the "Risk Report" chapter starting on page 92.

Close cooperation between Executive Board and Supervisory Board
The Executive Board and Supervisory Board work closely together for the benefit of the company. The Executive Board informs the Supervisory Board regularly, punctually and comprehensively on corporate planning, business development and the risk situation. Target and budget variances in the course of business, and the strategic orientation and development of the group are promptly explained to the Supervisory Board. The Articles of Association provide approval reservations for the Supervisory Board with respect to any transactions of fundamental significance.

Avoiding conflicts of interest
Both the members of the Executive Board and the Supervisory Board are committed to the interests of the company and must, when making decisions and in connection with their functions, neither pursue any personal interests nor request or accept any contributions or other benefits for others nor grant any unjustified benefits for third parties. Such transactions or secondary occupations of the members of the Executive Board must be immediately reported to, and approved by, the Supervisory Board. The Supervisory Board will report any conflicts of interest and their treatment to the general meeting of shareholders. There were no such conflicts of interest or transactions with the company during the financial year 2005, neither with respect to members of the Executive Board nor with respect to members of the Supervisory Board.

Safe-guarding the interests of the shareholders
Shareholders are regularly informed of important dates through a Financial Calendar included in the Annual and Quarterly Reports. These dates are also updated regularly on our website www.gildemeister.com. Shareholders may either exercise their voting rights

themselves in the general meeting of shareholders or through an authorised person of their choice or through a proxy bound by their directives. In accordance with the Act on Corporate Integrity and Modernisation of the Right to Challenge Shareholders' Resolutions (Gesetz zur Unternehmensintegrität und Modernisierung des Anfechtungsrechtes = UMAG) that has been in effect since 1 November 2005, we have adapted the process for registration and authorisation to the general meeting of shareholders to these new methods, by amending the Articles of Association at our general meeting of shareholders on 20 May 2005. We thereby increase the motivation of our shareholders to attend the general meeting of shareholders and exercise their voting rights.

Reporting and auditing of annual accounts

In accordance with the regulations of the German Code of Corporate Governance, it has been agreed with the auditor, KPMG Deutsche Treuhand-Gesellschaft Aktiengesellschaft Wirtschaftsprüfungsgesellschaft, Berlin and Frankfurt am Main, to inform the chairman of the Supervisory Board promptly of any grounds of exclusion or bias that may arise during the audit. It has been further agreed that the auditor shall report promptly on all findings and events arising during the audit that are of significance for the duties of the Supervisory Board. The auditor will inform the Supervisory Board of, or include in the auditing report, any facts found during the audit process that prove the Declaration of Compliance with the German Code of Corporate Governance given by the Executive Board and Supervisory Board pursuant to Section 161 AktG to be incorrect.

Declaration of Compliance regarding the German Code of Corporate Governance

The following Declaration of Compliance pursuant to section 161 German Companies Act (AktG) was made by the Executive Board and Supervisory Board on 8 September 2005. Shareholders can access the declaration on our company's website:

"GILDEMEISTER Aktiengesellschaft will fully comply with the recommendations of the 'Government Commission on the German Code of Corporate Governance', as amended on 2 June 2005 and published by the Federal Ministry of Justice in the official section of the electronic Federal Gazette. Since the last Declaration of Compliance was made on 31 December 2004, GILDEMEISTER Aktiengesellschaft has complied with the recommendations of the "Government Commission on the German Code of Corporate Governance", as amended on 2 June 2005 with the following exceptions:

- The Interim Report as of 30 June 2005 was not made accessible to the public within 45 days following the end of the reporting period (Clause 7.1.2. para. 1 sent. 3).
- The Executive Board members' remuneration was not individually disclosed (Clause 4.2.4. para. 1 sent. 2)."

Suggestions included in the German Code of Corporate Governance

GILDEMEISTER also meets most of the so-called suggestions included in the Code. Deviations from the suggestions of the Code currently exist in the following areas:

General meeting of shareholders: In accordance with the Code, the proxy for the exercise of the shareholders' voting rights in accordance with directives should be available during the general meeting. For organisational reasons, GILDEMEISTER is currently not able to provide this option to its shareholders. The complete transmission of the meeting as webcast event is currently not envisaged. In our opinion, the cost of this would exceed the benefit.

Supervisory Board: To ensure continuity in the work of the Supervisory Board and equality of each Supervisory Board member we do not intend to introduce different terms of office for the shareholder side of the Supervisory Board.

Cooperation between Corporate governance, risk management and capital market communication

At GILDEMEISTER the ongoing development of good corporate governance will remain one of our top priorities. We intend to improve, and adjust to the changing business environment, the cooperation between corporate governance, risk management and communication with the capital markets.

Organisation, Management and Legal Corporate Structure

The GILDEMEISTER group comprises five product facilities at ten production sites, and DMG Vertriebs und Service GmbH and its subsidiaries. GILDEMEISTER Aktiengesellschaft acts as the parent company for these companies. Key functions across all areas of the group are controlled centrally. More detailed information on the companies is included in the "Segmental Reporting" chapter starting on page 52.

The GILDEMEISTER group runs all its companies as profit centres. The group structure illustrated on pages 6 and 7 shows the management and structure. To achieve optimal performance and results, all companies operate according to clear guidelines. All operational processes and sequences are standardised through the IT infrastructure that is coordinated throughout the group. The IT system therefore acts as an integral link within the group. The organisational expenses of GILDEMEISTER Aktiengesellschaft amounted to € 13.3 million (previous year: € 13.7 million).

GILDEMEISTER gears its **corporate governance** towards long-term value added performance. Our strategy is committed to a management of value. To accomplish this objective we use our integrated controlling system. This system enables the target-oriented control and management of the group. In the reporting year, our principal internal target and key performance indicators were the items "earnings before taxes" (EBT) and EBIT, which was adversely affected by imputed interest on fixed capital.

In its corporate communications GILDEMEISTER lays claim to a value-oriented reporting system (**Value Reporting**). The aim is to reduce information asymmetries generated between management and investors so as to enable an easier determination of corporate value. In the Consolidated Financial Statements and Management Report we provide information accordingly, in order to meet the high demands of the capital market. The future value-oriented statements on performance included in our Forecast Report stand as an example.

In the financial year 2005 GILDEMEISTER continued the reorganisation of the group's **legal corporate structure** that was begun in the previous year. Major changes occurred both in the legal corporate structure of the sales and service companies and of the Italian subsidiaries.

In January DMG Vertriebs und Service GmbH was expanded by two companies DMG Istanbul, Turkey, and DMG Russland, Moscow, were established as subsidiaries of DMG Europe Holding GmbH with an investment of more than 99% and a remaining investment held by DMG Vertriebs und Service GmbH. Both companies are expected to consolidate the GILDEMEISTER presence in their respective markets and profit from the growth evident in those regions.

Retrospectively, as from 1 January 2005, DMG Service BAZ GmbH, Geretsried, was integrated into the central service companies in Pfronten and Seebach. The central services organisation thereby reflects the supply plants' new product line responsibility.

Also with effect from 1 January 2005, GILDEMEISTER Aktiengesellschaft transferred its 100% interest in a & f Stahl- und Maschinenbau GmbH to DMG Vertriebs und Service GmbH in line with the company's positioning in the "Services" segment. A management and profit and loss transfer agreement was entered into.

With effect from 29 September 2005 DMG Benelux B.V. transferred 100% of its interest in DMG Asia Pacific Pte. Ltd., DMG Nippon K.K. and DMG Malaysia SDN BHD to DMG Europe Holding GmbH.

As part of the restructuring activities carried out at the Italian subsidiaries, Holding Macchine Utensili S.p.A., the former finance company for the Italian production facilities, merged with GILDEMEISTER Italiana S.p.A. In December the entire real estate of the Italian companies was combined into a fully owned subsidiary of GILDEMEISTER Italiana S.p.A., GRAZIANZO Immobiliare S.r.l.

DMG Benelux B.V. disposed of 100% of its investment in DMG Italia S.r.l. to GILDEMEISTER Italiana S.p.A.

Further details of the changes in the legal corporate structure and a detailed overview of the shareholding relationships at the GILDEMEISTER group as of 31 December 2005 are set out in the Notes to the Consolidated Financial Statements starting on page 154.

Also included in the Notes, starting on page 133, is an overview of all management and profit and loss transfer agreements.

The GILDEMEISTER group has **no major shareholdings**.

DMG Vertriebs und Service GmbH, Bielefeld, a fully owned subsidiary of GILDEMEISTER Aktiengesellschaft, maintains, apart from the 43 sales and service companies, further offices and the following international **branch offices**, which are not legally independent enterprises. DMG Danmark operates as a sales and service branch in Denmark. The sales offices of DMG Vertriebs und Service GmbH in Shanghai, Beijing, Guandong, Chongquing, Shenyang and Xian are authorised to market group products in China.

The following companies also maintain branch offices, which are not legally independent enterprises: DMG Italia S.r.l., Bergamo (Italy), DMG Austria GmbH, Klaus (Austria), DMG Czech s.r.o., Brno (Czech Republic), DMG Nippon K.K., Yokohama (Japan) and DMG Asia Pacific Pte. Ltd. (Singapore).

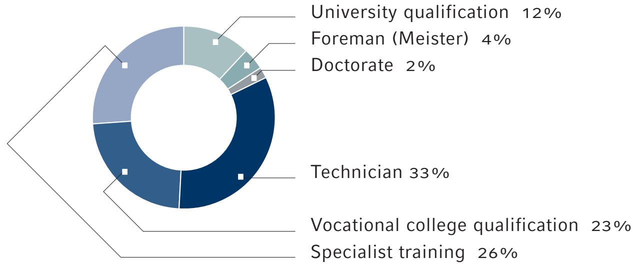
Research and Development

The requirements of the global markets and the expectations of our customers have a major influence on the development of our new products. Our future research and development policy includes the following four long-term, high-priority focal points of: the ultrasonic and laser machining of advanced materials, the integration of technology, the increase in machine dynamics and the increase in customer benefit within the process chain. In the reporting year, € 45.7 million were invested in research and development, thus exceeding the figure for the previous year (€ 37.8 million) by € 7.9 million or 21%. This increase was due primarily to increased customer-specific engineering costs as well as to ongoing completion of our option offer.

In the financial year 2005 the result of our innovation-oriented strategy was reflected in the successful presentation of a total of 22 new developments at numerous national and international trade fairs and exhibitions. Focal point of our activities was the industry's highlight, the EMO. At this most important of trade fairs worldwide we were able to reconfirm our innovative lead by exhibiting the entire range of our newly developed products including 9 world premieres. This means that about two thirds of our current delivery programme includes products that are younger than three years.

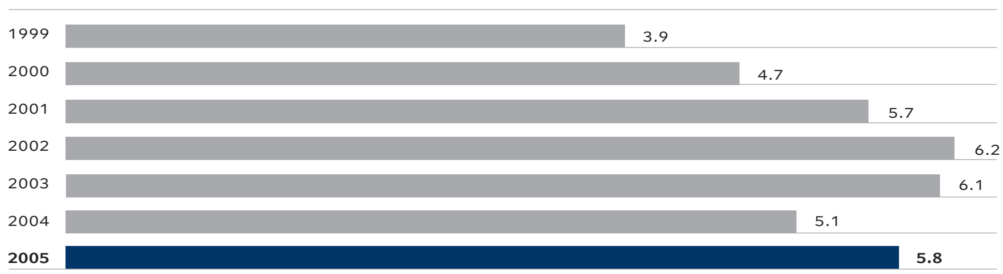
Group-wide qualification structure in the development/ construction area
in %

2005: 408 employees



We have continuously expanded our Central Development Coordination that was successfully introduced over the previous years. We were therefore able to further optimise both the coordination of development projects across all sites and the regular monitoring and controlling system for these projects. We will continue to intensify the modularisation and standardisation of components and sub-assemblies with the aim of developing and producing our machines with an even greater emphasis on marketability at a reasonable price. Examples are shown in the ”procurement“ chapter starting on page 75. 408 employees (13% of all staff working in the plants) are currently working on the development of new products, documenting the significance of this area.

Spending on research and development within the GILDEMEISTER group in %*



* of relevant sales achieved in the ”Machine Tools” segment

The significance of our innovative power is evident in the increased number of industrial property rights, such as patents, utility-model and design patents, brands and trademarks, the value of which has been determined in accordance with our internal commercial value method and is estimated at approximately € 260 million. In the reporting year, 21 new industrial property right applications safeguarded our expertise in important key technologies.

In the **Turning division** the product facilities GILDEMEISTER Drehmaschinen GmbH and GILDEMEISTER Italiana S.p.A. presented a total of six new developments. These machines were either produced in the product facility or in one of the group’s production facilities, with optimised logistics, highest quality and best prices in mind. GILDEMEISTER Drehmaschinen GmbH has developed from scratch new product variants for three machines of the CTX line (CTX 310 V6, CTX 410 V6, CTX 510 V6) that will noticeably expand the fields of applications of these product types. With the NEF 600 GILDEMEISTER has built on the successful NEF principle of the fourth generation and noticeably broadened the range of manufacturing options. The CTV 400 *linear* completes our successful vertical lathe line. This machine was designed by GILDEMEISTER Drehmaschinen GmbH specifically for mass production, and safeguards maximum performance through the use of *linear* drives and high rigidity and precision due to its solid cast iron structure. With the newly developed SPRINT 65 *linear*, GILDEMEISTER Italiana S.p.A. complements the CNC automatic lathes line.

Thanks to the use of three dynamic 12-unit turrets, the machine meets complex requirements for productivity and technological performance.

In the **Milling division** the modernisation of the majority of the product programme that was initiated in 2004 was continued with the exhibition of a total of 13 new developments. DECKEL MAHO Pfronten GmbH introduced seven machines in the CNC universal milling machine, CNC universal milling machines and horizontal machining centre lines. For example, the DMU 60, 80 and 100 models of the DMU MONOBLOCK® line were reworked completely. The CNC milling machine range with 5-side/5-axis machining was complemented by the DMU 80 P and DMC 125 FD in the patented DUOBLOCK® construction. The two DMC 70 H and 80 H models of the horizontal machining centre line were developed and exhibited with the use of numerous identical parts and the DUOBLOCK® construction.

Focal points of the research and development activities at DECKEL MAHO Seebach GmbH in the reporting year were the successful presentation of the DMC 635 V, 835 V and 1035 V entry machines. The product segment therefore saw a change of generations, resulting in an increase in productivity of up to 35% for the benefit of the customer. The products of the DMC 635 V line all have in common a consistent C-Frame construction principle, allowing for maximum accessibility and greatly improved chip clearance. The new DMU 50 eVo is equipped with a powerful linear drive and is now suitable for the machining of negative angles, in relation to the setting attachment. The vertical machining centre line was extended by the DMC 75 V which is equipped with integrated workpiece automation. The range of products in the traversing column machine line was completed with the introduction of the DMF 220 *linear* with B-axis.

The **Ultrasonic/Lasertec division** is led by its high level of innovative power. SAUER GmbH continued to expand its leading position with three new developments. The integration of the new ultrasonic actor system enables both hard machining of advanced materials, such as glass, ceramics, metal carbide or composites, and traditional machine milling. In contrast to traditional processes, the Ultrasonic product line is a convincing choice thanks to its higher precision, enhanced performance and optimised workpiece quality in the machining of these advanced materials. For example, the LASERTEC 40 includes optimised software, which is able to increase precision, process quality and long-term stability in laser machining, all at the same time.

Application-oriented innovations will continue to ensure a continuous increase in customer satisfaction with respect to our products. We also safeguard our technological lead with a wide range of modern service products as for example the innovative software solutions of DMG Powertools. Their development will continue to strengthen the “Services” segment.

All products developed in the divisions over the reporting year have been introduced to the market in accordance with our series start-up management. Further details are set out in the “Production and Logistics, Products and Services” chapter starting on page 78.

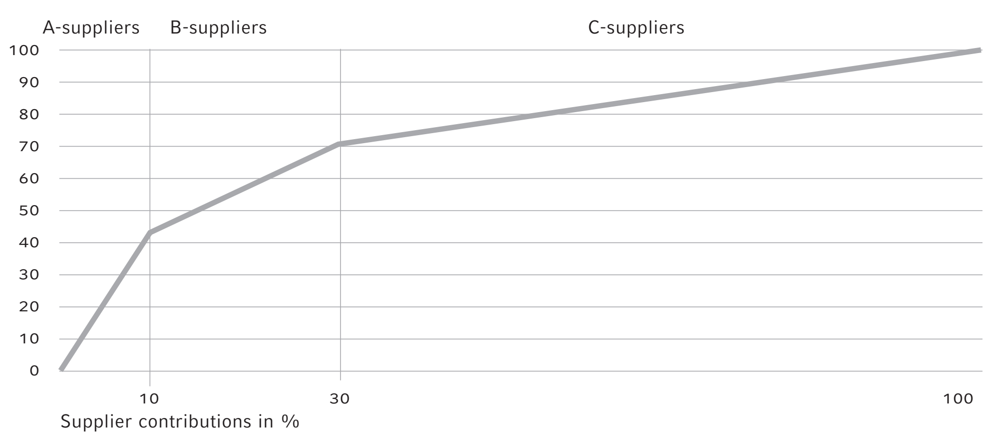
Procurement

In **Purchasing and Procurement** GILDEMEISTER has continued and deepened its partnership-based collaboration with suppliers in the financial year 2005, which led to further positive impacts. Cost of materials and purchased services amounted to € 608.5 million (previous year: € 553.7 million). An amount of € 506.8 million of this (previous year: € 459.7 million) was attributed to raw materials and consumables. The materials quota was 53.1% (previous year: 52.6%).

The group's fifth **Suppliers' Day** was characteristic of the quality of the group's collaboration with its supply partners. At the Pfronten location around 300 participants from the TOP supply companies attended the "Supplier-of-the-Year" awards for the categories innovation, quality, supply performance and overall winner.

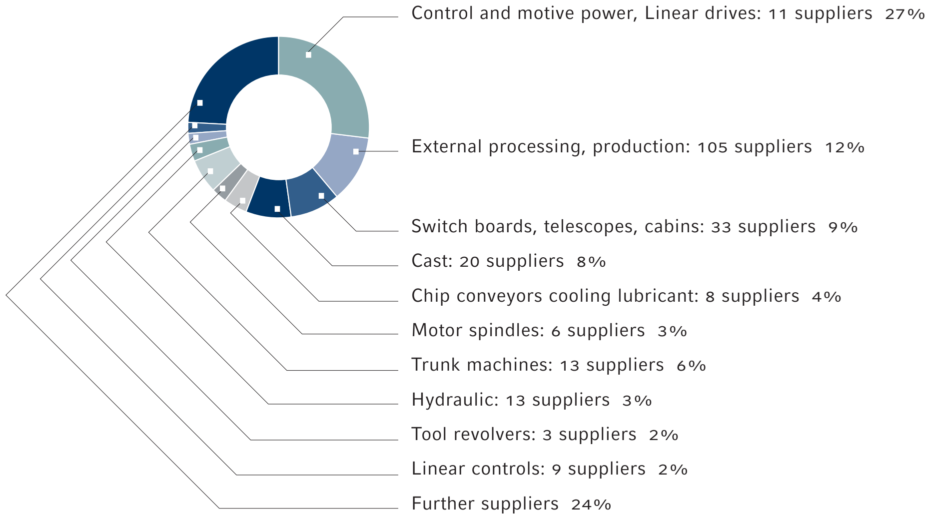
We continue to base our integrated procurement management activities on the following three pillars: coSupply® suppliers' management, materials group management and integrated global sourcing. This allows for a continuous increase in the efficiency of Purchasing and Logistics. Our TOP-50 supply partners, with whom we process 75% of our purchasing volume, are actively integrated by the coSupply®-suppliers'-management. Together with our supply partners we were able to initiate and implement numerous activities **to ensure the procurement of goods** and **to enhance the quality** of start materials. We continued to improve the performance and capacity of our communication platform www.coSupply.de, which was used by our suppliers in more than 37,000 online sessions. Our open and fair evaluation system ensures the transparency required for the ongoing optimisation and streamlining of our suppliers' structure. The **strategic supply partnerships** enable GILDEMEISTER to access the technical expertise of the partners, which strengthens and sustains the company's innovative power. The **early integration of suppliers** into the coSupply® suppliers' management lets us develop supply partnerships on a long-term basis, which in turn **ensures higher supply reliability.**

Structural analysis of the coSupply® suppliers
Supplier's contributions to the purchasing volume in %



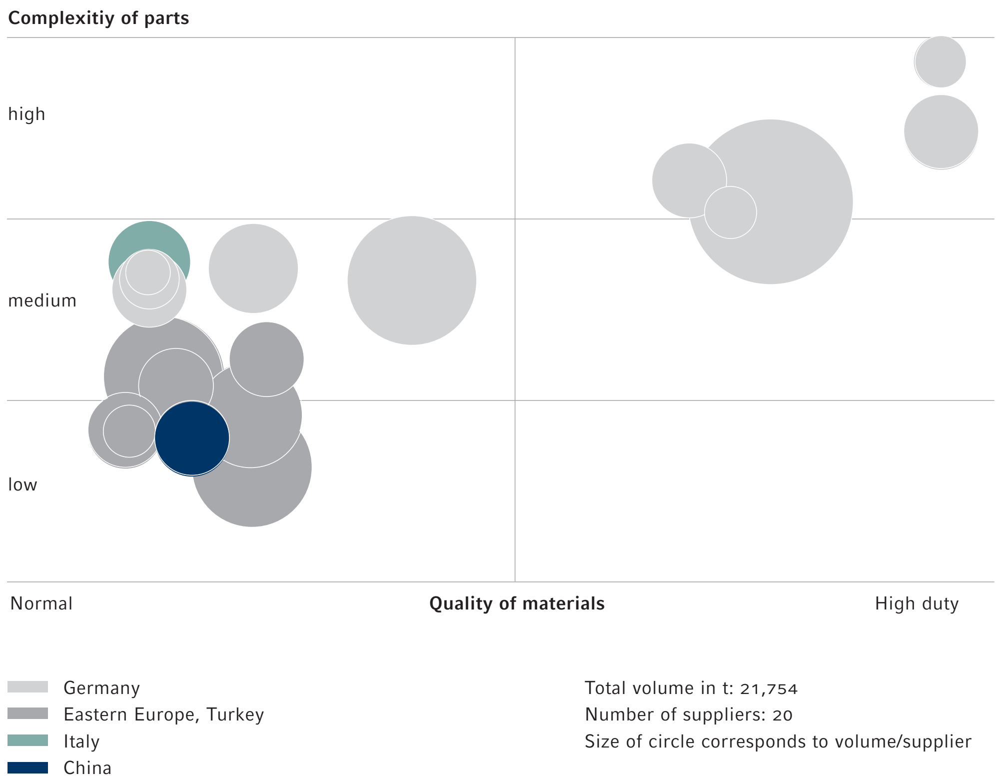
The GILDEMEISTER materials group management coordinates the team-based collaboration between purchasing and technology through strategic purchasing activities. Along with the transfer of knowledge and technology within the group, special emphasis is placed on the synchronising of the plants' procurement activities. The materials group management also supports further activities in the standardisation and modularisation areas. This enabled us to pursue the system integration in various projects (for example in the chip conveyor, motor spindle, hydraulics materials group) and to streamline our delivery programme. This resulted, for instance, in a reduction in the number of relevant hydraulic aggregate suppliers by two thirds. At the same time the number of variants used in this subassembly was reduced by 80% and brought into line throughout the group.

Materials group contributions to the purchasing volume (€)
in %



In the reporting year GILDEMEISTER procured cast components with a total weight of 21,754 tons (previous year: 22,765 tons) from 20 different suppliers. This reduction in weight was achieved primarily from the increased use of spheroidal cast iron, which has – at the same weight – much better mechanical qualities than traditional cast iron. Despite this trend and although prices of raw materials have increased we were able to compensate for the additional expenditure on cast components, and to limit it to 4%, through intensive price negotiations and by gradually moving the sources of supply to East Europe.

Casts suppliers – portfolio



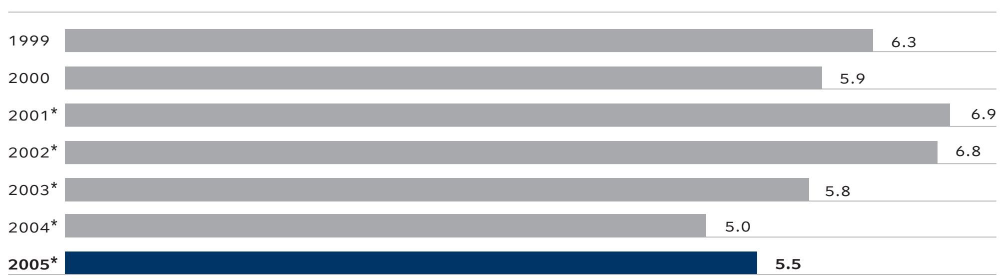
The strategy of International Sourcing for the procurement of cast components was continued and extended to more components and assembly units. Our objectives are for attractive and stable procurement prices and an independent supplier structure for our overseas plants. Due to the further increase in local procurement (Local Content) the group continues to benefit from the cost advantages present in the Chinese procurement market and from a reduction in costs arising from import duties. This meant that we were able to shorten the lead time for selected parts at our Shanghai plant by up to eight weeks. At the same time stock retention was reduced and flexibility increased. We continue to pursue the objective of increasing global procurement of A-components. In the reporting year, for example, for the first time we used tool revolvers and tool magazines manufactured by an Indian supplier in accordance with our specifications and quality standards.

The group purchases strategic production parts, and approximately one in two machines, as pre-assembled trunk machines from FAMOT. We have further strengthened the group's supply network by increasing the mechanical machining capacities by means of three machines included in our product programme.

This means we have installed a further DMU 340 P, a DMC 100 H duoBLOCK® and a DMC 80 H duoBLOCK®. We now have available a highly accurate measuring machine for the exact measuring of large parts, such as machine beds. This will secure and maintain the know-how of our strategic production components. With respect to the storage of goods, we continue to be faced with a trend towards complex technology machines with lower repeat frequency of components and long replenishing lead times. Due to the joint efforts of Purchasing, Production and Logistics, inventories were maintained at a consistent level, whilst sales increased. This resulted in an increase in the rate of turnover pertaining to raw materials and consumables of 10% to 5.5. When compared to the industry, and taking into account the entire stockpiling of spare parts, the average period of storage of raw materials and consumables of 67 days remains at a good level.

Rate of turnover pertaining to raw materials and consumables within the GILDEMEISTER group

*to IFRS



Production and Logistics, Products and Services

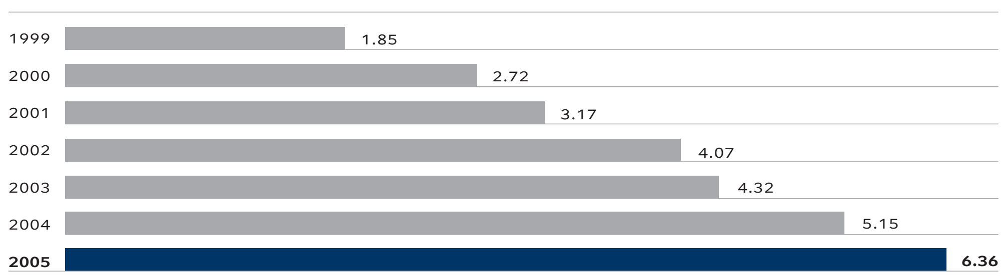
The reporting year saw the introduction of PULLplus in the **Production and Logistics** area. With this, a new integrated value-added system was introduced to all product and production facilities, and our employees were trained accordingly. With this measure we have expanded the GILDEMEISTER production system **PULL** (**P**roduktions- **U**nd **L**ogistik-**L**eistung – performance of production and logistics). This system has been used up to now for the continuous improvement and logistics-related organisation of production processes and sequences. **PULLplus** allows for a further considerable increase in efficiency of our processes, because it ensures consistency of processes across all departments and areas, which in turn safeguards the optimisation of interfaces, for example in production-related areas. With PULLplus we make available to our employees a wide range of practical tools, material and guidelines, which they can use to intensify process optimisation. Therefore, our trained PULLplus managers specifically use methods in accordance with the established continuous improvement process (CIP) principle, adapted to the GILDEMEISTER environment.

This puts the focus on our employees and their **suggestions for improvement**, thereby safe-guarding the sustained success of the value-added system. This resulted in an increase in suggestions for improvement to 21,171 (previous year: 17,113). At an average of 6.36 suggestions per employee working in the plants we achieved an increase of 24% (previous year: 5.15). The total net benefit (benefit of suggestions minus costs of implementation) increased above average. At € 3.6 million it exceeded the figure for the previous year (€ 2.7 million) by one third. Our staff's continuous commitment resulted in GILDEMEISTER occupying, for the sixth successive year, the three leading positions in the German industry ranking run by the German Institute of Business Management (DIB).

The PULLplus projects that were set up in all our plants are in accordance with the TOP process improvement ratios. They are geared towards the requirements of each plant and each area and are underpinned by practical improvement measures defined in workshops.

Regular audits across all plants assess both quantity and particularly quality, i.e. the directly measurable efficiency of the initiated PULLplus activities. The assessment is carried out by an interdisciplinary pool of auditors consisting of PULL and BVW managers of the plants. A regular best-practise benchmark is carried out both internally through our monthly "plant ranking" and externally through benchmark tours.

Suggestions for improvement at the production plants
Number per employee



The division into product and production companies that was introduced in the previous year allows for an optimised focus on the core expertise of each facility. We will continue to pursue our innovation-orientated strategy in order to secure our technological supremacy against global competition. This strategy is always implemented with the development and ramp-up of **new products**.

The technological lead at the **Turning division** is taken by the two product facilities at GILDEMEISTER Drehmaschinen GmbH in Bielefeld, and GILDEMEISTER Italiana S.p.A. in Bergamo. We offer our customers a worldwide unique production programme for lathes, ranging from universal turning machines through to CNC multi-spindle automatic lathes.

In the reporting year GILDEMEISTER Drehmaschinen GmbH began serial production of the successful 4th generation NEF line. Both the NEF 400 and the NEF 600 set new standards for entry machines, boasting high performance and state-of-the-art technology. In accordance with the capacity network of the group, the start of series production of both these types was taken up by the FAMOT and DMG Shanghai Machine Tools production plants, shortly after their development at our product plant in Bielefeld. The required preparations, for example for staff training, were carefully planed and coordinated by the relevant product plant. The success of this synchronised approach is reflected, for example, in a direct minimisation of the SKD set for our Shanghai plant with regard to series production of the NEF 400. Another focal point in the reporting year was the ramp-up of the three new types in the CTX line and of the CTV 400 *linear*. At the same time as the harmonisation of the production processes which took place at the Bielefeld and Tortona sites, further areas were synchronised in the reporting year. We expect important synergies from this measure, particularly in procurement, production and logistics, but also in the research and development area.

GILDEMEISTER Italiana S.p.A. is our production plant for CNC automatic turning machines and for CNC Swisstype automatic turning machines. The continuing trend from mechanical to CNC-multi-spindle automatic turning machines, which is also reflected in our product range and in the current development projects, is resulting in a continuing reduction in the necessary vertical ranges of manufacture for these products. In the reporting year we started a far-reaching optimisation procedure, primarily of the manufacturing processes. By restructuring mechanical processing we have now gained over 400 square metres of production area, which is additionally available for assembly. Together with further activities these measures are also preparing for the ramp-up of the new SPRINT 65 *linear*. This development completes our range of highly productive and technically high-quality products of the new generation in the CNC automatic lathe product line.

In the reporting year FAMOT Pleszew S.A. began production of three new final machines from the entry machine area. With the NEF 400, NEF 600 and DMC 635 V we have developed FAMOT into a qualified producer of final machines, which produces technologically advanced products in high quantities. This resulted in the production of twice as many final machines as in the previous year. At the same time FAMOT remained the group's major supplier of trunk machines, producing a total of 21 trunk machines.

The products and services in the **Milling division** are dominated by the product facilities at the Pfronten and Seebach sites. Our product selection ranges from small CNC universal milling machines to highly productive CNC machining centres and milling-turning centres through to the large universal CNC machining centres for 5-axis/5-sided simultaneous machining, in respect of which DECKEL MAHO is the technological leader. At DECKEL MAHO Pfronten GmbH production was dominated by a total of eight production ramp-up that were carried out shortly after each other. This was possible thanks to the group-standardised Preventive Quality Assurance (PQA) processes and the ramp-up management. This enables us to achieve an early integration of all specialist areas into the adaptation and coordination process. The production starts were supported by a range of PULLplus projects for the optimisation of the procurement, production and logistics processes. The complexity costs in the serial ramp-up were further reduced through the systematic development of the platform concept, for example with respect to the patented monoBLOCK® and duoBLOCK® line. This positive impact was evident in the production ramp-up of the reworked DMU 60, 80 and 100 monoBLOCK® and the new types of the DMC H line.

In the reporting year DECKEL MAHO Seebach GmbH began the production ramp-up of the new vertical milling machine line in the entry area. The success of the DMC 635 V in the market made heavy demands on the speed and particularly the stability of its start of series production. At the same time the DMU 50 that had been exhibited the previous year, developed into the group’s best selling machine. The reporting year also saw the ramp-up of the DMU 50 eVo *linear*, which is equipped with a highly dynamic linear drive and has a great swept volume of the B-axis. The above success has only been possible through the systematic expansion of our capacity network that enabled an almost simultaneous production start-up of the DMC 635 V at the production facilities in Pleszew and Shanghai. PULLplus projects were carried out at the same time so as to harmonise the production and logistics processes and in turn stabilise production. Within our capacity network remit, DECKEL MAHO Seebach continues to produce basic machines for SAUER GmbH.

In the reporting year our Shanghai production facility focused its activities on the optimisation of production processes and product quality, as this is the only way to access the important Chinese market. Collaboration particularly with the European product facilities was further strengthened and expanded. This enabled us to handle the technologically and, in terms of production, logistically demanding ramp-ups for our latest entry-level turning and milling machine generations both concurrently and in the shortest of time. The main basis for this was the system integration of the facility into our ERP system "BAAN" completed in February. This enables the Shanghai site to directly access all relevant product and production data, ensuring an efficient monitoring and controlling system.

At the sites of SAUER GmbH in Idar-Oberstein and Kempten, some of the products we produce in the **Ultrasonic/Lasertec** division are equipped with features that are unique throughout the world. In the ultrasonic technology area, we offer a complete range of products for the machining of technologically advanced materials with a fivefold increase of removal rate over alternative machining processes. Flexible vibration-aided grinding, drilling and milling result in a noticeable reduction in process forces, enabling an excellent surface quality, a reduction in depth damage of the material and longer tool service lives. The use of highly productive linear drives and torque motors, such as in the new ULTRASONIC 20-5 *linear*, and the introduction of the innovative actor tool holder, as used in the new ULTRASONIC 50, highlight our competitive edge in this innovative technology, in which we are at the forefront.

In the Lasertec area, we offer machines for 3D laser removal, laser fine cutting and laser precision boring. Our product assortment stands out due to the highest reliability and productivity. In the LASERTEC 40, for example, which is about to be produced, we use a diode laser, boasting a high level of long-term stability at improved measuring and repeating accuracy.

In the **"Services"** segment we combine all services and products provided by DMG Vertriebs und Service GmbH. Further details of the Service Support and Service Products area are included in the "Services" chapter of the Segmental Reporting on page 56. The range of products of this division is completed with products from SACO S.p.A., whose selection was further optimised and expanded over the reporting year. With our new MPT 65 and MPF 65 draw-in collet chucks, we offer customers in the tool machine area higher precision and repeatability in tool clamping. The product selection is supplemented by components and subassemblies, such as the SACO 35-6 bar loader magazine that was specifically developed for our multi-spindle automatic lathe programme. Optimised logistics allow SACO the supply of bar loaders in a total of three variants to GILDEMEISTER Italiana S.p.A. in Bergamo.

Employees

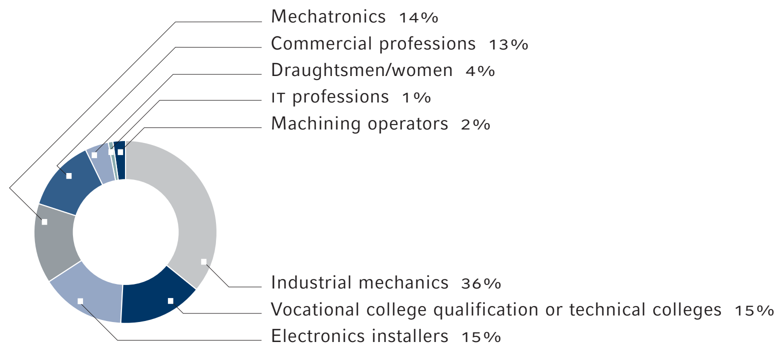
On 31 December 2005, GILDEMEISTER had 5,272 employees (previous year: 5,174), 189 of whom are trainees (31 December 2004: 190). The increased personnel requirement of 98 members of staff arose primarily in the “Services” segment and was due to the increased requirements of our customers. Staff levels particularly in our international sales and service companies were increased. Reductions in the number of staff were directly related to business development in each of the companies. Focal points of these measures were the Geretsried site and our product company in Bergamo.

At the end of year 3,163 employees were working in the national companies and 2,109 in our international companies. The percentage of staff working abroad was 40% (previous year: 39%).

189 trainees have contributed to our continued high standard of vocational training, enabling us to recruit a large number of skilled and executive personnel from our own ranks. A total of 64 trainees were taken on during the reporting year, which is a noticeable increase on the previous year’s number (49). GILDEMEISTER has thus given an even greater number of young people the opportunity of joining our attractive world of work. As in previous years, we have helped improve the vocational training situation of young people working at our production sites. In the “Machine Tools” segment the vocational training share is 5.8%, as in the previous year. We offer vocational training in ten different trades. In addition, we offer courses of study in association with regional colleges of advanced vocational education and technical colleges; this collaboration is constantly being improved.

Training in the GILDEMEISTER group
Allocation by fields
in %

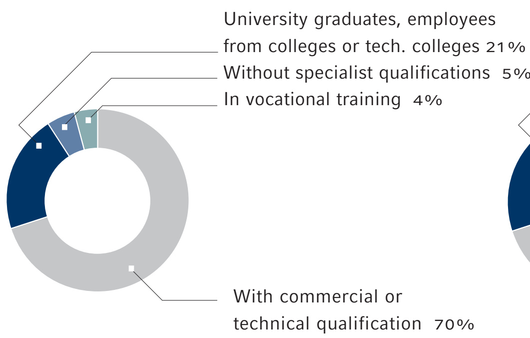
2005: 189 trainees



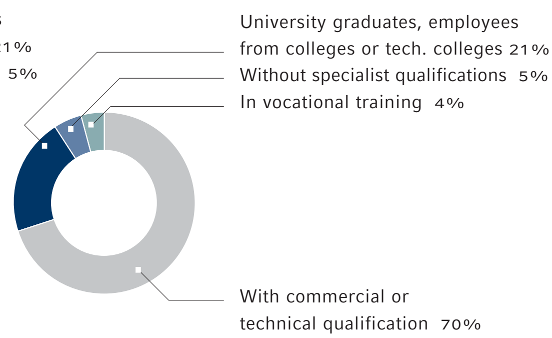
The qualification structure of our employees demonstrates that specialist vocational training enjoys a very high status in the GILDEMEISTER group:

Qualification structure of employees in the GILDEMEISTER group

2005: 5,272 employees



2004: 5,174 employees



As illustrated by the figures in the graph, the qualification structure has not changed since the previous year. 95% of our employees have a professional qualification or are currently in training.

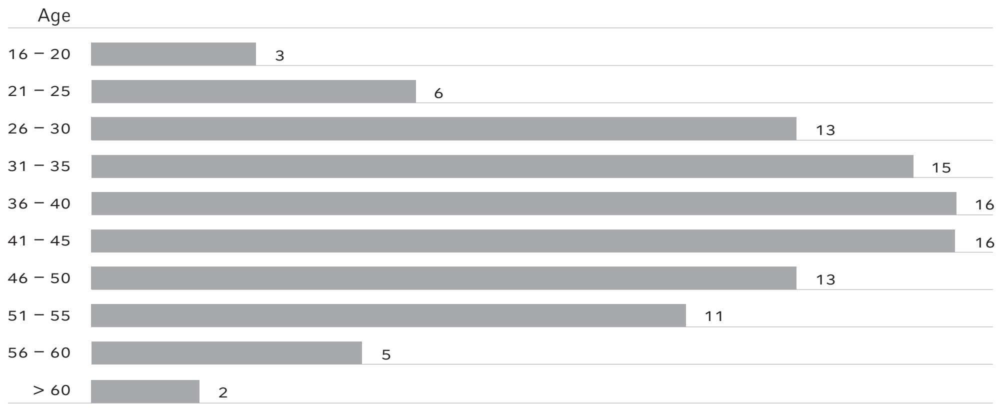
The number of employees taking part in further training has increased further since the previous year and, with 2,518 employees, represents 48% of total staff (previous year: 44%). One of the most extensive training activities in the reporting year was the qualifying of our domestic and foreign sales and service employees for the new machine generations and the familiarisation and qualifying of newly appointed staff. A further focus includes the training activities in IT and languages. A total of € 2.7 million (previous year: € 2.3 million) was spent on further training.

In the reporting year personnel costs amounted to € 295.9 million (previous year: € 282.5 million), which is 4.7% above the figure for the previous year. Of this, € 246.9 million were attributed to wages and salaries (previous year: € 234.9 million); € 45.7 million to social insurance contributions (previous year: € 44.2 million) and € 3.3 million to pension plan expenses (previous year: € 3.4 million). This increase of € 13.4 million was due primarily to the increases in standard wages, to extrawork pay and to the increased number of staff.

As part of our part-time retirement plan, GILDEMEISTER has entered into 123 parttime retirement agreements (previous year: 138), where the so-called 'block model' applies. In this model the whole period of part-time retirement is divided into active and passive phases of equal length. 58 employees were in the active phase, 55 in the passive phase. Participation in the part-time retirement plan has dropped by 11% in comparison with the previous year.

Our staff's age structure is balanced and has changed as follows: 53% (previous year: 56%) of our employees are 40 and younger, and 82% (previous year: 84%) are 50 and younger.

Age structure of employees in the GILDEMEISTER group 2005
in %



In 2005, the number of traffic and operational accidents, 131, was 12% above the previous year's figure of 117. In relation to the total number of staff this is an increase to 2.5% (previous year: 2.3%). The level of sickness of an average 2.7% was noticeably below the preceding year's level (2.8%) and again below the industry average of 3.5%.

During the reporting period, 26 employees at GILDEMEISTER celebrated their 40th anniversary and 58 employees their 25th anniversary. In addition, 104 employees were honoured for their 10-year service with the group. We would like to thank all our employees who are celebrating their jubilee for their loyalty to the company and their unceasing commitment. At this point we would also like to extend our thanks to all of our employees for their exemplary motivation. We also thank our employee councils. Their unbiased mediation between company management and staff has contributed to the implementation of many decisions.

Corporate Communications

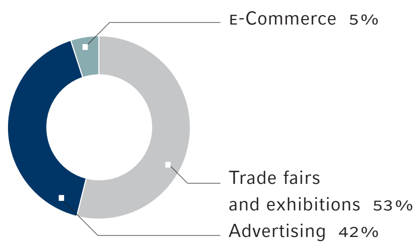
In the reporting year GILDEMEISTER maintained its internal and external communications at their usual high level of excellence. Our communication efforts continue to complement our model of market and value-orientated corporate governance. Thanks to a wide variety of instruments, we succeeded in promoting a strong international market image. Trade fairs and in-house exhibitions, printed information, advertising, our web page, investor relations activities and public relations work, all contributed to this image. Our innovations and the completion of our lines of products remained the focus in this respect. Activities in corporate design, sales, pricing and innovation policy were closely linked to our marketing measures. Market potentials were fully leveraged and new market segments accessed. In the reporting year, GILDEMEISTER spent a total of € 25.6 million (2004: € 23.2 million) on corporate communications work (marketing).

As a manufacturer of capital goods, **trade fairs and exhibitions** play a crucial role for GILDEMEISTER. In the reporting year, DMG was present at 67 events at home and abroad. The highlight of all the trade fairs was the EMO 2005 that took place in September in Hanover, boasting over 23,000 square metres of total exhibition area. In an area of more than 3,500 square metres, 54 new and used machines in production were exhibited, along with an additional 8 machines at the “Maschinenbauer” special show. Our efforts were well worth it: The trade fair business increased noticeably compared to the previous year, which was particularly due to the EMO. A recorded audience of 49,193 represented 36,088 firms and generated a direct intake of new orders of € 259.6 million. This is an increase of more than a third compared to the previous year (€ 189.0 million). At the EMO alone, we were able to sell 451 machines to a total value of € 88.1 million. In the reporting year, GILDEMEISTER invested € 13.6 million (2004: € 12.5 million) in trade fairs and exhibitions, representing 53% of total marketing expenses (previous year: 54%).

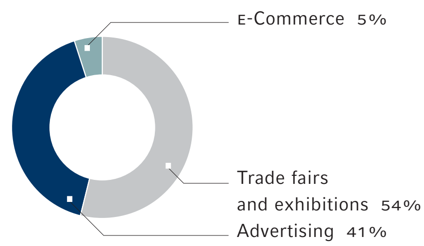
At GILDEMEISTER, **advertising** means primarily the marketing of our products. In the financial year, two issues of our customer journal were published with a total circulation figure of 1.2 million, each in 39 versions and 21 languages. The online versions were also increasingly used. The number of downloads and user sessions was, at around 55,000 more than 65% above the previous year. In the reporting year, a total of three million visitors were registered on our website, which is 62% more than in the previous year. The total volume of brochures was 670,000 (420,000 for the Milling/Ultrasonic/Lasertec area and 250,000 for the turning area). At the EMO alone 19 different current product brochures were available in German, English, French, Italian and Spanish. In the reporting year, we made a start on changing to a new design, which will be used on all brochures during 2006. Product and event mailings likewise continued to be stepped up with a total volume of 2.1 million. This was spread across 19 mailing campaigns with a daily average of 5,670 items. There were 21 different language versions for a total of 46 countries. The NEF/DMU mailing, for example, had a total circulation of 351,300 the year-end mailing was circulated 192,000 times. The NEF/DMU mailing was sent out in 39 versions in 21 languages and the year-end mailing was sent out in 17 versions in 11 languages. Specialist publications were another focal point. 157 advertisements in 55 trade magazines informed readers across the world of DMG products. GILDEMEISTER invested a total of € 10.8 million (2004: € 9.6 million) in the marketing of its products; representing 42% of marketing and corporate communication expenses (previous year: 41%).

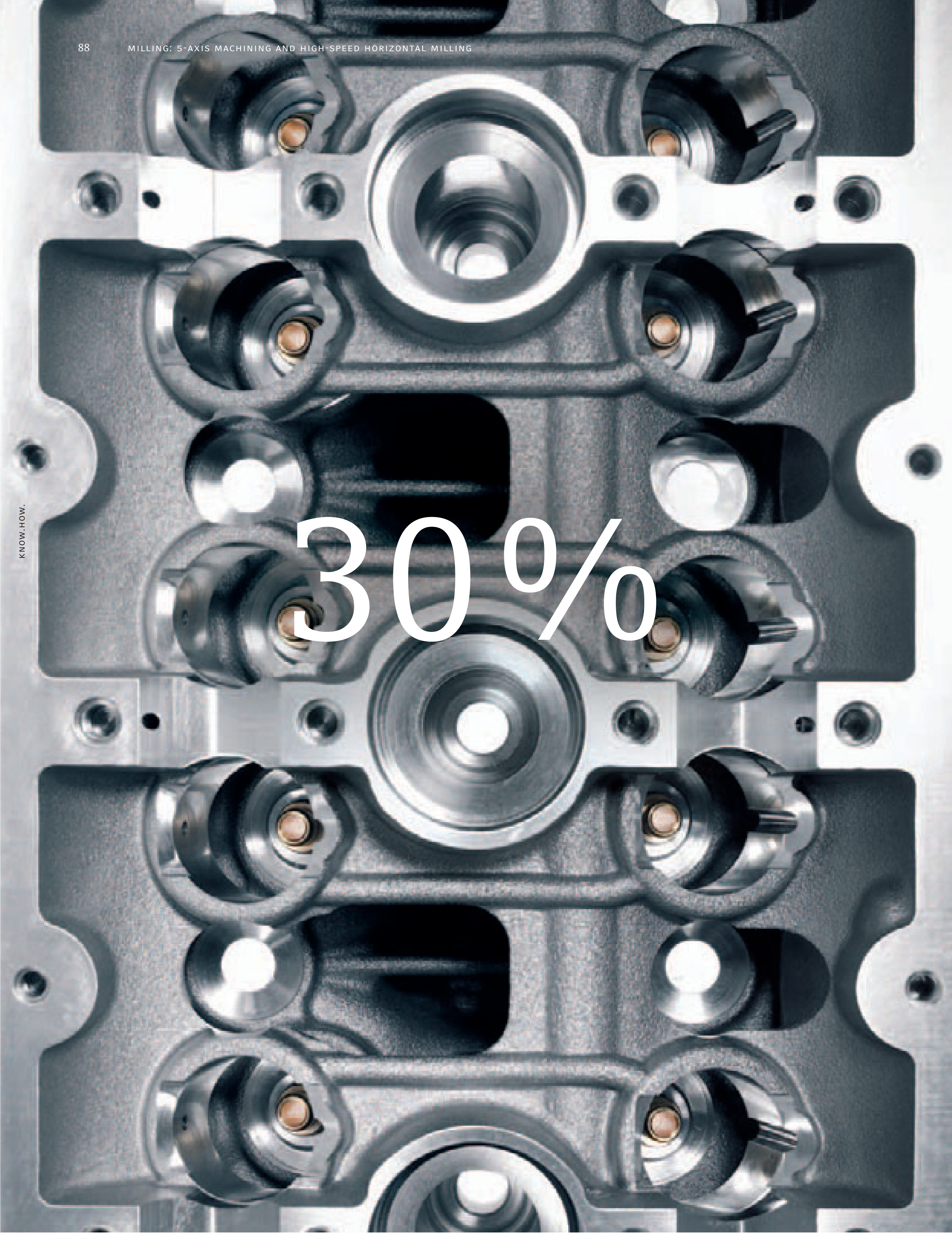
Marketing costs distribution at the GILDEMEISTER group
in %

2005: Total of € 25,6 million



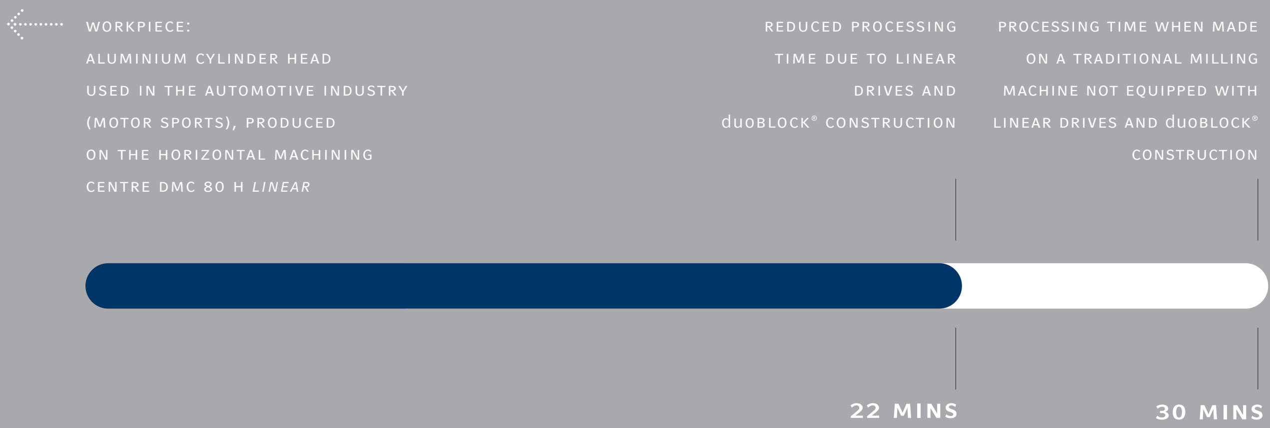
2004: Total of € 23,2 million




30%

Faster with a **100% Know.how** in milling.

UP TO 30% FASTER THROUGH STATE-OF-THE-ART MILLING TECHNOLOGY



The name DECKEL MAHO stands for milling technology at its best. Application-based technology, purposeful innovations such as the duoBLOCK® concept or the latest control technologies – our 7 milling product lines set international standards. Therefore our 5-axis universal machining centres, such as the DMC 80 H *linear* demonstrate their excellence by enabling the highly efficient and fully automated production of complex workpieces in one setting. Their thermo-symmetrical duoBLOCK® construction allows for highest precision and dynamics. The fast rotary pallet changer reduces non-productive time and therefore increases productivity.

Supplementary Report

Overall economic development continued to be targeted at growth over the first months of the current year.

GILDEMEISTER has started the year 2006 confidently. The order intake we achieved for January and February exceeded the figures for 2005. Sales revenues and order backlog were also above the previous year's level.

Economic Development 2006

Overall economic development moved further towards growth during the first few months of this year. The Organisation for Economic Cooperation and Development (OECD) expects the cyclical dynamics to continue over the year 2006. The USA and China remain the driving forces.

Sources: Institute for World Economics (IfW), Kiel; Organisation for Economic Cooperation and Development (OECD), Paris

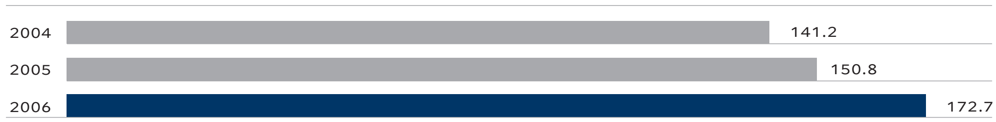
At the beginning of the current year, economic activity in the **German machine tool industry** continued its positive development. Currently available figures do not yet allow for a valid statement on the extent of these trends. In January, sales revenues were up 13% compared to the previous year. According to estimates by the VDW, order backlog is about 5.9 months.

Source: VDW (Association of German Machine Tool Factories)

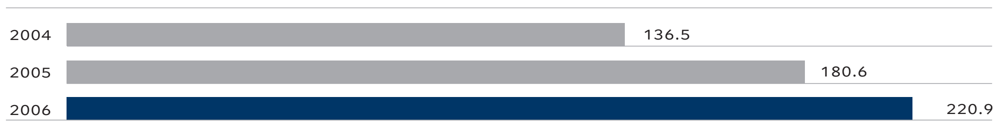
Corporate situation at the end of the reporting year

GILDEMEISTER started the new year confidently, and in January and February recorded an improvement in its **course of business** compared to the previous year. Sales revenues of € 172.7 million was 15% above the figure for the comparable months of the preceding year (€ 150.8 million). Compared to the corresponding months of the previous year, order intake increased by 22 % to € 220.9 million (€ 180.6 million). On 28 February, order backlog amounted to € 395.0 million (figure for the previous year: € 351.6 million). The result for the first two months has also improved compared to the previous year. At this point in time, we consider a more detailed statement on the matter to be premature.

Sales revenues of the GILDEMEISTER group in January and February
in € million



Order intake at the GILDEMEISTER group in January and February
in € million



At the beginning of 2006, the highlight of our **marketing measures** was the traditional in-house exhibition at our Pfronten site. The first two of 16 innovations planned for 2006 were exhibited at this important annual kick-off event. The 38 machines exhibited were greeted with great interest by the 2,793 trade specialists. With 205 machines sold at a total value of € 48.6 million the record result for the previous year was again exceeded.

In the first two months, **selling prices** were raised by approximately 1.5 to 3% depending on market conditions and each particular product.

In the first two month of the financial year 2006 there has been no change in the **organisational structure**.

A further measure in the reorganisation of our **legal corporate structure** was taken in February 2006. Direct investments of GILDEMEISTER Aktiengesellschaft in the productions facilities were transferred to GILDEMEISTER Beteiligungen AG through a non-cash contribution. There were no further changes in the legal structure of the company. No acquisitions or sales of **investments** or operating units were made in the said period.

The in-house exhibition in Pfronten served as an organisational framework for the GILDEMEISTER **Suppliers' Day** on 16 February. For the sixth time the "Supplier-of-the-Year awards" for the innovation, quality, supply performance and overall winner categories were presented from the TOP supply companies. At the in-house exhibitions of DMG Beijing in Beijing, DMG Nippon in Yokohama and DMG München in Pfronten, GILDEMEISTER presented its production programme to an international specialist audience.

Risk Report

The Executive Board has defined principles and guidelines in a risk management system so as to identify risks and take appropriate counter-measures at an early stage. It has provided rules of conduct that are included in a policy and are reinforced by control measures.

Risk management system: Our group-wide risk management system enables us to illustrate changes in the group's overall risk situation using a simple, group-level aggregated ratio. This ratio represents cumulative equity-related risks. Risks are part of our business and a necessary condition for our entrepreneurial success. A rational, controlled approach to risks enables us to utilise opportunities and competitive advantages.

The GILDEMEISTER risk management system uses the group's organisational, reporting and management structures and adds to these specific elements required to secure the proper management of risks. The core elements of the GILDEMEISTER risk management system include:

1. the company-specific Risk Management Manual;
2. a central Risk Management Representative, who is supported by a local Risk Representative from each group company;
3. area-specific Schedules of Risks;
4. the group's overall reporting structure within each area and across all areas;
5. the risk reporting system at group and at company level.

Main risks are regularly identified, hedged against, communicated and monitored

The main risks GILDEMEISTER is faced with are regularly identified, hedged against, permanently monitored and communicated to the Board within the remit of our risk management system. Risks are quantified wherever possible on the basis of reliable methods. As far as a risk can be counterbalanced through the use of efficient measures, its presentation is limited to the residual risk. This quantified residual risk is assessed on a probability of occurrence basis and presented in the Risk Management Report.

Special attention is paid to risks that endanger the future of each company or of the group as a going concern. If such risks to a company as a going concern are identified, the management of that company, and particularly the group executive board, must be notified immediately.

The illustration of the overall risk situation of the group requires the identification of local and central risks, and of group effects:

1. Local risks are individual risks the group companies are exposed to, which can be assessed locally. Local risks are to be documented, assessed and monitored by each group company in the form of risk schedules.
2. Central risks are risks that can, at least in part, only be assessed centrally. This includes risks arising from the group's financing.
3. Group effects usually arise from consolidation requirements. This includes the impairment test of goodwill.

No risks flat jeopardise continued existence to be recognised

General economic risks: Major potential risks for the GILDEMEISTER group result primarily from cyclical influences in those markets that are relevant to the company. Risk reducing activities include the ongoing adaptation of the production plan and the capacities to the development of the order intake. Potential risks also include natural disasters that may result in an increase in the costs of energy or in a delay of supply services. From today's perspective, there are no risks arising from overall economic development that would jeopardise GILDEMEISTER as a going concern.

Section risks: GILDEMEISTER handles the risks arising from cyclical section trends through its technological superiority, which was confirmed at the EMO, an attractive production programme and extensive clientele. We do not therefore expect any major adverse effects to our income, financial and net worth position. Risks continue to arise from the aggressive pricing policy of Asian suppliers. Due to increasing concentration resulting from this the machine tool industry may see a further restructuring of international market players. In the medium term we therefore expect an improvement in price quality.

Risks from operative tasks: The continued heavy pricing competition of our products in the international markets is counter-acted by reduced costs, enhanced production and procurement processes and optimised product starts at GILDEMEISTER. One of the key tasks of GILDEMEISTER Aktiengesellschaft is the limiting of **risks from financing and evaluation.** We do not expect any substantial restrictions on business development from the current development of the capital markets and the interest rate level. Currency related risks may arise from our other international activities. We reduce these risks through hedging transactions as part of our currency strategy. Risks arising from sales in foreign currencies are counter-balanced with purchasing and financing transactions in the respective currency wherever possible. The risk position arising from balance sheet items and business transactions is fully hedged. Hedging transactions are entered into by both corporate headquarters and the individual subsidiaries. The hedging instruments permitted in these transactions are stipulated in a currency policy. According to our evaluations

We estimate currency-related risks as being low

currency-related risks are low. In the reported year, the balance of foreign exchange earnings amounted to € 1.4 million. For regulating and controlling of liquidity we leverage instruments of financial planning and analysis that are continuously improved. Our outside financing has been secured on a long-term basis through the issue of the corporate bond, which will mature in July 2011. In addition, we have a syndicated loan facility with a total volume of € 141.0 million, which will mature in June 2007. For this purpose, indices (covenants) were agreed, based on our corporate planning. If any of these covenants are breached, creditors are entitled to terminate the agreement. At the balance sheet date all covenants were observed. We see the risk of a termination of the agreement to be low, mainly because we are planning to refinance the syndicated loan as early as 2006. About three quarters of our outside financing volume is secured against risks arising from changes in interest rates by agreements for long-term fixed interest rate or interest derivatives. A 1% increase in the level of interest rates pertaining to the non-hedged portfolio on the balance sheet date, would result in an increase in interest expenditure of about € 1 million.

The allocation of deferred tax assets to losses carried forward can be adversely affected by tax rate changes and the future profitability of the companies concerned. Due to the financial straits of public authorities in Germany, there is also considerable uncertainty with respect to the future development of tax legislation. According to our evaluations, the risks arising from necessary value adjustments of more than € 2 million are low.

IT risks arise from the increasing networking of our complex systems. We deal with these risks through regular investment in our hardware and software. The risks arising in this area amount to about € 1 million and can be controlled. We think the probability of their occurrence is low.

Personnel risks arise primarily from the fluctuation of employees in key positions, but also in connection with the recruitment, development and layoff of staff. GILDEMEISTER limits these risks through intense further and junior staff training programmes, appropriate remuneration, personnel standby plans and early successor plans. In our view the probability of occurrence of an estimated damage of about € 10 million is low due to the measures described above.

Procurement and purchasing risks result primarily from the loss of suppliers, quality problems and increases in prices. These risks are limited through comprehensive procurement management and close contact with all major suppliers. Following the easing situation in the raw commodity sector, risks arising from increases in prices occur mainly with respect to the prices of material and energy. We handle these risks through a closer collaboration with our suppliers in continuous value analyses and in the joint optimisation of the supply chain. Further measures include the ongoing standardisation of structural parts and components, the expansion of production of components and entry machines in Poland and China and international sourcing. We estimate the purchasing and procurement risk at about € 8 million, whilst the probability of occurrence is low.

Legal risks: The operative business of GILDEMEISTER results in legal risks, particularly with respect of the sale of machine tools and with respect of our services. Faulty deliveries and services may result in warranty and third party liability claims by our customers. Although we strive to monitor these risks through efficient quality management, such claims by our customers cannot always be avoided. To maintain the resulting risks at a manageable and calculable level, we pursue a stringent policy of limiting our warranties and liabilities. On the hand, this is achieved by our general terms and conditions that reduce the above risks. On the other hand, we enter into individual regulations, depending on the specific situation, that take into account the specific contractual circumstances.

Consistent agreement of risks arising from warranty and liability obligations

The consistent agreement of warranty and liability regulations enables us to minimise most risks arising from the operative business. For this purpose we have introduced an efficient contract management system. With an increased sales volume, our provision for warranties and retrofitting decreased by € 0.5 million to € 24.8 million in the reporting year.

Production risks at GILDEMEISTER are permanently monitored via indices pertaining to the assembly and production progress, processing time and processing continuity. This reduces capital tie-up in inventories and diminishes the inventory devaluation risk. In addition, a large number of other quality and production-related codes are employed to monitor possible risks. This includes the contribution margin per machine type and the turnover rate of raw materials and consumables and of inventories. In **Research and Development** risks may primarily arise from budget overruns, abortive developments and increased start-up costs of new products and can reach as much as € 3 million per development project. The continuous improvement of the development controlling system at GILDEMEISTER ensures an early response to risks in this area. We estimate the production risks at about € 12 million, whilst the probability of occurrence is low.

No fundamental changes in the risk situation

Overall risk: No major changes have occurred in the risk situation of the GILDEMEISTER group since the publication of our last report. Due to the fluctuating exchange rate development of the Euro in relation to the US $ and yen, a clear forecast on further developments is currently not possible. The exchange rate relations result in an increase in currency and price risks that may have an adverse effect on the sales of our products and services. However, at the same time they may offer opportunities. These risks are controllable. We are currently not expecting any fundamental changes in the group's risk situation.

Forecast Report

According to economic experts, global economic development will continue to be vibrant throughout the current financial year, with China and the USA remaining the main driving forces. Increasing growth trends are forecasted for Germany.

Current forecasts for the German machine construction industry expect further growth for 2006. Following a 4% increase in the preceding year the German Mechanical Engineering Association (VDMA) is expecting a 2% increase in production. The majority of the VDMA's trade units anticipate moderate growth. With regard to machine tools the ifo Institute and the VDW expect an increase in consumption of 5% worldwide and of 2% in Germany.

Continuing strong economic cycle expected in China

Overall economic development is expected to continue its dynamic development over the current year. The Organisation for Economic Cooperation and Development (OECD) expects this expansion to broaden. The prices of energy and the US dollar exchange rate will remain risk factors. According to estimates by the Institute for World Economics (IfW), global gross domestic product may reach 4.5%. In the **USA** the increase in gross domestic product is expected to be more moderate compared to the previous year. Consumer demand is expected to slow down due to the increase in interest rates for private households. The imbalance on the current account may also have a destabilising effect. The American economy is expected to grow by 3.4%. The positive development in **Japan** is expected to continue. Assuming a permanent improvement in the job market situation, consumption is likely to increase. The growth forecast is around 2.4%. In **China** the lively activity of the Chinese economy is expected to continue. Public measures to save the economy from overheating may result in a slight setback. An 8.5% growth in gross domestic product is forecast. In **Europe** the growth process is likely to accelerate. A pickup in consumption and a revival in investment activity in the manufacturing sector could contribute to this. The growth forecast by the economic researchers for gross domestic product of the Euro countries is 2.0%. In the case of the 25 member strong European Union 2.2% is expected.

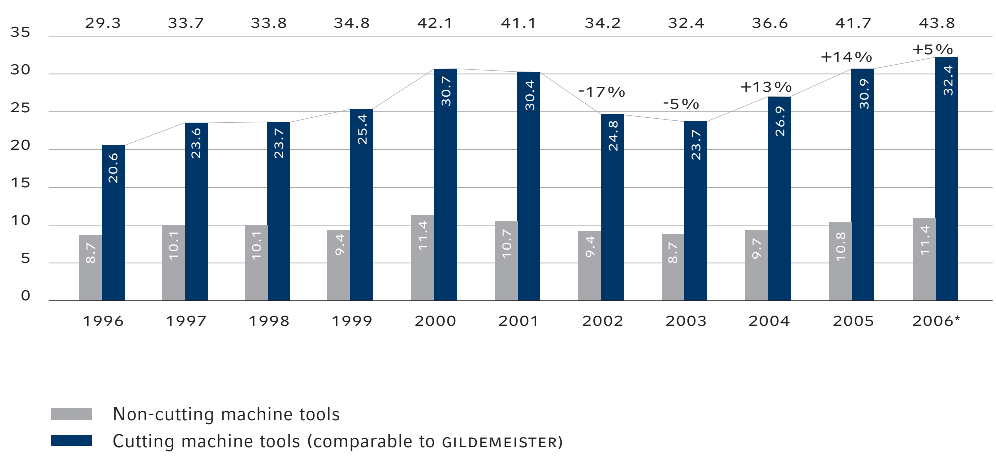
In Germany indicators of an economic recovery become increasingly apparent

In **Germany** indicators of a recovery become increasingly apparent. The growth forecasts have recently been upgraded gradually and are now clearly above the figure for the previous year. The Institute for World Economics (IfW) expects 1.5%, whilst the latest ifo forecast is 1.7%. According to the German Federal Government a 1.8% growth may even be possible. In their autumn survey for 2005 the German Council of Economic Experts on the Assessment of Economic Trends expected growth of 1.0%. For the first time in a long time, the tension in the job market is expected to ease slightly in the current year. However, overall unemployment will remain at a very high level. Progress in public debt is also thought to be likely. It remains doubtful, however, that the deficit quota will be met.

Sources: Institute for World Economics (IfW), Kiel; ifo Institute, Munich; German Council of Economic Experts on the Assessment of Economic Trends, Berlin; Organisation for Economic Co-operation and Development (OECD), Paris

The **worldwide market for machine tools** will continue to grow in 2006. Current forecasts of the ifo Institute and the VDW expect an increase in the **market volume** of 5%. This assessment is based on the positive prospects for China, Japan and other major Asian markets. The American market is also expected to continue to grow. Furthermore, analysts expect an above average growth in the new EU member states. With respect to the **sales volume**, we expect an increase against the previous year. There are currently no statements on the **market and sales potential** of machine tools.

Worldwide consumption of machine tools (1996–2006)
in € billion



Source: VDW worldwide machine tools statistics (excl. parts and supplies; revised figures since 2000)

* VDW estimate

In contrast to the global market, **economic activity** in the **German machine tool industry** will develop at a slower pace: For 2006 the VDW and the ifo Institute do not expect any growth in production and an increase in consumption of just 2%. Exports are expected to decrease slightly by 1%. On a medium-term basis, however, forecasts anticipate an average growth in production and exports of almost 3% p.a. for the years 2007 to 2009. Risks in this forecast are seen primarily in further increases in the prices of raw materials and energy, the exchange rate development, and in the prevailing political conditions.

Source: "The German Machine Tool Industry in the Year 2005": VDW (Association of German Machine Tool Factories)

GILDEMEISTER is well positioned with its innovative products and global market presence

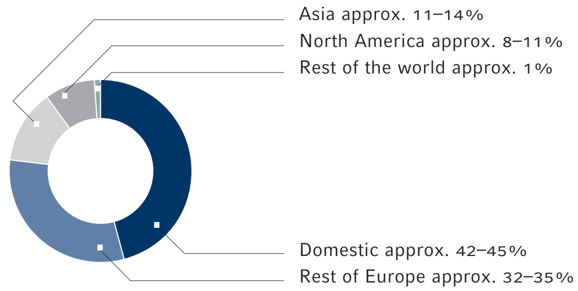
Due to the ongoing concentration process (mergers and acquisitions) in the machine tool industry the **industry structure** will experience lasting changes. As a result of an increasing concentration, the number of producers operating in the world markets will decrease, but those who are left will increasingly operate globally. With its innovative products and global market presence, GILDEMEISTER is well prepared to face future challenges.

For the financial year 2006, we expect further improvement in our orders position. For the first quarter, we expect **order intake** to exceed € 300 million (previous quarter: € 281.0 million). For the year as a whole we expect order intake to exceed € 1.2 billion for the first time. The regional distribution of these orders will shift towards Asia. Influencing factors on **sales prices** include exchange rate risks and the continuing competitive pressure.

For the first quarter, we expect **sales revenues** to exceed € 250 million (previous quarter: € 239.6 million). In view of our order backlog and in line with order intake, we intend to increase our sales figures. Based on a domestic sales contribution of approx. 42-45%, we expect an increase of about 32-35% for the rest of Europe, about 11-14% for Asia and 8-11% for America. The distribution shown is based on the assumption that current economic trends, particularly in Asia and America, will continue this year.

In the first quarter of 2006, **order backlog** exceeded the figure for the previous year; on 28 February 2006 it was € 395.0 million.

Expected sales revenues distribution 2006 of the GILDEMEISTER group by regions
in %



For the first quarter, we expect **EBT** at least to break even. For the financial year 2006 we expect an improvement in EBT and in the annual profit of more than 30%. In this respect, gross profit will increase compared to the previous year. We intend to improve the financial result in 2006. Due to the positive business and performance prospects, we are planning to distribute a dividend for the current financial year. In the medium term we are planning for a reduction in the tax load ratio to about 40%.

This year we are striving for a further optimisation of our **financial structure** and our refinancing potential. We are structuring an **ABS** (asset-backed securities) programme. The ABS programme, with a volume of € 100 million, will run for five years. Implementation is planned for the second quarter of the current year. Given the current positive environment, we are looking into the early refinancing of the syndicated loan facility with a new term of five years and a volume of € 150 million. The object of these activities is a reduction in our cost of finance. Another focal point is the implementation of measures to reduce working capital.

Risk and reward management is continually optimised

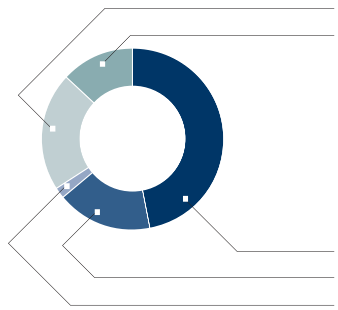
We will continue the optimisation of our **risk and reward management** and will systematically utilise opportunities. For the future risks may particularly arise from cyclical influences and exogenous factors. Opportunities may arise from positive trends in international markets and a stabilisation of the costs of material and energy.

For the financial year 2006 our **investments** amount to approximately € 35 million. The planned investment volume therefore roughly corresponds with the level of planned depreciation. This includes about € 5 million for capitalised development costs. In the Machine Tool segment we are planning for investments in tangible fixed assets and intangible assets of around € 19 million. The investments are intended primarily for the provision of tools, fixtures and measuring equipment for new machine types, maintaining the company's readiness to operate and the modernisation and renovation of production systems and buildings. In the "Services" segment investment activities focused on investments in tools and measuring equipment and in the office equipment of our sales and service companies. We are planning for investments in tangible fixed assets and intangible assets of around € 7 million in this segment. In the "Corporate Services" segment we are planning an investment of € 4 million. Focal points include IT projects and investments in buildings and furnishing at the Bielefeld site. Several of our group companies are expected to profit from this. The **structure of the investments** is well balanced between the varying requirements of the production sites and markets. According to current assessments, no risks are involved with the intended investments.

Structure of the investments is well balanced

Contribution by each segment to the planned investments in intangible and tangible assets
in %

2006: Total € 35 million



Cost advantages by international sourcing

In **Procurement** we will continue to expand and intensify the three pillars: **coSupply®** suppliers' management, materials group management and international sourcing. Thanks to this strategy, we define unambiguous development opportunities for our suppliers and focus on the most efficient partners worldwide. We aim to work with suppliers who have a high level of innovative power and can ensure excellent delivery quality and availability. Together with our suppliers we continuously identify further cost potentials in products and processes, which will be systematically implemented. Within the context of our integrated global sourcing we increasingly rely on suppliers operating in a global environment, who utilise local advantages with respect to quality, costs and performance. GILDEMEISTER will therefore continue to increase the 'local content' of machines produced at the Shanghai site. The site will therefore benefit from the cost advantages present in the local procurement market, in particular with respect to cast and sheet metal parts and simpler machine components.

Our materials group management pursues a value-added optimisation strategy and pools cross-group activities. Due to the series start of new machine types with improved machine bed features, the purchasing share for high-quality spheroidal graphite iron increases. Focal points in this respect therefore include the procurement of medium and high complexity cast parts of high duty quality such as spheroidal graphite iron. This trend makes new demands on the increased procurement of cast iron from countries in Central and Eastern Europe. As part of its coSupply® campaign, GILDEMEISTER is therefore engaged in the systematic and comprehensive development of suppliers, supporting them in the development of their technological expertise. Our materials group management allows for a pooling of volumes, which will result in a permanent reduction in the **costs of procurement**. In close collaboration with selected suppliers, projects for a reduction in inventory tie-up and an increase in the group's **liquidity** are intensified.

A stable and **reliable supply** of our production, particularly with respect to the 'A' component range of aggregates, modules and subassemblies, is safe-guarded through basic agreements that have been coordinated throughout the group. In accordance with market development, purchase prices and delivery terms might have to be agreed on retrospectively, as required. We expect the **costs of basic commodities** to remain at a high level. In all, we expect the increase in prices of raw materials, such as cast iron and sheet metal, to continue to affect our purchase prices in 2006. In relation to the group's entire purchasing volume we anticipate a rate of price increase of 1–2%. We will continuously deepen the established collaboration between Central Development Coordination and Purchasing. Due to the potentials accessed through the standardisation of subassemblies and components, for example in the chip conveyor, motor spindle, hydraulics materials group, we will continue to reduce the number of suppliers and variants. The 'early supplier involvement strategy', i.e. the early integration of suppliers, enables us to identify and, together with our suppliers, to implement standardisation and integration potentials at an early stage in the product development process. Thanks to this we will profit from our suppliers' innovative power, thus avoiding expensive follow-up costs of development.

In the financial year 2006, our activities in **Production and Logistics** will be led by the continued simplification and standardisation of processes and sequences.

PULLplus forms the basis for increases in efficiency

Our PULLplus value-added system forms the basis for a continuous increase in efficiency. Along with the number of suggestions for improvement per employee, we will increasingly focus on the total net benefit, i.e. the benefit of suggestions minus costs of implementation. The worldwide introduction of our group-wide workflow management system, Front Office, optimises and automates numerous technical processes within the entire order processing chain. Front Office uses existing IT systems, such as the group-standardised BAAN ERP system, and links the required information in process-based tasks. This enables us to coordinate and control the worldwide capacity network from our product facilities so as to achieve a concentration on core expertise and an increase in **production flexibility**. The order control offices that are also integrated into this system ensure the logistics-optimised processing and harmonisation of **capacity utilisation** in the plants. In the absence of generally accepted formulae that can be intelligently applied to assembly plants, we are not able to comment on the quantitative extent of the expected capacity utilisation.

In the financial year 2006 we will expand our products with 16 new developments from the **"Machine Tools" segment**. This will reconfirm our innovative power. In the **Milling division** DECKEL MAHO Pfronten will expand the range of applications of the DMC H and DMC H *linear* line. In the horizontal and vertical machining centre area, additional innovations will further broaden our production programme. DECKEL MAHO Seebach will complete the range of its DMU line with two new machine types that build on the platform principle, thus ensuring a high level of reuseability of the parts selection.

In the **Turning division** GILDEMEISTER Drehmaschinen will expand the range of the CTV line with further variants, which will result in a further strengthening of its position in the vertical lathe area. The GMX line of production milling and turning centres will be further reinforced in the lower price section, allowing for an easier access to this high-performance field of applications.

The **Ultrasonic/Lasertec division** will be reinforced through new products from both the high-speed cutting (HSC) and fine-cutting (FC) areas. This will result in a further expansion of the entry-level sections in the **new processes** lasertec and ultrasonic technology.

We will continue to meet market trends and satisfy customer requirements in all divisions by expanding and enhancing our range of options. In the projects business we expect an increase in customer-specific solutions.

16 newly developed products will be presented in 2006

Throughout the year we will present our newly developed products at international trade fairs, such as the METAV Nord in Düsseldorf, the IMTS in Chicago, the AMB in Stuttgart, the JIMTOF in Tokyo and at the in-house exhibitions of our product facilities.

GILDEMEISTER will strengthen the **"Services" segment** through the further expansion of the innovative service and software product range. We thereby follow market trends and meet the increasing demand for product-accompanying services for all aspects of the machine tool. We will adapt the powerful applications of the DMG Powertools product family to the innovations from the "Machine Tools" segment and will equip them with new functions. Our related range of training activities and user-friendly services will be continuously optimised.

Product lines are continually modernised and added to

In **Research and Development** we continue to keep to our strategic aims and focal points. The continuous modernisation and expansion of product lines in all divisions secures our products' long-term competitiveness. For the financial year 2006 the planned spending volume on R&D amounts to around € 45 million. Our activities in this area are led by market requirements and are coordinated both in terms of time and contents. Along with the continuous improvement in the performance of our products, further focal points of our R&D activities include the integration of technologies, for example by combining milling and laser eroding processes, and also in the turning and milling machine area. The development and improvement of intelligent software products support the performance of our products and results, for example, in a significant increase in machine dynamics. Particularly in the system integration area, we work closely with our TOP suppliers and research organisations in the areas of fundamental research, applied research and experimental development.

The related expenses and the number of employees working in Research and Development are based on the strategic goals mentioned above. We continually develop the expertise of our employees in this area through training measures and thus secure the basis for a further expansion of our technological superiority.

No further changes in the group's **legal corporate structure** are planned for the financial year 2006.

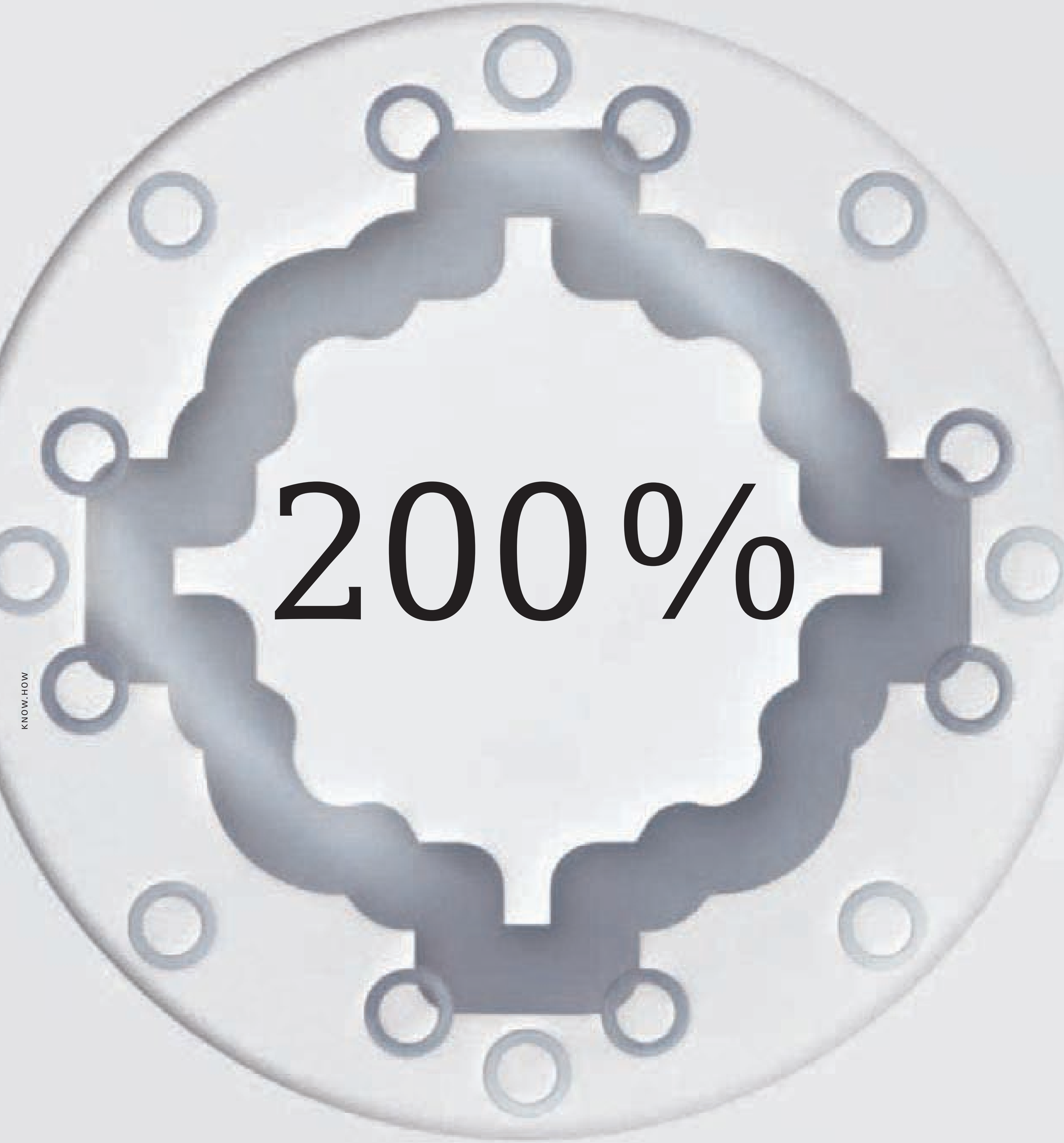
In the interest of a **value-based corporate governance** and along with EBT, we will gradually introduce two new central key performance indicators: return on capital employed (ROCE) and the relative economic value added – difference between ROCE and cost of capital. We have thus adapted to capital market requirements. This concept is based on the assumption that corporate value increases when a positive Economic Value Added is achieved and maintained. ROCE reflects the efficiency of capital employed in form of a relative variable, and arises from the ratio of EBIT to the average working funds. Capital employed can be calculated from the asset side of the balance sheet or the equity and liabilities side of the balance sheet. If calculated from the asset side, it arises from fixed assets and net working capital. For internal control purposes we intend to use the asset side calculation method. For the financial year 2006 we are planning for a further increase in ROCE to about 10%. The cost of capital is calculated as weighted average of the cost of debt and equity valuation in accordance with the WACC method (Weighted Average Cost of Capital). At the GILDEMEISTER group the weighted average cost of capital is 10.2% before tax.

Return on capital employed as a new additional key performance indicator

We will continue to compete for good **personnel**. In accordance with current plans we expect an increase in the number of employees of about 2% for 2006. The increasing globalisation trend will result in an increase in the number of employees particularly at our international subsidiaries. Vocational and further training activities will continue to be one of our top priorities and will enable GILDEMEISTER to recruit skilled and executive personnel from its own ranks. In addition, the "exchange of best practices" amongst the trainees and other employees of the group companies will be further promoted. It gives both young and experienced members of staff the option to work in other countries of the world.

Recruitment of specialists and executive staff from own ranks

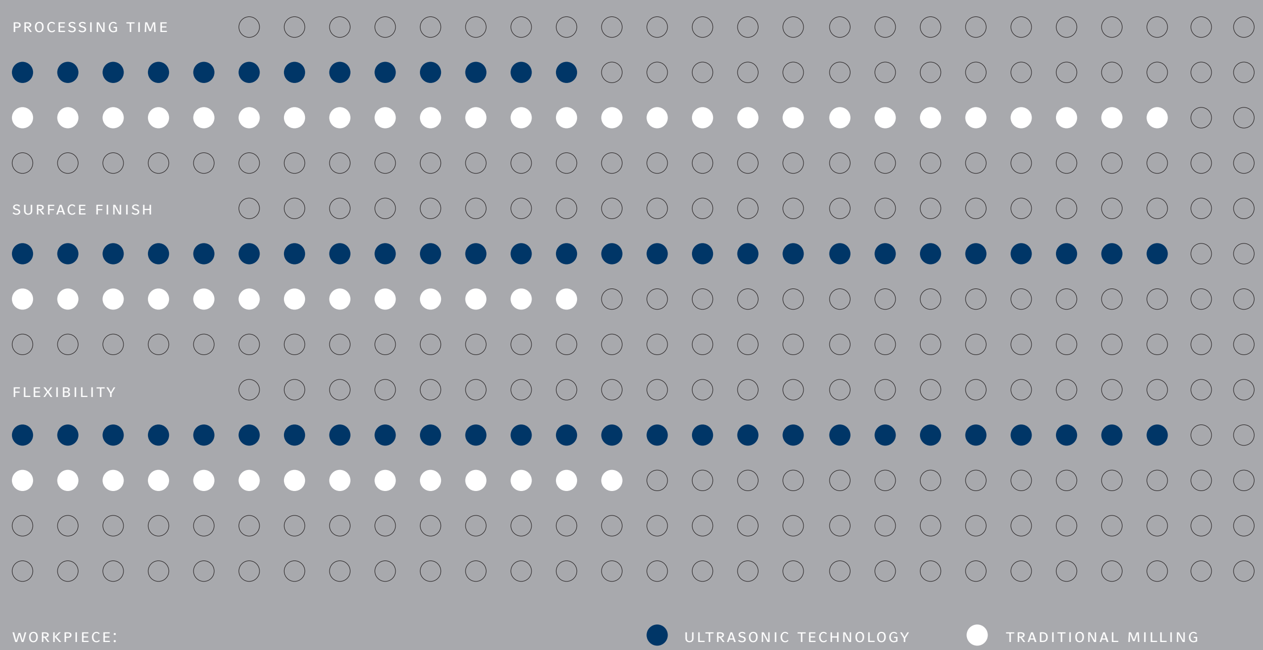
Should the general economic situation prove to be as expected, **GILDEMEISTER** will assume a positive overall business development in 2006. Thanks to the completed restructuring and continued optimisation of our cost and process management we expect a further noticeable strengthening in our profitability in 2006. The measures introduced in previous years will be pursued, and attention will be paid to our growth being both profitable and sustainable. We will continue to meet the requirements of our customers. We will live our cooperative corporate culture and continue to enhance our efficiency through modern production plants and innovative technologies. We will continue to pursue our value and growth-oriented strategy in the **financial year 2007**.



200%

Increased productivity through a **100% Know.how** in ultrasonic technology.

AN UP TO 200% INCREASE IN PRODUCTIVITY IN THE MACHINING OF ADVANCED MATERIALS



WORKPIECE:
CERAMIC SET COLLAR (Ø 28 MM) FOR X-RAY EQUIPMENT, MACHINED ON THE ULTRASONIC 20-5 *LINEAR*

The new Ultrasonic and Lasertec technologies access new markets. The machines from the Lasertec line, for example, enable the economic machining of the smallest parts with filigree cavities. Ultrasonic technology enables machining of advanced materials such as glass, metal carbide or precious stones at noticeably reduced process forces. Our customers therefore benefit from a removal rate that is up to five times higher than that of traditional processes. The ULTRASONIC 20-5 *linear* thus increases dynamics and precision through linear drives and torque motors on four axes. This gives access to a broad range of applications, ranging from the aerospace industry to the medical equipment area.

Consolidated Income Statement
for the period 1 January to 31 December 2005
of GILDEMEISTER Aktiengesellschaft

	Notes	2005 € K	2004 € K
Sales revenues	6	1,125,897	1,051,500
Changes in finished goods and work in progress		11,195	-4,687
Other capitalised payments	7	9,141	6,330
Total work done		1,146,233	1,053,143
Other operating revenues	8	34,606	26,180
		1,180,839	1,079,323
Cost of materials			
Cost of raw materials, consumables and goods for resale	9	506,784	459,693
Cost of purchased services		101,757	94,023
		608,541	553,716
Personnel costs	10		
Wages and salaries		246,942	234,931
Social security contributions, pensions and other benefits		48,984	47,593
		295,926	282,524
Depreciation	11	31,369	29.339
Other operating expenses	12	188,569	171,891
Operating result		56,434	41,853
Other interest receivable and similar income	13	2,069	2,302
Interest payable and similar expenses	14	33,138	32,135
Profit on ordinary activities		25,365	12,020
Taxes on profit	15	11,835	6,444
Annual profit		13,530	5,576
Profit share to other shareholders	16	-189	42
Profit share of shareholders of GILDEMEISTER Aktiengesellschaft		13,719	5,534
Earnings per share in accordance with IAS 33	17	0.32	0.15

Consolidated Balance sheet as at 31 December 2005 of GILDEMEISTER Aktiengesellschaft

Assets

	Notes	As at 31 Dec. 2005	As at 31 Dec. 2004[1]
		€ K	€ K
Long-term assets			
Intangible assets	18	100,928	98,912
of which Goodwill		67,929	67,929
Tangible assets	19	161,191	163,348
Financial assets	20	234	240
Trade debtors	21	1,276	2,249
Other long-term assets	21	10,900	22,403
Deferred taxes	25	27,669	24,797
		302,198	**311,949**
Short-term assets			
Inventories	22	288,777	276,565
Trade debtors	23	286,822	279,466
Other short-term assets	23	61,600	42,317
Cash and securities	24	22,019	60,350
		659,218	**658,698**
		961,416	**970,647**

Equity and Liabilities

	Notes	As at 31 Dec. 2005	As at 31 Dec. 2004[1]
		€ K	€ K
Equity			
Subscribed capital	26	112,587	112,587
Capital provisions		68,319	68,319
Revenue provisions		85,014	68,597
Shares to other shareholders		-138	1,037
		265,782	**250,540**
Long-term liabilities			
Long-term financial liabilities	29	266,509	320,017
Pension provisions	27	27,479	27,723
Other long-term provisions	28	22,317	20,835
Trade creditors	31	1,787	1,325
Other long-term liabilities	31	8,128	7,878
Deferred taxes	25	7,988	4,039
		334,208	**381,817**
Short-term liabilities			
Short-term financial liabilities	29	43,809	34,953
Short-term provisions	28	75,611	74,898
Payments received on account		32,486	27,678
Trade creditors	32	143,106	139,121
Bills of exchange payable	30	16,773	19,427
Other short-term liabilities	32	49,641	42,213
		361,426	**338,290**
		961,416	**970,647**

[1] Adjusted

Consolidated Cash Flow of GILDEMEISTER Aktiengesellschaft

	2005	2004	Changes against previous year
	€ K	€ K	€ K
Cash flow from current operations			
Earnings before taxes (EBT)	25,365	12,020	13,345
Depreciation of assets	31,262	29,339	1,923
Net interest expenses	31,069	29,833	1,236
Change in long-term provisions	1,238	- 1,207	2,445
Other expense/income not affecting payments	762	-3,039	3,801
Change in short-term provisions	-1,729	-9,917	8,188
Income from the disposal of fixed assets	- 899	138	-1,037
Income tax refunds	565	0	565
Income taxes paid	-8,930	-4,051	-4,879
Interest received	1,448	1,488	-40
Interest paid	-30,978	-20,228	-10,750
Changes in current assets			
_ Inventories	-17,244	-12,199	-5,045
_ Trade debtors	-3,399	-22,097	18,698
_ Other assets not from investment or financing activity	-14,605	5,718	-20,323
_ Trade creditors	4,118	15,347	-11,229
_ Other liabilities not from investment or financing activity	9,150	- 8,299	17,449
	27,193	**12,846**	**14,347**
Cash flow from investment activity			
Amounts received from the disposal of tangible assets and intangible assets	2,610	1,216	1,394
Amounts paid out for investments in tangible assets	-17,645	-12,730	-4,915
Amounts paid out for investments in intangible assets	-8,969	-7,773	-1,196
Amounts received from the disposal of financial assets	-425	-833	408
	-24,429	**- 20,120**	**-4,309**
Cash flow from financing activity			
Amounts received from the issue of a loan	0	175,000	-175,000
Amounts paid out for costs of a loan	0	-7,819	7,819
Amounts received for increase in share capital	0	60,064	-60,064
Amounts paid out for increase in share capital	0	-4,789	4,789
Amounts paid out for repayments of (financing) credits	-41,546	-165,481	123,935
Amounts received from investment allowance/grant	89	114	-25
Amounts paid to other shareholders	-258	-107	-151
	-41,715	**56,982**	**-98,697**
Changes affecting payments	-38,951	49,708	-88,659
Consolidation and exchange rate related changes not affecting payments	574	-836	1,410
Liquid funds as at 1 January	60,297	11,425	48,872
Liquid funds as at 31 December	**21,920**	**60,297**	**-38,377**

See explanatory notes included to the Consolidated Financial Statements

Development of Group Equity of GILDEMEISTER Aktiengesellschaft for the period 1 January 2005 to 31 December 2005

			Revenue provisions				
	Subscribed Capital	Capital provisions	Revenue provisions	Difference from currency translation	Market valuation of derivate financial	Shares to other shareholders	**Total**
	€ K	€ K	€ K	€ K	€ K	€ K	**€ K**
As at 01 Jan. 2004	75,087	48,734	68,134	-3,505	-857	1,198	**188,791**
Change in market valuation of derivative financial instrument					795		**795**
Consolidation transactions / other changes						-96	**-96**
Changes in currency				-1,504			**-1,504**
Net income recognised directly in equity				**-1,504**	**795**	**-96**	**-805**
Annual profit			5,534			42	**5,576**
Total recognised income and expense			**5,534**	**-1,504**	**795**	**-54**	**4,771**
Increase in share capital from authorized capital	37,500	19,585					**57,085**
Dividend						-107	**-107**
As at 31 Dec. 2004	**112,587**	**68,319**	**73,668**	**-5,009**	**-62**	**1,037**	**250,540**

			Revenue provisions				
	Subscribed Capital	Capital provisions	Revenue provisions	Difference from currency translation	Market valuation of derivate financial	Shares to other shareholders	**Total**
	€ K	€ K	€ K	€ K	€ K	€ K	**€ K**
As at 01 Jan. 2005	112,587	68,319	73,668	-5,009	-62	1,037	**250,540**
Change in market valuation of derivative financial instrument					-1,891		**-1,891**
Consolidation transactions / other changes						-986	**-986**
Changes in currency				4,589			**4,589**
Net income recognised directly in equity				**4,589**	**-1,891**	**-986**	**1,712**
Annual profit			13,719			-189	**13,530**
Total recognised income and expense			**13,719**	**4,589**	**-1,891**	**-1,175**	**15,242**
Increase in share capital from authorized capital							**0**
Dividend							**0**
As at 31 Dec. 2005	**112,587**	**68,319**	**87,387**	**-420**	**-1,953**	**-138**	**265,782**

See explanatory notes in the Consolidated Financial Statements page 138 et sqq.

Consolidated Fixed Asset Movement Schedule as at 31 December 2005 of GILDEMEISTER Aktiengesellschaft

Acquisition and production costs

Intangible assets
Goodwill
Development costs
Industrial property and similar rights
Payments on account
Tangible assets
Land and buildings
Technical equipment and machinery
Other equipment, factory and office equipment
Payments on account and construction in progress
Financial assets
Shares in affiliated companies
Securities
Total fixed assets

Depreciation

	As at 01 Jan. 2005	Other changes
	€ K	€ K
Intangible assets		
Goodwill	0	0
Development costs	12,607	2
Industrial property and similar rights	38,458	-628
Payments on account	607	0
	51,672	**-626**
Tangible assets		
Land and buildings	49,399	203
Technical equipment and machinery	45,252	379
Other equipment, factory and office equipment	65,600	310
Payments on account and construction in progress	61	17
	160,312	**909**
Financial assets		
Shares in affiliated companies	0	0
Securities	0	0
	0	**0**
Total fixed assets	**211,984**	**283**

As at 01 Jan. 2005	Other changes	Additions	Disposals	Book transfers	**As at 31 Dec. 2005**
€ K	€ K	€ K	€ K	€ K	**€ K**
67,929	0	0	0	0	67,929
36,852	6	7,695	107	4,574	49,020
44,963	-592	897	35	238	45,471
840	0	377	0	-233	984
150,584	**-586**	**8,969**	**142**	**4,579**	**163,404**
174,615	858	2,304	1,381	-252	176,144
60,871	587	2,564	2,645	665	62,042
87,336	718	10,704	3,960	150	94,948
838	123	2,272	56	-568	2,609
323,660	**2,286**	**17,844**	**8,042**	**-5**	**335,743**
208	1	0	0	0	209
32	0	25	11	0	46
240	**1**	**25**	**11**	**0**	**255**
474,484	**1,701**	**26,838**	**8,195**	**4,574**	**499,402**

				Net book value	
Depreciation of the period	Disposals	Book transfers	**As at 31 Dec. 2005**	**As at 31 Dec. 2005**	As at 31 Dec. 2004
€ K	€ K	€ K	**€ K**	**€ K**	€ K
0	0	0	0	67,929	67,929
8,468	0	0	21,077	27,943	24,245
2,996	34	0	40,792	4,679	6,505
0	0	0	607	377	283
11,464	**34**	**0**	**62,476**	**100,928**	**98,912**
5,860	128	-178	55,156	120,988	125,216
4,120	2,542	360	47,569	14,473	15,619
9,366	3,738	-182	71,356	23,592	21,736
431	38	0	471	2,138	777
19,777	**6,446**	**0**	**174,552**	**161,191**	**163,348**
21	0	0	21	188	208
0	0	0	0	46	32
21	**0**	**0**	**21**	**234**	**240**
31,262	**6,480**	**0**	**237,049**	**262,353**	**262,500**

Segmental Reporting in the Consolidated Financial Statements 2005 for GILDEMEISTER Aktiengesellschaft

Segmentation by business segments

	"Machine Tools" 2005	2004	Changes against previous year		"Services" 2005	2004
	€ K	€ K	€ K	%	€ K	€ K
Sales revenues with third parties	788,042	743,321	44,721	6.0	337,356	307,629
EBITDA	54,477	50,284	4,193	8.3	46,738	34,655
EBIT	30,303	28,236	2,067	7.3	41,622	29,610
Net interest income	-12,113	-11,590	-523	4.5	-13,627	-11,494
Profit/loss on ordinary activities	18,190	16,646	1,544	9.3	27,995	18,116
Segment assets [1]	652,064	672,135	-20,071	-3.0	460,012	436,881
Segment liabilities [1]	458,555	497,839	-39,284	-7.9	411,713	391,146
Investments	18,930	15,248	3,682	24.1	6,668	4,534
Depreciation	24,174	22,048	2,126	9.6	5,116	5,045
Employees	3,270	3,264	6	0.2	1,935	1,846

Segmentation by geographical regions

	Germany 2005	2004	Changes against previous year		Rest of Europe 2005	2004	Changes against previous year		North America 2005	2004
	€ K	€ K	€ K	%	€ K	€ K	€ K	%	€ K	€ K
Sales revenues with affiliated companies	275,982	231,705	44,277	19.1	96,006	83,916	12,090	14.4	2,813	2,689
Sales revenues with third parties	641,670	621,438	20,232	3.3	344,923	313,974	30,949	9.9	78,472	70,698
Segment assets [1]	826,056	834,727	-8,671	-1.0	420,987	400,684	20,303	5.1	50,538	39,450
Investments	18,029	13,689	4,340	31.7	7,353	5,884	1,469	25.0	129	154

[1] figures pertaining to the previous year were adjusted

Changes against previous year		"Corporate Services" 2005	2004	Changes against previous year		Transition 2005	2004	Group 2005	2004	Changes against previous year	
€ K	%	€ K	€ K	€ K	%	€ K	€ K	€ K	€ K	€ K	%
29,727	9.7	499	550	-51	-9.3	0	0	1,125,897	1,051,500	74,397	7.1
12,083	34.9	-13,106	-5,132	-7,974	-155.4	-306	-8,614	87,803	71,193	16,610	23.3
12,012	40.6	-15,185	-7,378	-7,807	-105.8	-306	-8,614	56,434	41,854	14,580	34.8
-2,133	18.6	-5,244	-6,750	1,506	-22.3	-85	0	-31,069	-29,834	-1,235	4.1
9,879	54.5	-20,429	-14,128	-6,301	-44.6	-391	-8,614	25,365	12,020	13,345	111.0
23,131	5.3	588,862	591,684	-2,822	-0.5	-739,522	-730,053	961,416	970,647	-9,231	-1.0
20,567	5.3	286,155	297,236	-11,081	-3.7	-475,690	-466,114	680,733	720,107	-39,374	-5.5
2,134	47.1	1,240	1,201	39	3.2	0	773	26,838	21,756	5,082	23.4
71	1.4	2,079	2,246	-167	-7.4	0	0	31,369	29,339	2,030	6.9
89	4.8	67	64	3	4.7	0	0	5,272	5,174	98	1.9

Changes against previous year		Asia 2005	2004	Changes against previous year		Other 2005	2004	Changes against previous year		Transition 2005	2004	Group 2005	2004	Changes against previous year	
€ K	%	€ K	€ K	€ K	%	€ K	€ K	€ K	%	€ K	€ K	€ K	€ K	€ K	%
124	4.6	10,721	8,097	2,624	32.4	756	1,065	-309	-29.0	-386,278	-327,472	0	0	0	0.0
7,774	11.0	51,548	42,380	9,168	21.6	9,284	3,010	6,274	208.4	0	0	1,125,897	1,051,500	74,397	7.1
11,088	28.1	92,082	70,892	21,190	29.9	7,245	3,355	3,890	115.9	-435,492	-378,461	961,416	970,647	-9,231	-1.0
-25	-16.2	1,196	1,073	123	11.5	131	183	-52	-28.4	0	773	26,838	21,756	5,082	23.4

ANNUAL FINANCIAL STATEMENTS

Notes to the Consolidated Financial Statements of GILDEMEISTER Aktiengesellschaft

1 APPLICATION OF REGULATIONS

The Consolidated Financial Statements of GILDEMEISTER Aktiengesellschaft for the year ended 31 December 2005 were prepared in accordance with International Financial Reporting Standards (IFRS) of the International Accounting Standards Board (IASB), London, Great Britain, applicable on the reporting date. All mandatory International Financial Reporting Standards (IFRS) and interpretations by the International Financial Reporting Interpretations Committee/Standing Interpretations Committee (IFRIC/SIC) applicable to the accounting period 2005 in the European Union were applied. The Consolidated Financial Statements were amended by further explanatory notes pursuant to Section 315a German Commercial Code (HGB).

The following notes include statements and comments that, pursuant to IFRS, must be included as Notes to the Consolidated Financial Statements along with the Income Statement, the Balance Sheet, the Statement of Changes in Equity and the Cash Flow Statement. For a better and clearer representation we have summarised individual items in the Balance Sheet and the Income Statement; these are shown separately in the Notes with further explanatory notes.

The Consolidated Financial Statements were prepared in Euros. The report currency is Euro. Unless stated otherwise, all amounts are shown in thousand Euro (€ K).

The Consolidated Financial Statements for the year ended 31 December 2005 and the Group Management Report of GILDEMEISTER Aktiengesellschaft will be lodged at the Commercial Register of Bielefeld District Court (HRB 7144).

The Executive Board of the GILDEMEISTER Aktiengesellschaft has released the Consolidated Financial Statements and Group Management Report on 23 March 2006 for submittal to the Supervisory Board. The Supervisory Board is responsible for reviewing the Consolidated Financial Statements and for declaring whether it approves of the Consolidated Financial Statements.

2 CONSOLIDATED GROUP

Number of fully consolidated companies	31 Dec. 2005	31 Dec. 2004
National	25	25
International	38	35
Total	63	60

At the reporting date the GILDEMEISTER group comprised 64 companies (previous year: 61), including GILDEMEISTER Aktiengesellschaft, 63 of which (previous year: 60) were included in the Consolidated Financial Statements as part of the full consolidation process. GILDEMEISTER Aktiengesellschaft has the direct or indirect majority of voting rights in, or has a dominant influence over, the fully consolidated companies. This includes three lease object companies ("Special Purpose Entities"). Due to the inclusion of the following companies for the first time, the consolidated group has changed since the accounting period 2004:

- GRAZIANO Tortona S.r.l., Tortona, Italy,
- DMG Istanbul Makine Tikaret ve Servis Limited Sirketi, Istanbul, Turkey,
- DMG Russland o.o.o., Moscow, Russia,
- GILDEMEISTER Italiana Deutschland GmbH, Stuttgart
  and
- Chemnitzer Grundbesitz Limited, Birmingham, Great Britain.

Compared to the previous year, the following companies are no longer included in the consolidated group:

- Holding Macchine Utensili S.p.A., Milan, Italy,
- DMG Service BAZ GmbH DECKEL MAHO GILDEMEISTER, Geretsried,
- DMG Lyon S.A.S., Lyon, France.

As part of the restructuring activities carried out at the Italian subsidiaries, Holding Macchine Utensili S.p.A. (HMU), Milan, Italy, the former finance company for the Italian production facilities, merged with GILDEMEISTER Italiana S.p.A., Brembate di Sopra (Bergamo), Italy. For this purpose GILDEMEISTER Aktiengesellschaft had transferred 100% of its shares in HMU through a non-cash contribution at book values to GILDEMEISTER Italiana S.p.A. prior to the merger. In October 2005 GRAZIANO Tortona S.p.A. was converted from a stock corporation (S.p.A.) to a limited liability company (S.r.l.) and the name of the company changed to GRAZIANO Immobiliare S.r.l. The share capital of € 3,120 K is fully paid up. The company now serves as the central property management company in Italy. In December 2005 the entire real estate of the Italian companies was combined in this company.

In addition, GRAZIANO Tortona S.r.l., Tortona, Italy, was newly established as the fully owned subsidiary of GRAZIANO Immobiliare S.r.l. The share capital of € 3,000 K is fully paid up. The new GRAZIANO Tortona S.r.l. took over the operative business of former GRAZIANO Tortona S.p.A. with effect from October 2005 and has been fully consolidated since this date. On 20 December 2005 GILDEMEISTER Italiana S.p.A. took over 100% of the shares in GRAZIANO Tortona S.r.l. at book value. In January 2005 DMG Istanbul Makine Tikaret ve Servis Limited Sirketi, Istanbul, Turkey, was established as a subsidiary of DMG Europe Holding GmbH, Klaus, Austria, (99.99%) and of DMG Vertriebs und Service GmbH, Bielefeld, Germany (0.01%). The share capital of TRY 0.9 million (approx. € 473 K) is fully paid up. Also in January DMG Russland o.o.o., Moscow, Russia, was established as a subsidiary of DMG Europe Holding GmbH with an investment of 99.0% and of DMG Vertriebs und Service GmbH with an investment of 1.0%. The share capital of RUB 37 million (approx. € 958 K) is fully paid up. Both companies have been fully consolidated with effect from January. In December 2005 GILDEMEISTER Italiana Germany GmbH, Leonberg, was established as a fully owned subsidiary of DMG Stuttgart Vertriebs und Service GmbH, Leonberg, with a share capital of € 25 K. It will begin its operative business with effect from 1 January 2006 and has been fully consolidated with effect from December 2005.

Chemnitzer Grundbesitz Limited, Birmingham, Great Britain, is a 94.9% owned subsidiary of DMG Berlin Vertriebs und Service GmbH. The remaining 5.1% of shares are owned by third parties. It was established with a share capital of GBP 10 K (approx. € 15 K) in March 2005 as a cost-effective funding vehicle for the centre of technology of DMG Berlin Vertriebs und Service GmbH. The company has been fully consolidated since then.

With effect from January 2005 GILDEMEISTER Aktiengesellschaft transferred its 100% investment in a & f Stahl- und Maschinenbau GmbH to DMG Vertriebs und Service GmbH at book value.

Retrospectively, as from 1 January 2005, DMG Service BAZ GmbH, Geretsried, was integrated into the central service companies in Pfronten and Seebach through a company split-up by absorption. The corporate names of DMG Service UFB GmbH, Pfronten, to DMG Service Fräsen Pfronten GmbH, and of DMG Service UFB Seebach GmbH, Seebach, to DMG Service Fräsen Seebach GmbH were changed in December 2005. Both companies will continue to operate at the Geretsried site.

With effect from 30 December 2005 DMG Lyon S.A.S., Lyon, France merged with DMG Paris S.a.r.l., Les Ulis, France.

In the accounting period 2005 DMG Europe Holding GmbH acquired the remaining 49.0% of shares in DMG Austria GmbH, Klaus, Austria, at a price of € 740 K. No undisclosed reserves or encumbrances were identified in the company's assets and liabilities. Neither were any intangible assets present, the fair value of which can be determined with sufficient reliability.

With effect from 29 September 2005 DMG Benelux B.V., Veenendaal, Netherlands (formerly DMG Nederland B.V., Veenendaal) transferred 100% of its shares in DMG Asia Pacific Pte. Ltd., DMG Nippon K.K. and DMG Malaysia SDN BHD to DMG Europe Holding GmbH, each at its book value. DMG Benelux B.V. sold 100% of its shares in DMG Italia S.r.l. to GILDEMEISTER Italiana S.p.A. at a price of € 8,400 K. As a result GILDEMEISTER Italiana S.p.A. is now the 100% shareholder of all Italian group companies.

The consolidated group has not changed significantly since the previous year so that the comparability with the Consolidated Financial Statements of the previous year is not affected. There were no disposals or close-downs of plants or operating units in the past accounting period. The impact of the unconsolidated companies on the group's net worth, financial and profit situation is minor. No pro rata consolidation or inclusion under the equity method was required either in the accounting period 2005 or in the previous accounting period.

An overview of all affiliated companies is shown on page 154 sqq.

3 CONSOLIDATION PRINCIPLES

Consolidation of investments is carried out in accordance with the purchase method pursuant to IFRS 3 "Business Combinations". With this method, the investment book value of the parent company is set off against the group share in the fully revalued equity of the subsidiary. In the course of the revaluation process, all acquired assets and liabilities, and also identifiable intangible assets that must be recognised as assets, are measured at their fair value. Any positive balance remaining after the allocation of the purchase price will be recognised as goodwill.

IFRS 3 "Business Combinations" and IAS 36 "Impairment of Assets" provide for amortisation of goodwill only, if a valuation adjustment requirement was determined, instead of scheduled amortisation. Any goodwill arising from business combinations is therefore no longer amortised over the period of anticipated use, but will be reviewed annually in terms of impairment and amortised if required. GILDEMEISTER applies the above standards since 1 January 2004.

Any shares in the equity of the subsidiaries that the parent company is not entitled to are shown as a separate item within equity.

Any reciprocal receivables and payables between the companies included in the Consolidated Financial Statements are set off with each other. Intercompany profits from intragroup supplies are eliminated; deferred tax debits and deferred tax credits from consolidation transactions recognised in the Income Statement included. Intragroup sales revenues are, as is any intragroup income, set off against the relating expenses without being recognised in the Income Statement. The applied consolidation methods remain unchanged in comparison with the previous year.

4 ACCOUNTING AND VALUATION PRINCIPLES

All Annual Financial Statements of those companies that were included in the Consolidated Financial Statements were prepared at the reporting date of the Consolidated Financial Statements and in accordance with uniform accounting and valuation principles.

For this purpose, those accounts that were prepared in accordance with local regulations were adjusted to the group-standardised accounting and valuation principles of GILDEMEISTER Aktiengesellschaft to the extent that they do not comply with IFRS and the deviations in the valuation are major.

Changes in accounting and valuation methods due to new standards

In the course of the so-called "Improvements Project", the IASB has revised existing IFRS and adopted new IFRS. Their application has been mandatory since 1 January 2005. Out of these standards – to the extent that they had an impact on the business of our company – the following were applied for the first time in the accounting period 2005:

IAS 1	Presentation of Financial Statements
IAS 2	Inventories
IAS 8	Accounting, Policies, Changes in Accounting Estimates and Errors
IAS 10	Events after the Balance Sheet Date
IAS 16	Property, Plant and Equipment
IAS 17	Leases
IAS 21	The Effects of Changes in Foreign Exchange Rates
IAS 24	Related Party Disclosures
IAS 27	Consolidated Financial Statements
IAS 28	Investments in Associates
IAS 31	Interests in Joint Ventures
IAS 32	Financial Instruments: Disclosure and Presentation
IAS 33	Earnings per Share
IAS 39	Financial Instruments: Recognition and Measurement
IAS 40	Investment Property
IFRS 2	Share-based Payment
IFRS 4	Insurance contracts
IFRS 5	Non-current assets held for sale and discontinued operations

The application of these standards was in accordance with the respective transitional provisions. Unless expressly provided for by individual standards and commented on separately in the following, the application was retrospective, i.e. the representation was so as if the revised accounting policies have always been applied. The benchmark figures for the previous year were adjusted accordingly and marked "adjusted".

The following material effects on the periods shown in the Consolidated Financial Statements 2005 included:

IAS 1 "Presentation of Financial Statements"

The application of the revised Standard requires the classification of the Consolidated Balance Sheet by maturities. This requires the separate presentation of assets and liabilities in current and non-current categories. Current items include items that are expected to be realised or settled within the company's operating cycle of our divisions or within a period of twelve months after the reporting date.

Minority interests in group equity are presented in the Balance Sheet as a separate item within equity. In the Income Statement, profit or loss attributable to minority interests are part of the group profit or loss. The allocation of the group profit or loss to equity holders of the parent company and to minority interests is presented separately.

The presentation of changes in equity has been extended by minority interests.

IAS 39 "Financial Instruments: Recognition and Measurement"

The application of IAS 39 has resulted in changes with respect to the new derecognition regulations for financial assets. In accordance with the amended IAS 39 the company continues to bear the material risks and rewards arising from discounted customers' bills. Therefore a derecognition is not permitted before the bill has been fully paid back at the due date. In the Balance Sheet the benchmark figures for the previous year have been adjusted pursuant to IAS 8. Other non-current assets and financial liabilities increased by € 19,862 K, other current assets and financial liabilities by € 10,790 K.

Due to the adjustment of the Consolidated Financial Statements for the financial year 2004 pursuant to IAS 8, there were no effects on equity or annual profit of the GILDEMEISTER group.

New accounting principles

The following standards and interpretations issued and adopted by the European Union with effect from 31 December 2005 that have not as yet come into effect, were not applied in these Financial Statements:

- IAS 19: Amendment to IAS 19, Employee Benefits
- IAS 39: Financial Instruments: Recognition and Measurement
- IAS 39: Financial Instruments: Recognition and Measurement including the provisions on the application of the 'fair value option'
- IFRS 6: International Financial Reporting Standards (IFRS) 6 Exploration for and Evaluation of Mineral Resources
- IFRIC 4: Determining whether an Arrangement Contains a Lease
- IFRIC 5: Rights to Interests Arising from Decommissioning, Restoration and Environmental Funds

The new standards are not expected to impact the Consolidated Financial Statements of GILDEMEISTER Aktiengesellschaft during the period of their initial application.

The preparation of the Consolidated Financial Statements in accordance with IFRS requires that assumptions are made and estimates are used that will affect the amount and the statement of the assets and liabilities, income and expenses and contingent liabilities shown in the balance sheet. These assumptions and estimates relate primarily to the definition of useful economic life, the valuation of the net realisable values of inventories, the accounting and valuation of provisions and the feasibility of future tax relieves. In individual cases, the actual values may differ from the assumptions and estimates made. Pursuant to IAS 8 "Accounting Policies, Changes in Accounting Estimates and Errors", changes will be taken into account at the time of their discovery and recognised in the Income Statement.

The application of specific IFRS is included in the explanatory notes on individual balance sheet items. In principle, the following accounting policies have been applied:

Intangible and tangible assets

Useful economic life of assets	
Software and other intangible assets	3 to 5 years
Development costs	3 to 5 years
Office and factory buildings	10 to 50 years
Technical equipment and machines	6 to 20 years
Factory and office equipment	2 to 20 years

Acquired and internally generated intangible assets were capitalised pursuant to IAS 38 "Intangible Assets", if it is probable that the use of the asset will result in an economic benefit and the costs of the asset can be reliably determined. They were shown at their acquisition or production costs, reduced by scheduled straight-line depreciation in accordance with their useful economic life.

Development costs of machine tool projects, service products and specific software solutions were capitalised at their production costs, as far as the definite charging to expense requirement pursuant to IAS 38 "Intangible Assets" was possible, the technical feasibility and marketing established and the anticipated generation of future economic benefit demonstrated. The production costs include those that can be directly and indirectly ascribed to the development process and necessary parts of development-related overheads. Capitalised development costs are written off by scheduled depreciation from the start of production over the expected product life cycle. Research costs are shown as expense in the period when they were incurred.

IFRS 3 "Business Combinations" provides for amortisation of goodwill, provided a valuation adjustment requirement was determined, instead of scheduled amortisation.

Intangible fixed assets and tangible fixed assets were assessed at their acquisition or production costs, reduced by scheduled depreciation through use. Depreciation was normally carried out by the straight-line method in accordance with the useful life. Low value items were fully written off in the year of their addition. A revaluation of tangible fixed assets pursuant to IAS 16 "Property, Plant and Equipment" was not carried out. There was no property held as financial investment pursuant to IAS 40 "Investment Property".

The production costs of internally generated assets include those that can be directly ascribed to the manufacturing process, and necessary parts of production-related overheads. This includes production-related depreciation, prorated administration costs and prorated costs from the social contribution area.

Borrowing costs are not assessed as part of acquisition or production costs. Costs of repair are immediately charged to expenses.

Leases, including tangible assets leased by way of sale-and-lease-back arrangements, were recognised as finance leases, if all the risks and rewards incident to ownership are substantially transferred to the lessee. Leasing agreements for leased tangible assets that meet the criteria of a finance lease pursuant to IAS 17 “Leases”, are capitalised at the lessee’s at their acquisition costs or at the lower cash value of the minimum lease payments. Depreciation is carried out by scheduled straight-line method over the shorter of the useful economic life of the asset or the lease term. The relating financial obligations arising from future lease payments were carried as liability under other liabilities.

Impairment

In accordance with IAS 36 “Impairment of Assets”, the book values of the assets of the GILDEMEISTER group, with the exception of inventories and deferred tax assets, are tested for signs of impairment at every balance sheet date. If such signs exist, the fair value of the assets will be estimated and, if required, adjusted accordingly. This adjustment will be recognised in the Income Statement. An impairment test for individual assets is only possible if recoverable amounts can be allocated to the individual asset. If this is not possible, the recoverable amount of the cash-generating unit pertaining to the asset must be determined (asset’s cash-generating unit).

Pursuant to IAS 36 “Impairment of Assets”, goodwill has to be tested for impairment at least once a year. GILDEMEISTER Aktiengesellschaft has carried out an impairment test on 30 September 2005. In the impairment test, the book value of a cash-generating unit is compared to the recoverable amount. The recoverable amount of the cash-generating unit is the higher of the asset’s fair value less costs to sell and its value in use.

In the GILDEMEISTER group, the “Machine Tools” and “Services” segments were defined as cash-generating units. The “Machine Tools” segment was allocated goodwill to the value of € 38,258 K and the “Services” segment was allocated goodwill to the value of € 29,671 K. The recoverable amount equals the value in use and was calculated as the present value of future cash flows. The future cash flows were derived from the planning of GILDEMEISTER group. Planning is based on a detailed planning period extending up to the accounting period 2008. A growth rate of 1% was assumed for the period following the detailed planning period, which is in line with general expectations of future business development.

The cash flows defined were discounted at a post-tax weighted cost of capital rate of 6.59%. This represents a pre-tax percentage of 10.22%.

If the recoverable amount of a cash-generating unit is lower than its book value, the value of goodwill allocated to the cash-generating unit will, initially, be reduced at an amount equal to the remaining balance.

Financial assets

Financial assets were initially recognised in the balance sheet at their acquisition costs and subsequently shown at their fair values. The financial assets are classified as "available for sale". However, they are always shown at their respective acquisition costs, since there is no active market for these companies and their fair value cannot be reasonably determined.

Inventories / Trade debtors and other assets

Valuation of inventories was carried out at the acquisition or production costs or the lower net realisable value. Pursuant to IAS 2 "Inventories" elements of the production costs include, along with production material and manufacturing labour, prorated materials and production overheads and prorated administrative expenses and expenses arising in the social contribution area. Borrowing costs are not assessed as part of acquisition or production costs. When determining the net realisable value, inventory risks arising from the period of storage and reduced usability were recognised through appropriate reductions in value.

Lower values at the balance sheet date arising from a reduction in sales revenues were recognised. Raw materials and consumables as well as merchandise were primarily assessed by the average cost method.

Receivables and other assets were shown in the balance sheet at their amortised initial value. Long-term non-interest bearing or low-interest bearing receivables have been discounted. All identifiable risks were taken into account by adjusting their relating accounts accordingly. Current asset securities are classified as "available for sale" and recognised at their fair value on the balance sheet date. Liquid funds are assessed at face value.

Deferred tax

Pursuant to IAS 12 "Income Taxes" deferred taxes are assessed in accordance with the balance-sheet oriented liability method. For this purpose, deferred tax assets and liabilities were basically recognised for all temporary accounting and valuation differences between the IFRS balance sheet valuations for group purposes and the tax valuations (temporary differences), and with respect to consolidation processes recognised in the Income Statement. Deferred tax assets for future financial benefits arising from tax-loss credits were also reported in the balance sheet. However, deferred tax assets for all deductible temporary differences and for tax-loss credits were only recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences or unused tax losses can be utilised. The deferred taxes were calculated on the basis of income tax rates that, pursuant to IAS 12 "Income Taxes", at the date of valuation apply or have been enacted in the individual countries in accordance with the current legal status. Deferred tax assets and liabilities were balanced out only to the extent that an offset is legally permissible. Deferred tax assets and liabilities were not discounted in accordance with the provisions contained in IAS 12 "Income Taxes".

Provisions and liabilities

Company pension reserves are calculated on the basis of the "Projected Unit Credit Method" pursuant to IAS 19 “Employee Benefits”. Under this method, not only those pensions and pension rights known or accrued at the balance sheet date are recognised, but also expected future increases in pension payments and salaries by estimating the relevant factors impacting such payments. Calculation is based on actuarial reports taking into account biometric calculation principles. The amounts not yet shown in the balance sheet emanate from actuarial gains and losses from inventory changes and deviations between assumptions made and actual development. Actuarial gains and losses are only recognised as income or expense if they exceed a 10% margin of the defined benefit obligation. Distribution is carried out over the participating employees’ expected average residual period of service. The option pursuant to IAS 19.93A to fully recognise actuarial gains and losses and set them off against revenue reserves was not used.

Pursuant to IAS 37 “Provisions, Contingent Liabilities and Contingent Assets” other provisions were only recognised in case of an existing present obligation to third parties, the use of which is probable and if the anticipated amount of the required provision can be reliably estimated. In this case the probability of occurrence must exceed 50%. In each case the most probable amount of performance was recognised. The measurement is carried out using the best estimate of the amount required to settle the obligation on the balance sheet date. Provisions with a remaining term of more than one year were discounted on the customary conditions.

Liabilities are recognised at amortised costs. Liabilities were recognised at their amounts repayable. Liabilities arising from finance leases are shown in other liabilities at the present value of the future lease payments. Customer prepayments were charged to liabilities.

Derivative financial instruments

The hedging of risk items from currency and interest rate fluctuations is often carried out through the use of derivative financial instruments such as forward exchange dealings and interest rate swaps. The hedging covers financial risks from underlying transactions and, in the case of currency risks, also risks from pending supply and service transactions. For the hedging of currency risks arising from transactions within the GILDEMEISTER group forward exchange dealings are used primarily. Interest hedging tools in the form of swaps are used to eliminate the effect from future changes in the interest rate on the cost of financing credits that are subject to a floating rate. With respect to derivative financial instruments the GILDEMEISTER group is exposed to a credit risk that arises from the non-performance of contractual agreements by the other party. This credit risk is minimised by only entering into transactions with parties of superb financial standing.

Pursuant to IAS 39 “Financial Instruments: Recognition and Measurement” all derivative financial instruments are recognised at their fair market value, regardless of the purpose or intention for which they were entered into.

Forward exchange dealings are valued individually at the futures price at the balance sheet date. In the case of cashflow-hedges, any price differences from the agreed futures price will be recognised in equity. If no cashflow-hedges exist, price differences are shown in the Income Statement.

The changes in market value of the interest rate swap agreements where hedge accounting is applied are shown in equity. If cashflow-hedges exist that are used to counterbalance future cash flow risks arising from existing underlying transactions, the unrealised profits and losses corresponding to the amount of the hedged underlying transaction (hedge effective portion) are initially recognised directly in equity. The portion of the change in fair market value which is not hedged by the underlying transaction (hedge ineffective portion) is recognised directly in the income statement. A book transfer to the Income Statement is carried out at the same time when the hedged underlying transaction affects profit or loss.

As soon as the underlying transactions are discontinued, the amounts previously shown in equity, will be retransferred to the Income Statement.

The conclusion and processing of derivative financial instruments is based on binding internal regulations defining scope, responsibilities, reporting and controlling.

Sales revenues

Pursuant to the criteria laid down in IAS 18 “Revenue”, sales revenues arising from the sale of products is recognised at the time of transfer of the relevant risks and rewards, if a price has been agreed or can be determined and it can be assumed that such price will be paid. In the case of revenue arising from the sale of goods this is continuously the time of delivery. Before delivery sales revenues are recognised if the product has not been delivered at the request of the customer, legal ownership has been transferred to the customer and the customer has accepted the invoicing. Sales revenues arising from services is recognised after the services were rendered.

Consideration receivable for deliveries and services charged to the customer and reduced by any sales deductions, contract penalties and cash discounts are shown in sales revenues.

5 FOREIGN CURRENCY TRANSLATION

The currency translation of all Annual Financial Statements of the international group companies that were prepared in foreign currencies was carried out in accordance with the “functional currency” principle pursuant to IAS 21 “The Effects of Changes in Foreign Exchange Rates”. Since all subsidiaries operate their business independently in financial, economic and organisational respects, their respective currencies represent the respective local currency. All assets and liabilities of foreign subsidiaries were translated at the average rate of exchange of the balance sheet date, and all revenue and expense at the average annual market price. The translation differences arising from items being translated at different rates in the Balance Sheet and the Income Statement, were recognised directly in equity. The exchange differences arising from the currency translation of the equity capital were also transferred to equity.

In the individual financial statements monetary items (cash, receivables and liabilities) in a foreign currency were valued at the exchange rate at the reporting date. Non-monetary items in foreign currencies were assessed at the historical values. The differences arising from the currency translation of monetary items were shown in the Income Statement.

Goodwill resulting from the acquisition of international companies was translated at the exchange rates at the time of the transactions.

Accounting in accordance with the regulations contained in IAS 29 “Financial Reporting in Hyper-inflationary Economies” was not required, as the GILDEMEISTER group has no significant subsidiaries with registered offices in a hyper-inflationary economy.

The exchange rates of the major currencies developed as follows:

		Current price on reporting date = 1 €		Average price = 1 €	
Currencies	**ISO-Code**	31 Dec. 2005	31 Dec. 2004	2005	2004
British Pound	GBP	0.68700	0.70710	0.68504	0.68192
Swiss Francs	CHF	1.55550	1.54370	1.54732	1.54531
Polish Zloty	PLN	3.86860	4.08770	4.03712	4.54375
Czech Koruna	CZK	28.99000	30.39000	29.80615	31.94538
US-Dollar	USD	1.18340	1.36400	1.24771	1.24740
Canadian Dollar	CAD	1.37690	1.64300	1.50992	1.61652
Mexican Pesos	MXN	12.61000	15.24000	13.61308	14.11769
Brazilian Real	BRL	2.75670	3.62060	3.04968	3.62915
Japanese Yen	JPY	139.13000	139.83000	137.14308	133.92077
Singapore Dollar	SGD	1.96880	2.22740	2.07418	2.10500
Malaysian Ringgit	MYR	4.48230	5.01930	4.71004	4.70275
Indian Rupee	INR	53.28000	59.27000	54.97308	56.40000
Chinese Renminbi	CNY	9.55150	11.28910	10.22318	10.32521
Taiwan Dollar	TWD	38.95000	43.17000	40.11885	41.48614
Korean Won	KRW	1191.00000	1412.29000	1277.08769	1421.86385
Australian Dollar	AUD	1.61450	1.74890	1.63556	1.69164

Notes to individual accounts in the Income Statement

6 SALES REVENUES

Consideration receivable for deliveries and services charged to the customer and reduced by any sales deductions, contract penalties and cash discounts is shown in sales revenue. Sales revenue is broken down by distribution areas as follows:

	2005	2004
	€ K	€ K
Germany	**501,946**	502,892
EU (excl. Germany)	**344,012**	308,719
USA	**81,343**	74,590
Asia	**113,253**	93,860
Other countries	**85,343**	71,439
	1,125,897	1,051,500

Sales revenues are explained in detail in the “Segmental Reporting” chapter of the Management Report.

7 OTHER CAPITALISED PAYMENTS

Other capitalised payments primarily arise from the capitalisation of development costs of machine tool projects pursuant to IAS 38 “Intangible Assets”.

8 OTHER OPERATING INCOME

	2005	2004
	€ K	€ K
Income unrelated to accounting period		
Retransfer of provisions	**9,120**	6,957
Retransfer of value adjustments	**1,248**	1,940
Profit on asset disposals	**1,287**	374
Receipt of payment for written off delinquent accounts	**44**	41
Other income unrelated to accounting period	**2,793**	964
	14,492	10,276
Other operating income		
Use of provisions	**1,089**	2,122
Changes in exchange rates	**9,112**	8,076
Refund of expenses and on-debiting	**5,142**	1,911
Compensation for damages	**1,887**	492
Letting and leasing	**398**	755
Bonuses and allowances	**719**	577
Other	**1,767**	1,971
	20,114	15,904
Total	**34,606**	26,180

The increase in other income compared to the previous year is due primarily to income arising from the derecognition of time-barred liabilities of € 1,173 K and the reimbursement of the public utility contribution of € 316 K to the water supply company Trinkwasserverband Eisenach.

The changes in exchange rates are to be seen in relation to exchange rate and currency losses in other operating expenses, against which they are offset.

The increase in income from the payment of damages compared to the previous year is due primarily to an increase in insurance refunds for fire and transport damages as well as for a flood damage.

Income from the refund of expenses and on-debiting mainly include income from the on-debiting of advertising charges of € 1,000 K.

9 COST OF MATERIALS

Payments received primarily pertain to expenses for external production.

10 PERSONNEL COSTS

In the accounting period 2005, pension plan expenses including employers' contributions to the statutory pension insurance, in the group amounted to € 17,817 K (previous year: € 16,910 K)

Remuneration for members of the Executive Board

The structure of the remuneration system for members of the Executive Board is discussed and decided on by the Supervisory Board at the proposal of its Personnel, Nomination and Remuneration Committee. The chairman of the Supervisory Board has provided the Supervisory Board with detailed information on the discussions held by the Committee.

Members of the Executive Board receive direct and indirect remuneration components. The indirect remuneration component primarily consists of pension plan expenses. The direct remuneration for members of the Executive Board of GILDEMEISTER Aktiengesellschaft includes fixed and variable components. Criteria for the adequacy of the remuneration primarily include the tasks rendered by each Executive Board member, his or her personal performance, the performance of the Executive Board and the company's economic situation, success and future prospects in view of its comparative environment.

For the accounting period 2005, direct remuneration for active members of the Executive Board amounted to € 2,489 K (previous year: € 2,032 K). Of this amount, € 1,090 K (previous year: € 1,004 K) were attributed to fixed remuneration, € 1,014 K (previous year: € 600 K) to the management bonus, € 300 K (previous year: € 350 K) to a project bonus and € 85 K (previous year: € 79 K) to remuneration in kind.

In 2005, the direct remuneration for members of the Executive Board was made up as follows:

Direct remuneration for Executive Board members

	Fixed Remuneration	Management bonus	Projekt bonus	Remuneration in kind	Total
	€ K	€ K	€ K	€ K	€ K
Dr. Rüdiger Kapitza, chairman	455	338	100	31	924
Prof. Dr.-Ing. Raimund Klinkner, deputy chairman	350	338	100	33	821
Dipl.-Kfm. Michael Welt	285	338	100	21	744
Total	**1,090**	**1,014**	**300**	**85**	**2,489**

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The fixed remuneration is the contractually defined basic remuneration that is paid in equal amounts as a monthly salary. It is usually reviewed in the course of the contract renewal negotiations. The management bonus is based on the achievement of internal target values. In the accounting period 2005, its reference value was EAT ("earnings after taxes"). The differentiation of the target values is redefined annually. The profit-sharing system has a risk characteristic, which means it is not a secure remuneration.

The Supervisory Board offered a project-related bonus to all members of the Executive Board for the achievement of defined cost adjustment targets at the GILDEMEISTER group.

Remuneration in kind arises mainly from amounts for the use of company cars, which will be assessed in accordance with applicable tax regulations, and individual insurance contributions. Every member of the Executive Board is contractually entitled to remuneration in kind. Amounts can vary depending on the member's personal situation and are subject to tax payable by each member.

Pension commitments for members of the Executive Board are primarily implemented through a contribution-based pension plan. Expenses in this respect amounted to € 90 K (previous year: € 90 K), recognised in equal parts with respect to the deputy chairman and the ordinary member of the Executive Board. Defined-benefit pension commitments for the chairman of the Executive Board are exceptional. In the early 1990s, when the current chairman was appointed to the Executive Board, this type of commitment was market standard in the remuneration of Executive Board members. In accordance with IFRS this resulted in provision expenses of € 96 K in 2005. Every Executive Board member has the option of taking part in a deferred compensation model, where the member can contribute to his/her old age pension through a salary conversion.

Advances and loans to Board members, or to Supervisory Board members, were not granted, and no declarations of liability (e.g. guarantees) in favour of the above mentioned persons were entered into.

There are no stock option plans or similar security-orientated incentive systems of the company. Stock option plans or similar remuneration components with a long-term incentive effect for officers do therefore not exist either. Notices by members of the company's Executive Board or by other persons subject to reporting requirements, on the acquisition or disposal of shares or related rights of purchase or disposal (such as options) or rights that are directly dependent on the company's stock exchange price, were not received.

Neither did the group companies of the GILDEMEISTER group pay any remuneration to officers for services personally rendered, in particular consulting and introduction services. Former members of the board and their surviving dependants received € 586 K (previous year: € 598 K).

Company pension obligations (present value of future pension commitments or "defined benefit obligation") for former members of the Executive Board and their surviving dependants amounted to € 8,151 K (previous year: € 7,483 K). Advances and loans to officers were not granted nor were any contingencies in favour of officers entered into.

In comparison with the previous year the number of persons employed has developed as follows:

	Average number of persons employed		At the balance sheet date	
	2005	2004	31 Dec. 2005	31 Dec. 2004
Wage earners	1,628	1,717	1,631	1,727
Salary earners	3,462	3,215	3,452	3,257
Trainees	166	185	189	190
	5,256	5,117	5,272	5,174

11 DEPRECIATION/ AMORTISATION

Depreciation/amortisation totalling € 31,369 K includes amortisation of intangible assets and tangible assets of € 31,241 K and depreciation of inventories of € 128 K, as far as these exceed normal depreciation.

12 OTHER OPERATING EXPENSES

	2005	2004
	€ K	€ K
Expenses unrelated to accounting period		
Losses from fixed asset disposal	**388**	511
Other taxes	**123**	404
Other expenses unrelated to accounting period	**2,535**	868
	3,046	1,783
Other operating expenses		
Marketing, trade fairs and other advertising expenses	**25,571**	23,246
Rental and leases	**21,918**	19,920
Travelling and entertainment expenses	**20,678**	19,670
Freight out, packaging	**21,441**	17,942
Other external services	**16,511**	15,241
Sales commissions	**10,546**	12,788
Cost of preparation of accounts, legal and consultancy fees	**8,877**	9,766
Stationery, post and telecommunication expenses	**8,561**	8,044
Exchange rate and currency losses	**7,677**	7,683
Transfer to provisions	**7,607**	6,077
Other personnel costs	**5,773**	5,529
Monetary transactions and capital procurement	**4,637**	3,979
Losses from the decline in value of assets/receivables	**5,085**	3,711
Insurance	**3,659**	3,258
Other taxes	**1,362**	1,200
Investor- and Public-Relations	**2,130**	1,713
Licences and trade marks	**967**	518
Other	**12,523**	9,823
	185,523	170,108
Total	**188,569**	171,891

Compared to the previous year expenses for rents and leases increased due to an increase in lease expenses. This was due to a basic agreement for the operating lease of exhibition machines that was entered into in the middle of 2004.

The increase in freights out and packaging over the previous year is due to the increase in international sales and the related increase in the cost of transport. In addition, increased fuel surcharges and tolls were incurred compared to the previous year.

The transfer to provisions results primarily from expenses for warranty commitments, retrofittings and losses from pending transactions.

In the accounting period 2005, € 175 K (previous year: € 173 K) were transferred to provisions for Supervisory Board members' remuneration to be paid in 2006. An individualised and detailed breakdown of Supervisory Board members' remuneration for the accounting period 2005 is included in the Corporate Governance Report starting on page 65.

13 OTHER INTEREST RECEIVABLES AND SIMILAR INCOME

Interest receivable and similar income of the entire group amounted to € 2,069 K (previous year: € 2,302 K).

14 NET INTEREST PAYABLE AND SIMILAR CHARGES

Net interest payable, amounting to € 31,500 K (previous year: € 30,432 K), primarily relates to the group's financial liabilities.

Net interest payable and similar charges also include the interest component of € 1,638 K (previous year: € 1,703 K) from the transfer to company pension provisions.

15 TAXES ON PROFITS

This account represents current and deferred tax expenditure and income that break down as follows:

	2005	2004
	€ K	€ K
Current taxes	**9,532**	4,154
Deferred taxes	**2,303**	2,290
	11,835	6,444

In the domestic companies current taxes include corporate income and trade tax, and in the international companies comparable earnings-linked taxes that were determined on the basis of the appropriation of profits. The computation was made on the basis of the tax regulations applicable to the individual companies. In the accounting period 2005, an amount of € 1,018 K (previous year: € 1,710 K) resulted from tax income for prior years. An amount of € 940 K (previous year: € 501 K) is included for tax expenses for prior years.

Deferred tax income unrelated to the accounting period of € 4,335 K (previous year: € 3,462 K) is set off by deferred tax expenditure unrelated to the accounting period of € 3,066 K (previous year: € 2,352 K). Current income tax expenditure was reduced by € 1,368 K (previous year: € 71 K) due to the use of tax loss credits not yet recognised from previous accounting periods. Another reduction in deferred tax expenditure due to tax loss not yet recognised from prior periods in the amount of € 1,362 K (previous year: € 3,215 K) and due to deferred tax assets from temporary differences not yet recognised in an amount of € 2,974 K (previous year: € 0 K).

Writedowns of prior years' deferred tax assets from tax loss credits were carried out in the reporting year in an amount of € 3,066 K (previous year: € 1,874 K).

Current taxes in relation to the discontinuance of business divisions did not occur in the reporting year. Due to the continued application of the accounting methods no additional tax expenditure or income arose. There were no material errors in the past so that no consequences arose in this respect.

Deferred taxes are calculated on the basis of income tax rates that at the date of valuation apply or are expected in the individual countries in accordance with the current legal status. Taking into account trade earnings tax and the solidarity surcharge (Solidaritätszuschlag), this results in a tax rate applicable to the valuation of deferred taxes of 38% (previous year: 38%) for domestic companies. International tax rates are between 19% and 41%.

Deferred tax assets and liabilities were recognised directly in equity at the balance sheet date amounted to € 1,810 K (previous year: € 1,848 K). In the accounting period 2005, the recognised income tax expenditure of € 11,835 K (previous year: € 6,444 K) has increased by € 2,247 K (previous year: € 1,900 K) when compared with the expected income tax expenditure of € 9,588 K (previous year: € 4,544 K), which would in theory arise if the national tax rate of 38% (previous year: 38%) applicable for the accounting period 2005 had been applied at group level. The difference between current and expected income tax expenditure is due to the following:

	2005	2004
	€ K	€ K
Results of ordinary activities before taxes	25,365	12,020
GILDEMEISTER Aktiengesellschaft tax rate in percent	38	38
Theoretical tax income/expenditure	9,588	4,544
Tax consequences on the following influences		
Adjustment due to differing tax rate	-534	346
Effects from changes in tax rate	6	63
Tax reduction due to revenues exempt from taxation	-1,212	-694
Deferred taxable losses	634	535
Temporary differences	-1,892	268
Tax increase due to non-deductible expenses	6,028	3,206
Tax income or expenditure for prior years	-78	-1,210
Other adjustments	-705	-614
Taxes on corporate income and revenue	**11,835**	6,444

Future dividends of GILDEMEISTER Aktiengesellschaft payable in Germany will not influence the group's tax charge.

16 OTHER SHAREHOLDERS

An annual loss of € 189 K (previous year: annual profit of € 42 K) is attributed to other shareholders.

17 EARNINGS PER SHARE

In accordance with IAS 33 "Earnings per Share", the undiluted earnings per share ("basic earnings per share") are determined by dividing the consolidated earnings – excluding profit shares by other shareholders – by the average number of shares, as follows:

		2005	2004
Group result excluding profit share to other shareholders	€ K	**13,719**	5,534
Average weighted number of shares		**43,302,503**	36,721,482
Earnings per share	€	**0.32**	0.15

Earnings resulted exclusively from continued business. There were no diluted earnings per share for either the accounting period 2005 or the previous accounting period.

Notes to individual balance sheet items

18 INTANGIBLE ASSETS

As in the previous accounting period, € 66,857 K (previous year: € 66,857 K) of goodwill shown relate to the asset-side difference from the consolidation of investments and € 1,072 K (previous year: € 1,072 K) to goodwill from the individual financial statements.

Capitalised development costs relate to new machine tool projects in the domestic and international production companies, to development costs for service products of DMG Vertriebs und Service GmbH and to specific software solutions. Development costs capitalised at the end of the accounting period amount to € 27,943 K (previous year: € 24,245 K) . Research and development costs directly charged to expenses amount to € 32.9 million in the accounting period 2005 (previous year: € 31.6 million). In the financial year reclassifications regarding current and fixed assets amounting to € 4,574 K have been made.

The amount stated for industrial property rights and similar rights includes acquired patents, design patents and trade marks as well as data processing software. Rights and software are amortised by scheduled method over a useful economic life of three to five years.

Changes in, and a breakdown of, items included in the group's intangible assets are illustrated in the consolidated fixed-asset movement schedule. Investments are explained in further detail in the Group Management Report on starting on page 51.

19 TANGIBLE ASSETS

Changes in, and a breakdown of, items included in the group's tangible assets are illustrated in the consolidated fixed-asset movement schedule. Investments are explained in further detail in the Group Management Report on page 51.

The change in currency between the balance sheets dates is shown in the consolidated fixed-asset movement scheduled under "Other changes".

Neither value adjustments due to impairments nor reversals of appreciation were required for tangible assets in the reporting period.

Land and buildings are mortgaged for the security of long-term bank loans. Tangible assets include leased assets to the value of € 4,035 K (previous year: € 6,702 K) that must be charged to the respective group company as beneficial owner due to the structuring of the underlying leases ("finance lease").

The book values of capitalised lease items are divided as follows:

	31 Dec. 2005	31 Dec. 2004
	€ K	€ K
Land and buildings	**1,243**	3,344
Technical equipment and machinery	**1,394**	1,548
Other fixed assets, factory and office equipment	**1,398**	1,810
	4,035	6,702

20 FINANCIAL ASSETS

Changes in the group's financial assets are illustrated in the consolidated fixed-asset movement schedule.

Impairments of € 21 K (previous year: € 0 K) occurred in the reporting year. An overview of the affiliated companies and information on principal places of business, equity capital, capital shares and results for the accounting period 2005 are set out in a separate summary starting on page 154.

GILDEMEISTER Aktiengesellschaft has entered into management and profit and loss transfer agreements with the following companies:

_ GILDEMEISTER Drehmaschinen GmbH,
_ DECKEL MAHO Seebach GmbH,
_ DMG Vertriebs und Service GmbH DECKEL MAHO GILDEMEISTER,
_ GILDEMEISTER Beteiligungen Aktiengesellschaft.

DMG Vertriebs und Service GmbH DECKEL MAHO GILDEMEISTER has entered into management and profit and loss transfer agreements with the following subsidiaries:

_ DMG Stuttgart Vertriebs und Service GmbH DECKEL MAHO GILDEMEISTER,
_ DMG Berlin Vertriebs und Service GmbH DECKEL MAHO GILDEMEISTER,
_ DMG Service Drehen GmbH DECKEL MAHO GILDEMEISTER,
_ DMG Service Fräsen Pfronten GmbH,
_ DMG Service Fräsen Seebach GmbH,
_ DMG Trainings-Akademie GmbH DECKEL MAHO GILDEMEISTER,
_ DMG Gebrauchtmaschinen GmbH DECKEL MAHO GILDEMEISTER,
_ a & f Stahl- und Maschinenbau GmbH (with effect from 1 Jan. 2005).

DMG Stuttgart Vertriebs und Service GmbH DECKEL MAHO GILDEMEISTER has entered into management and profit and loss transfer agreements with the following subsidiaries:
_ DMG München Vertriebs und Service GmbH für Werkzeugmaschinen DECKEL MAHO GILDEMEISTER,
_ DMG Hilden Vertriebs und Service GmbH DECKEL MAHO GILDEMEISTER,
_ DMG Bielefeld Vertriebs und Service GmbH DECKEL MAHO GILDEMEISTER,
_ DMG Frankfurt Vertriebs und Service GmbH DECKEL MAHO GILDEMEISTER.

Further management and profit and loss transfer agreements were entered into between DECKEL MAHO Geretsried GmbH and DECKEL MAHO Pfronten GmbH and between DECKEL MAHO Pfronten GmbH and SAUER GmbH. Another management and profit and loss transfer agreement was entered into between DECKEL MAHO Geretsried GmbH and GILDEMEISTER Beteiligungen Aktiengesellschaft.

21 LONG-TERM RECEIVABLES AND OTHER ASSETS

	31 Dec. 2005	31 Dec. 2004
	€ K	€ K
Trade debtors	**1,276**	2,249
Other long-term assets	**10,900**	22,403
	12,176	24,652

Existing individual risks were recognised by direct method of depreciation.
Other long-term assets include the following items:

	31 Dec. 2005	31 Dec. 2004
	€ K	€ K
Tax refund claims	**1,832**	1,240
Creditors with debit balance and advance payments	**529**	36
Receivables from employees and former employees	**36**	30
Security deposits and other security payments	**791**	247
Loans to third parties	**1**	158
Discounted customers' bills	**6,881**	19,862
Other	**830**	830
	10,900	22,403

22 INVENTORIES

Inventories are made up as follows:

	31 Dec. 2005	31 Dec. 2004
	€ K	€ K
Raw materials and consumables	**92,354**	92,510
Work in progress	**89,087**	87,374
Finished goods and goods for resale	**104,889**	95,143
Payments on account	**2,447**	1,538
	288,777	276,565

Inventories increased by € 12,212 K when compared with the previous year. This is primarily due to the increase in the inventory of work in progress, finished goods and goods for resale. Intercompany profits of € 15,775 K arose in inventories from intercompany supplies and deliveries (previous year: € 14,724 K) . Any differences against the previous year were consolidated and recognised in the Income Statement.

€ 62,106 K (previous year: € 63,833 K) of inventories recorded on 31 December 2005 were recognised at their net realisable values. In the financial year, depreciation of inventories in an amount of € 2,392 K were recognised as expense in the Income Statement.

23 Short-term receivables and other assets

	31 Dec. 2005	31 Dec. 2004
	€ K	€ K
Trade debtors	**286,822**	279,466
Other short-term assets	**61,600**	42,317
	348,422	321,783

Other short-term assets include the following items:

	31 Dec. 2005	31 Dec. 2004
	€ K	€ K
Tax refund claims	**11,249**	6,631
Creditors with debit balance and advance payments	**6,386**	7,784
Factoring settlement account	**10,378**	4,024
Receivables from employees and former employees	**1,356**	1,469
Security deposits and other security payments	**1,659**	2,527
Market values of derivative financial instruments	**1**	786
Loans to third parties	**1,012**	300
Receivables from compensation claims	**765**	360
Prepaid expenses	**4,925**	4,555
Discounted customers' bills	**18,266**	10,790
Other	**5,603**	3,091
	61,600	42,317

The accrued prepaid expenses primarily include interest, tenancy and insurance contributions. The remaining other assets include refund claims of € 1,057 K (previous year: € 0 K) with respect to additional compensation paid from part-time retirement agreements against the Federal Labour Office (Bundesanstalt für Arbeit).

24 Cash and Securities

At the balance sheet date, bank credit balances amounted to € 21,920 K (previous year: € 60,297 K).

The movement of liquid funds constituting the financial resources pursuant to IAS 7 “Cash Flow Statements” is illustrated in the Cash Flow Statement.

The securities of € 99 K (previous year: € 53 K) include securities available for sale that are shown at fair market values. These are held by GILDEMEISTER Aktiengesellschaft.

25 DEFERRED TAXES

Deferred tax assets and liabilities are allocated to the following accounts:

	31 Dec. 2005		31 Dec. 2004	
	Assets	Liabilities	Assets	Liabilities
	€ K	€ K	€ K	€ K
Fixed assets	3,760	12,614	2,058	14,262
Current assets	2,446	2,735	2,671	1,545
Provisions	3,856	3,479	3,232	882
Liabilities	6,133	3,991	5,577	3,685
Tax loss carried forward	18,280	-	24,041	-
Consolidation	10,289	2,264	5,882	2,329
	44,764	25,083	43,461	22,703
Balancing out	-17,095	-17,095	-18,664	-18,664
Total	27,669	7,988	24,797	4,039

The total deferred tax assets shown in the balance sheet of € 27,669 K (previous year: € 24,797 K) include capitalised tax reduction claims of € 18,280 K (previous year: € 24,041 K) arising from the expected future utilisation of existing losses carried forward. The realisation of these losses carried forward is guaranteed with sufficient security.

The valuation of deferred tax assets was adjusted if sufficient future income cannot be expected taking into account all impacting factors. The valuation applied is subject to changes depending on future development.

The tax losses carried forward amounted to € 75,997 K (previous year: € 84,819 K), of which € 17,472 K (previous year: € 13,562 K) were not recognised. Deductible temporary differences of € 3,071 K (previous year: € 0 K) are not included.

Deferred taxes are calculated on the basis of income tax rates that at the date of valuation apply or are expected in the individual countries in accordance with the current legal status.

Taking into account trade earnings tax and the solidarity surcharge (Solidaritätszuschlag), this results in a tax rate of 38% (previous year: 38%) for domestic companies. The tax rates abroad are between 19% and 41%.

26 EQUITY

The movement of individual components in group equity for the accounting periods 2005 and 2004 are illustrated in the Development of Group Equity.

Subscribed capital

The company's share capital is € 112,586,507.80. It is divided into 43,302,503 owner shares. The owner shares have an accounting par value of € 2.60.

The Executive Board is authorised, with the approval of the Supervisory Board, to increase the share capital by up to € 56,000,000.00 in nominal terms during the period until 15 May 2010 by issuing new owner shares for contributions in cash and/or in kind (authorised capital). This authority can be exercised on one occasion or, in partial amounts, on more occasions.

The new shares may be taken over by one or more banks designated by the Executive Board, with the obligation to offer them to the shareholders for subscription (direct subscription right).

With respect to a partial amount of € 5,000,000.00 the Executive Board will be authorised to issue shares to the employees of the company and of companies affiliated to the company. The shareholders' statutory subscription rights are excluded to this extent.

In addition, the Executive Board is authorised, with the approval of the Supervisory Board, to exclude the shareholders' statutory rights in the case of:

a) capital increases through non-cash capital contribution so as to acquire, in applicable cases, companies, sections of the company or participating interests in companies in return for the transfer of shares,
b) to the extent required for dilution protection purposes, in order to grant the holders of warrants or the creditors of convertible bonds issued by the company or its associated companies as part of an authorisation of the Board issued by the general meeting of shareholders, a subscription right to new shares to the extent they would be entitled to following the exercising of the option or conversion right or the fulfilment of conversion obligations.
c) to exclude any residual amounts from the subscription right, and
d) capital increase through cash contribution, if the issue price of the new shares is not significantly lower than the exchange price at the time the issue price is finally defined by the Board within the meaning of section 203 paragraphs 1 and 2, and section 186 paragraph 3 sentence 4 of the German Companies Act (AktG), and the prorated amount of the share capital relating to the new shares that are subject to the exclusion of the subscription right, in aggregate does not exceed 10% of the share capital at the time the new shares are issued. The limit of 10% of the share capital includes shares that are sold during the lifespan of the authorised capital to the exclusion of the shareholders' subscription rights pursuant to section 71 paragraph 1 no. 8 sentence 5 and section 186 paragraph 3 sentence 4

of the German Companies Act (AktG), and shares with respect to which a conversion right or option right or a conversion obligation or option obligation due to option and / or convertible bonds exists and that were issued by virtue of authorisation of the general meeting of shareholders from 14 May 2004 to the exclusion of the subscription right pursuant to section 221 paragraph 4 section 186 paragraph 3 sentence 4 of the German Companies Act (AktG). The Executive Board is authorised, with the approval of the Supervisory Board, to lay down further details for the capital increase and its implementation.

The share capital has been conditionally increased by up to a further € 37,500,000.00 through the issue of up to 14,423,076 owner shares (conditional capital I). The conditional capital increase is to be effected only in so far as the options or conversion rights relating to warrant or convertible bonds, issued or granted by the company or a 100% indirect or direct holding company of the company pursuant to an authorising resolution passed by the general meeting of shareholders held on 14 May 2004 in the period up to 31 March 2009, are exercised or any conversion obligation or obligation to exercise an option under the above named bonds are fulfilled. The new shares will be issued at an option or conversion price to be determined in accordance with the above named authorising resolution. The new shares will profit as of the beginning of the financial year, in which they are issued following the exercising of options or conversions rights, or the fulfilment of conversion or option obligations. The Executive Board is authorised, with the approval of the Supervisory Board, to lay down further details for the implementation of the conditional capital increase.

Capital provisions

Capital provision includes the share premium of € 71,297,862. In the accounting period 2004, transaction costs of € 4,788,596 that can be allocated directly to the capital procurement, reduced by related benefits arising from tax on income of € 1,810,089 have been deducted from the capital provision in accordance to SIC 17. The capital provision of € 68,319,355 has not changed since the previous year.

Revenue provisions

Statutory provisions

The statutory provision of € 680,530 has not changed since the previous year.

Other revenue provisions

Revenue provisions include prior-period profits generated by the companies included in the Consolidated Financial Statements as far as they were not distributed. Revenue provisions also include the offset of liabilities-side differences from the consolidation of investments of those subsidiaries that were consolidated before 1 January 1995, and the adjustments directly in equity in accordance with the first application of IFRS rules. Finally, they show the differences arising from foreign currency translation in the financial statements not affecting net income of international subsidiaries, recognised directly in equity, and the post-tax effects from the valuation of financial instruments, recognised directly in equity. Deferred taxes recognised directly in equity amount to € 0 K (previous year: € 38 K).

A detailed overview on the composition of, or changes in, other revenue provisions in the accounting period 2005 and in the previous year is included in the Development of Group Equity.

Proposed appropriation of earnings

In accordance with the German Companies Act (AktG), the Annual Financial Statements of GILDEMEISTER Aktiengesellschaft form the basis for the appropriation of profits of the financial year. The dividend to be distributed to shareholders is therefore subject to the retained profits shown in the Annual Financial Statements of GILDEMEISTER Aktiengesellschaft.

The financial year 2005 of GILDEMEISTER Aktiengesellschaft closes with an annual profit of € 26,838,813.35. The Executive Board and Supervisory Board will propose to the general meeting of shareholders to be held on 19 May 2006 to appropriate the earnings of € 13,400,000.00 retained after transfer to other revenue provisions of € 13,438,813.35 as follows:

- to distribute € 4,330,250.30 to the shareholders by dividend payout of € 0.10 per share,
- to carry the remaining balance of € 9,108,563.05 forward to new account.

Shares held to other shareholders

Shares held to other shareholders include minority interests in the consolidated equity of the companies included and, in the financial year 2005, amount to € -138 K (previous year: € 1,037 K) .

27 PENSION PROVISIONS

Company pension provisions are set up for obligations arising from legal rights to future pension payments and from current pension payments to entitled, active and former employees at companies of the GILDEMEISTER group and their surviving dependants. According to the respective legal, economic and tax conditions prevailing in each country, there are different forms of old age protection that are usually based on the duration of employment and the employees’ remuneration.

Employee pension schemes are usually based on either contribution-oriented or performance-oriented benefit systems.

In the case of contribution-oriented pension plans ("defined contribution plans") the respective company does not assume any further obligations which go beyond the payment of contributions into an earmarked reserve fund. In the financial year 2005, related expenses amounted to € 17,246 K (previous year: € 16,680 K). The company's contributions to the statutory pension insurance amounting to € 14,547 K (previous year: € 13,798 K) are included.

In the case of benefit-oriented pension plans it is the company's obligation to pay the promised benefits to active and former employees ("defined benefit plans"), whereby one distinguishes between pension plans that are financed through reserves and those that are financed through a fund.

In the GILDEMEISTER group, pension commitments are financed through transfer to provisions.

The amount of the pension obligation (present value of future pension commitments or "defined benefit obligation") was calculated on the basis of actuarial methods by estimating the relevant factors impacting the pension commitment. Along with the assumptions on life expectancy, the following premises for the parameters to be applied to the actuarial calculations in the reports were defined:

	Germany		Remaining countries	
	2005	2004	**2005**	2004
	%	%	%	%
Interest rate	4.00	4.85	3.00–3.50	3.00–4.00
Salary trend	0.00	0.00	2.00–3.00	3.00
Pension trend	1.75	1.50	0.00	0.00

The pension development includes expected future increases in salary that are assessed annually and are subject to, amongst other things, inflation and the duration of employment at the company. Since the pension commitments that were entered into at the domestic subsidiaries are not subject to future increases in salary, salary development was not taken into account when determining the relating company pension provisions.

Due to increases or reductions in the present value of defined-benefit obligations, actuarial gains or losses may arise, which may result, amongst others, from changes in the calculation parameters or changes in the risk development assessment relating to the pension commitments. The pension provisions net value can be derived from the following:

		31 Dec. 2005	31 Dec. 2004
		€ K	€ K
	Cash value of provisions-financed pension commitments	38,337	33,726
–	Balance of actuarial profits/losses not yet recognised in the balance sheet	-10,858	-6,003
=	Net value of amounts shown in the balance sheet on the reporting date	27,479	27,723

Of the company pension provisions amounting to € 27,479 K (previous year: € 27,723 K), € 27,160 K (previous year: € 27,452 K) are attributed to domestic group companies, representing about 99% of the total.

The changes of the cash value over the previous year are due to the use of the new reference tables by Prof. Dr. Klaus Heubeck that were initially published in July 2005, the adjustment of the underlying interest rate from 4.85% to 4.0% and the change in the number of pensioners included the calculations.

In the financial year 2005, total expenditure amounted to € 2,209 K (previous year: € 1,932 K), comprising of the following components:

		2005	2004
		€ K	€ K
	Current expenditure of service	165	132
+	Interest expenditure	1,638	1,703
+	Actuarial profits (-) and losses (+)	406	97
=	Total expenditure of payment-oriented pension plans	2,209	1,932

		2005	2004
		€ K	€ K
	Balance sheet value as at 1 January	27,723	28,073
+	Personnel costs	2,209	1,932
–	Pension payments made	-2,453	-2,282
=	Balance sheet value as at 31 December	27,479	27,723

28 OTHER PROVISIONS

The following lists the major contents of provisions:

	31 Dec. 2005 Total	31 Dec. 2005 of which short term	31 Dec. 2004 Total	31 Dec. 2004 of which short term
	€ K	€ K	€ K	€ K
Tax provisions	10,035	10,035	8,802	8,802
Obligations arising from personnel	48,726	26,409	44,715	23,880
Risks arising from warranties and retrofitting	24,765	24,765	25,293	25,293
Obligations arising from sales	8,044	8,044	8,729	8,729
Legal and consultancy fees and costs of preparation of accounts	2,542	2,542	2,948	2,948
Anticipated losses related to incomplete contracts	305	305	350	350
Other	3,511	3,511	4,896	4,896
	87,893	65,576	86,931	66,096
Total	**97,928**	**75,611**	95,733	74,898

Tax provisions include taxes on corporate income and business profits and other company taxes that were set up for prior accounting periods and for the accounting period 2005.

Provisions for personnel costs in the group include € 8,455 K for part-time retirement (previous year: € 8,359 K) and € 4,799 K for anniversary bonuses (previous year: € 3,994 K). The provisions for anniversary bonuses and part-time retirement will be discounted and carried as liability at their present value. Obligations arising from part-time retirement are secured against potential insolvency through a mutual trust relationship. To secure the pension plan, cash assets are transferred into a trust property. The members of this trust property are domestic group companies.

The assets are defined as “plan assets” in accordance with IAS 19.7 and balanced against the related provision. Any proceeds arising from the pension plan assets are balanced against the related expenses. On 31 December 2005, liquid assets of € 3,706 K (previous year: 2,826 K) were transferred into the trust property.

Risks arising from warranties and retrofitting relate to present obligations to third parties, the use of which is probable and the anticipated amount of which can be reliably estimated. Due to previous experience, valuations of provisions were carried out on the basis of the conditions on the balance sheet date.

The other obligations primarily include provisions for installations to be carried out, invoiced sales and other various services.

The movement in the other provisions is illustrated in the Analysis of Provisions:

	01 Jan. 2005	Transfers	Used	Retransfers	Other changes	31 Dec. 2005
	€ K	€ K	€ K	€ K	€ K	€ K
Tax provisions	8,802	7,005	5,947	21	196	10,035
Obligations arising from personnel	44,715	26,366	20,954	1,803	402	48,726
Risks arising from warranties and retrofitting	25,293	11,038	7,222	4,402	58	24,765
Obligations arising from sales	8,729	7,792	7,355	1,358	236	8,044
Legal and consultancy fees and costs of preparation of accounts	2,948	2,406	2,586	258	32	2,542
Anticipated losses related to incomplete contracts	350	305	350	0	0	305
Other	4,896	2,646	2,872	1,299	140	3,511
	86,931	50,553	41,339	9,120	868	87,893
Total	**95,733**	57,558	47,286	9,141	1,064	**97,928**

Other changes include the change in foreign currency adjustments and book transfers.

29 FINANCIAL LIABILITIES

Details of short-term and long-term financial liabilities are listed in the following table:

	31 Dec. 2005	of which due within 1 year	of which due within 1 to 5 years	of which due within 5 years	31 Dec. 2004 [2]
	€ K	€ K	€ K	€ K	€ K
Bond	168,435	0	0	168,435	167,585
Bank loans and overdrafts [1]	116,736	25,543	77,253	13,940	156,733
Discounted customers' bills	25,147	18,266	6,881	0	30,652
	310,318	43,809	84,134	182,375	354,970
Outstanding in each maturity period at 31 Dec. 2004 [2]		34,953	136,716	183,301	354,970

[1] of which secured by mortgage: € 38,451 K (previous year: € 39,328 K)
[2] adjusted due to application of IAS 39 with respect to discounted customers' bills

In July 2004 GILDEMEISTER Aktiengesellschaft issued a long-term, secondary corporate bond. The bond with a nominal volume of € 175.0 million and a coupon of 9.75% p.a. will mature in July 2011. Pursuant to IAS 39 “Financial Instruments: Recognition and Measurement” all allocable transaction costs of originally € 7,819 K were deducted from the liabilities of the bond and will be allocated over maturity of the bond. An amount of € 850 K (previous year: € 404 K) was allocated to the accounting period 2005.

The group companies DECKEL MAHO Geretsried GmbH, DECKEL MAHO Pfronten GmbH, DECKEL MAHO Seebach GmbH, GILDEMEISTER Drehmaschinen GmbH, GILDEMEISTER Beteiligungen Aktiengesellschaft, DMG Vertriebs und Service GmbH DECKEL MAHO GILDEMEISTER, FAMOT PLESZEW S.A. and GILDEMEISTER Italiana S.p.A. are guarantors in relation to the loan agreement. In addition, the shares of the above companies to the nominal value of € 101,195 K (previous year: € 96,177 K) are secondarily pledged in favour of the bond holders. Set out below are the major liabilities to financial institutions:

	31 Dec. 2005				31 Dec. 2004			
	Currency	Carrying amount	Remaining term in years	Effective interest rate	Currency	Carrying amount	Remaining term in years	Effective interest rate
		€ K		%		€ K		%
Loans	EUR	49,800	up to 12	3.05–10.90	EUR	63,425	up to 13	3.05–10.90
Loans	JPY	1,710	up to 7	0.95–2.50	JPY	1,944	up to 8	0.95–2.50
Overdraft facilities	various	65,226	up to 1.5	1.90–6.50	various	91,364	up to 2.5	1.90–6.50
		116,736				156,733		

The reduction in liabilities to financial institutions of € 39,997 K in comparison to the previous year is due to the scheduled repayment of long-term loans, as well as to a lower availment of overdrafts. As at 31 December 2005, the international share in liabilities to financial institutions therefore amounts to approximately 25.38% (previous year: approx. 18.57%).

The short and medium term resource requirements of GILDEMEISTER Aktiengesellschaft and, as part of the intragroup cash management system, of the majority of domestic subsidiaries are covered through a syndicated loan agreement. The syndicated loan has a term until 30 June 2007 and a volume of € 141.0 million. The lending volume contains three tranches, which differ in terms of amounts, usability, maturity/drawing terms and the agreed interest rates. In favour of the lending banks, the shares of DECKEL MAHO Pfronten GmbH, DECKEL MAHO Seebach GmbH, DECKEL MAHO Geretsried GmbH, GILDEMEISTER Drehmaschinen GmbH, DMG Vertriebs und Service GmbH DECKEL MAHO GILDEMEISTER, GILDEMEISTER Beteiligungen Aktiengesellschaft, FAMOT PLESZEW S.A. and GILDEMEISTER Italiana S.p.A., to the nominal value of € 101,195 K (previous year: € 96,177 K) were pledged in first place to the national banking consortium. The above group companies are also guarantors to the loan agreement.

As further securities for loans, fixed and current assets in an amount of € 6,822 K were assigned to the lending banks by DECKEL MAHO Seebach GmbH, in an amount of € 2,745 K by SAUER GmbH and by various DMG sales companies.

For the liabilities to financial institutions of € 116,736 K (previous year: € 156,733 K) no significant differences between book and market value arise due to the short-term conditions. In other payables, the fair market values of short-term liabilities and of medium and long-term liabilities correspond with the values shown in the balance sheet. Liabilities that, in legal terms, arise after the balance sheet date, are of minor economic significances.

The value of the bond shown in the Consolidated Financial Statements falls below the fair market value by € 29,315 K (previous year: € 22,203 K). The fair market value is determined by the price of the bond at the balance sheet date.

30 LIABILITIES ARISING FROM BILLS OF EXCHANGE

As of 31 December 2005, liabilities arising from bills of exchange amounted to € 16,773 K (previous year: € 19,427 K) and had a remaining term of up to one year. They include liabilities arising from the acceptance of drafts and the issue of promissory notes.

31 TRADE CREDITORS AND OTHER LONG-TERM LIABILITIES

Trade creditors include long-term amounts of € 1,787 K (previous year: € 1,325 K). Other long-term liabilities of € 8,128 K (previous year: € 7,878 K) primarily include liabilities arising from finance leases of € 2,536 K (previous year: € 2,381 K).

Pursuant to IAS 20 “Accounting for Government Grants and Disclosure of Government Assistance”, this account also includes investment allowances and investment subsidies in accordance with the German Investment Subsidy Law (Investitionszulagengesetz) totalling € 3,625 K (previous year: € 3,747 K) granted by the joint aid programme “Improvement of the Regional Economic Structure”. In the accounting period 2005 investment subsidies of € 89 K (previous year: € 114 K) were received that were allocated to deferred income. This item will be closed in accordance with the depreciation procedure for privileged assets and recognised in the Income Statement.

32 TRADE CREDITORS AND OTHER SHORT-TERM LIABILITIES

	31 Dec. 2005	31 Dec. 2004
	€ K	€ K
Payments received on account	32,486	27,678
Trade payables	143,106	139,121
Other short-term liabilities	49,641	42,213
	225,233	209,012

Other short-term liabilities include the following items:

	31 Dec. 2005	31 Dec. 2004
	€ K	€ K
Tax liabilities	**16,188**	11,558
Liabilities relating to social insurance	**7,187**	7,678
Payroll account liabilities	**3,003**	2,474
Liabilities arising from finance lease	**2,538**	1,631
Debtors with credit balance	**3,809**	2,990
Fair market values of derivative financial instruments	**2,799**	942
Liabilities from accrued interest paid on the corporate bond	**7,631**	7,631
Deferred income	**4,407**	3,438
Other liabilities	**2,079**	3,871
	49,641	42,213

Liabilities arising from short-term finance leases amounted to € 2,538 K (previous year: € 1,631 K). They are recognised, without future interest payable, under other liabilities. All future payments arsing from finance leases total € 5,457 K (previous year: € 4,490 K).

The minimum lease payments from the respective lease agreements are as follows:

	31 Dec. 2005	31 Dec. 2004
	€ K	€ K
Total future minimum lease payments		
Due within one year	**2,766**	1,846
Due within one and five years	**2,686**	2,639
Due in more than five years	**5**	5
	5,457	4,490
Interest component included in future minimum lease payments		
Due within one year	**228**	215
Due within one and five years	**155**	262
Due in more than five years	**0**	1
	383	478
Net present value of future minimum lease payments		
Due within one year	**2,538**	1,631
Due within one and five years	**2,531**	2,377
Due in more than five years	**5**	4
	5,074	4,012

Current liabilities from accrued interest paid are due to the accrual-based recognition of interest paid on the bond of € 7,631 K for the period 19 July 2005 to 31 December 2005 that will be paid in January 2006.

At an amount of € 782 K (previous year: € 1,440 K) deferred income results from the subgroup GILDEMEISTER Italiana and pertains to deferred future interest earnings from a specific financing programme of the Italian state (Sabatini funding). It also includes further deferred income from sale and leaseback transactions that resulted in finance lease relations.

33 CONTINGENCIES AND OTHER FINANCIAL OBLIGATIONS

No provisions were set up for the following contingent liabilities, which are assessed at their nominal values, since the risk of usage is deemed as not very probable:

	31 Dec. 2005	31 Dec. 2004
	€ K	€ K
Contingencies		
Guarantees	**7,650**	4,143
Warranties	**3,921**	8,170
Other contingencies	**17,019**	16,147
	28,590	28,460

Other financial obligations consist mainly of lease agreements and long-term tenancy agreements. In operating lease agreements, the beneficial owner of the leased items is the lessor, which means risks and rewards are borne by the lessor, who thereby also carries the investment risk.

The total of minimum lease payments from permanent tenancies and lease agreements (finance lease and operating lease relations) is made up, as set out below, by due dates. The agreements have terms of 2 to 20 years; some of them include options to extend or purchase options.

	31 Dec. 2005	31 Dec. 2004
	€ K	€ K
Total face value of future minimum lease payments		
Due within one year	**19,827**	19,702
Due within one and five years	**26,597**	23,674
Due in more than five years	**3,742**	4,055
	50,166	47,431

Of which are attributed to operating lease relations:

	31 Dec. 2005	31 Dec. 2004
	€ K	€ K
Total face value of future minimum lease payments		
Due within one year	**17,061**	17,856
Due within one and five years	**23,911**	21,035
Due in more than five years	**3,737**	4,050
	44,709	42,941

The operating lease relations result primarily from a basic agreement with a total volume of € 17.0 million on the operating lease of machines used for shows and exhibitions entered into between the German production facilities and the DMG companies. This agreement has a basic term of 4 years and may be terminated after 3 months. Following the expiry of the agreement, the lease may be extended or the lease items may be either returned or purchased. Due to the contractual conditions the majority of the risks is attributet to the lessor.

Further operating lease agreements include an operating lease to the value of € 5.3 million entered into in relation with the funding of a building at DMG Europe Holding GmbH in Klaus, Austria, an operating lease for machines to the value of € 3.3 million entered into by FAMOT Pleszew S.A., Poland, and operating leases for machines, fleet of vehicles and other equipment and factory and office equipment entered into by other group companies. The agreements have terms of 3 to 14.5 years and some of them include purchase options at the end of the basic lease term.

There are no permanent subtenancies that have to be included in the total of future minimum lease payments. There are no contingent rents that are recognised in the Income Statements.

Tangible assets commitments amount to € 10,705 K (previous year: € 1,863 K). The change over the previous year is due primarily to investments in the development of the IT infrastructure at the GILDEMEISTER group planned for the financial year 2006.

34 DERIVATIVE FINANCIAL INSTRUMENTS

The face and fair market values of derivative financial instruments existing at the balance sheet date are set out below:

	Face values		Fair market values	
	31 Dec. 2005	31 Dec. 2004	31 Dec. 2005	31 Dec. 2004
	€ K	€ K	€ K	€ K
Forward exchange dealings	96,174	40,632	-2,767	598
Interest rate swaps	10,163	70,487	-77	-753
	106,337	111,119	-2,844	-155

The face values correspond with the non-balanced total of the currency and interest portfolio. The fair market values shown correspond with that price, at which third parties would assume the rights or obligations arising from the financial instruments. The fair market values are the current values of the derivative financial instruments excluding any adverse trends in value from underlying transactions. The fair market values of the derivative financial instruments used are determined on the basis of quoted market prices or through accrual methods based on customary models.

All of the forward exchange dealings carried out mature within one year with the exception of a future with a total volume of € 1,065 K (previous year: € 0 K), which will mature in more than a year.

Interest rate swaps are used by the group company GILDEMEISTER Italiana S.p.A., Brembate di Sopra (Bergamo), Italy and mature within half a year. They provide for payment of fixed interests within a 2.48%–5.42% p.a. margin and a 3-month Euribor as reference rate. The changes in fair market values of € 497 K (previous year: € 715 K) were recognised in the Income Statement.

In the accounting period 2005, effects of € 1,891 K (previous year: € 224 K) arising from the market valuation of financial instruments alloted to cash flow hedges were recognised directly in equity on an accrual basis.

Notes to the Cash Flow Statement

35 CASH FLOW STATEMENT

The Cash Flow Statement pursuant to IAS 7 “Cash Flow Statements” records the payment flow in a financial year and represents the inflow and outflow of the company’s liquid funds. The payment flow is distinguished between cash flow from current operations and cash flow from investment and financing activity.

The financing resources set out in the Cash Flow Statement includes all liquid funds stated in the balance sheet, i.e. cash in hand, Bundesbank balance and bank balances to the extent that these are available within three months.

The cash flow from current operations was calculated by the indirect method through adjusting the group’s annual result by changes in inventories, trade receivables and payables, non-cash items and all other items showing cash flows in the investment or financing areas. The cash flows from the investment or financing activity were each calculated in terms of actual sums paid. Effects from foreign currency translation and changes in the consolidated group are adjusted accordingly.

The financial investments of the financial year 2005 include the acquisition of the remaining 49% shares in DMG Austria GmbH, Klaus, Austria, at a purchase price of € 740 K. The purchase price will be settled in two instalments. The first instalment of € 400 K was due in November 2005 and was fully settled in cash. The second instalment is € 340 K and is due in February 2006. No cash was taken over with the acquisition.

Notes to segmental reporting

36 EXPLANATORY NOTES TO SEGMENTS

In segmental reporting pursuant to IAS 14 “Segment Reporting”, the business activities of the GILDEMEISTER group are distinguished between business segments requiring primary segment reporting and geographical areas requiring secondary segment reporting.

The business activities of the GILDEMEISTER group consist of the "Machine Tools", “Services” and “Corporate Services” segments. This segmentation follows the group’s management and control. Each group company is allocated to the segment pertaining to its respective economic activities. The **“Machine Tools”** segment covers the group’s new machines business and includes the “turning”, “milling” and “ultrasonic/lasertec” technologies. This includes the lathes and turning centres of

_ GILDEMEISTER Drehmaschinen GmbH, Bielefeld,
_ GILDEMEISTER Italiana S.p.A., Brembate di Sopra (Bergamo), Italy,
_ GRAZIANO Tortona S.r.l., Tortona, Italy,
_ FAMOT Pleszew S.A., Pleszew, Poland,
_ DECKEL MAHO GILDEMEISTER (Shanghai) Machine Tools Co., Ltd., Shanghai, China,

the milling machines and machining centres of

_ DECKEL MAHO Pfronten GmbH, Pfronten,
_ DECKEL MAHO Seebach GmbH, Seebach,
_ DECKEL MAHO GILDEMEISTER (Shanghai) Machine Tools Co., Ltd., Shanghai, China,

the ultrasonic and laser machines of

_ SAUER GmbH, Idar-Oberstein/Kempten.

All of our machines are classified as cutting machine tools, and all business segments are concurrent with each other.

The **“Services”** segment, which covers all areas, is directly related to the machine tools and, with its products and technical services offered, represents an independent segment. It substantially includes DMG Vertriebs und Service GmbH DECKEL MAHO GILDEMEISTER, Bielefeld, and its subsidiaries.

Across the entire lifespan of a machine tool, customers are offered a comprehensive range of high-quality services and service products. The Service Support offers services provided by our highly qualified service staff. Their worldwide network ensures direct contact with the customer and prompt availability. Along with introduction and consulting services, this includes the traditional maintenance and service activities, the installations and initial training, the vocational and further training provided by DMG Trainingsakademie GmbH, the retrofitting of machines and the used machines business. This objective is supported by our service products that complete the range of products offered by the Service segment. They comprise the DMG spare parts, the innovative software solutions of DMG Powertools, the machine tool components of SACO S.p.A., the setting equipment and tool management of DMG Microset GmbH and the procurement services provided by a & f Stahl- und Maschinenbau GmbH. Another area is key accounting, the management of our major customers, which has been centralised to include all areas and products in order to meet the increasing globalisation of international companies.

The **"Corporate Services"** segment primarily consist of GILDEMEISTER Aktiengesellschaft with its group-wide holding functions, such as group strategy, development and purchasing coordination, management of overall projects in the logistics and production areas, funding, corporate controlling and corporate personnel management as well as group-standardised IT.

37 EXPLANATORY NOTES TO SEGMENTAL INFORMATION

The definition of terms used in individual segmental information is in line with the management principle for value-oriented corporate governance at the GILDEMEISTER group. Segmental information is in principle based on the same accounting and valuation methods as the Consolidated Financial Statements.

Segmental assets include all assets tied up in the business including goodwill and prepaid expenses; it does not include income tax claims.

As part of the exercising of the voting right pursuant to IFRS 3 "Business Combinations", goodwill was allocated to the segments as follows: Goodwill of € 38,258 K (previous year: € 38,258 K) is alloted to the "Machine Tools" segment, € 29,671 K (previous year: € 29,671 K) to the "Services" segment and € 0 K (previous year: € 0 K) to the "Corporate Services" segment.

There was no impairment of goodwill in the accounting period.
Segmental debts consist of outside capital and financial liabilities including provisions and deferred income; they do not include income tax liabilities.

Investments include the additions to tangible fixed assets and intangible assets. Depreciation pertains to segmental fixed assets. In the accounting period non-cash expenses were incurred in the "Corporate Services" segment due to the accrual of costs of transactions with respect to financial instruments in an amount of € 2,398 K. No major non-cash expenses were incurred in the two other segments.

The "Reconciliation" column represents the elimination of intercompany receivables and liabilities, income and expenses and results between the segments.

The secondary segmentation is based on the corporate seats of the group companies and is divided into the geographical areas: Germany, rest of Europe, North America, Asia and rest of the world, which includes Mexico and Brazil.

In the presentation of secondary segmentation, data is determined on the basis of regional subgroups.

Other explanatory notes

38 Auditor's fees and services

In the accounting period 2005, the fees of the auditor of the Consolidated Financial Statements KPMG Deutsche Treuhand-Gesellschaft, Aktiengesellschaft, Wirtschaftsprüfungsgesellschaft amounted to € 736 K. This includes the fees for the group audit and the audit of the statutory financial statements of GILDEMEISTER Aktiengesellschaft and its domestic subsidiaries. A further amount of € 403 K for other services was also charged to expenses.

39 Events occurring after the balance sheet date

Up to the date of submittal to the Supervisory Board on 23 March 2006, material events have not occurred after the Balance Sheet Date or are set out in the Supplementary Report chapter and the Forecast Report of the Group Management Report.

40 Information about relationships to related companies and persons

Related companies and persons within the meaning of IAS 24 "Related Party Disclosures" are, in principle, members of the Executive Board and the Supervisory Board, close members of their families and subsidiaries that are not fully consolidated. Related persons were not party to any major transaction or any transaction of unusual nature or structure with companies of the GILDEMEISTER group.

Sales between the GILDEMEISTER group and non-consolidated companies are of secondary importance.

41 Corporate governance

The declaration of compliance in accordance with Section 161 AktG was made on 8 September 2005 and has been permanently made accessible to the shareholders on our website **www.gildemeister.com**.

Affiliated companies

		Equity [1]		Participation quota	Result for the accounting period 2005 [1]
	National currency		€ K	in %	in € K
Production plants, sales and service companies, procurement/components					
GILDEMEISTER Drehmaschinen GmbH, Bielefeld [2/4]			16,650	100.0	0
GILDEMEISTER Italiana S.p.A., Brembate di Sopra (Bergamo), Italy			58,601	100.0	5,241
GRAZIANO Tortona S.r.l., Tortona, Italy [3]			3,165	100.0	165
SACO S.p.A., Castelleone, Italy [3]			9,761	100.0	-149
GRAZIANO Immobiliare S.r.l., Tortona, Italy [3]			2,586	100.0	-611
DMG Italia S.r.l., Brembate di Sopra, Italy [3]			3,500	100.0	52
GILDEMEISTER Beteiligungen Aktiengesellschaft, Bielefeld [2]			62,909	100.0	0
DECKEL MAHO Geretsried GmbH, Geretsried [4/5/6/7]			49,624	100.0	0
DECKEL MAHO Pfronten GmbH, Pfronten [4/8/9]			28,222	100.0	0
SAUER GmbH, Stipshausen/Idar-Oberstein [4/10/11]			6,942	98.8	0
DECKEL MAHO Seebach GmbH, Seebach [2/4]			8,363	100.0	0
FAMOT Pleszew S.A., Pleszew, Poland	PLN K	19,044	4,923	100.0	580
DECKEL MAHO GILDEMEISTER (Shanghai) Machine Tools Co., Ltd., Shanghai, China	CNY K	44,211	4,629	100.0	-870
DMG Vertriebs und Service GmbH DECKEL MAHO GILDEMEISTER, Bielefeld [2/4/5]			50,375	100.0	
DMG Stuttgart Vertriebs und Service GmbH DECKEL MAHO GILDEMEISTER, Leonberg [4/5/12/13]			45,001	100.0	
DMG München Vertriebs und Service GmbH DECKEL MAHO GILDEMEISTER, Munich [4/5/14/15]			929	100.0	
DMG Hilden Vertriebs und Service GmbH DECKEL MAHO GILDEMEISTER, Hilden [4/5/14/15]			935	100.0	
DMG Bielefeld Vertriebs und Service GmbH DECKEL MAHO GILDEMEISTER, Bielefeld [4/5/14/15]			957	100.0	
DMG Berlin Vertriebs und Service GmbH DECKEL MAHO GILDEMEISTER, Berlin [4/5/13/14]			301	100.0	
DMG Frankfurt am Main Vertriebs und Service GmbH DECKEL MAHO GILDEMEISTER, Bad Homburg [4/5/14/15]			310	100.0	
GILDEMEISTER Italiana Deutschland GmbH, Leonberg [4/5/14]			25	100.0	
DMG Europe Holding GmbH, Klaus, Austria [12]			40,883	100.0	
DMG Russland o.o.o., Moscow, Russia [16]	RUB K	36,912	1,087	99.0	
DMG Istanbul Makine Tikaret ve Servis Limited Sirketi, Istanbul, Turkey [16]	TRL K	1,285	806	100.0	
DMG Asia Pacific Pte. Ltd., Singapore [16]	SGD K	7,869	3,997	100.0	
DMG Australia Pty. Ltd., Clayton Victoria, Australia [17]	AUD K	3,983	2,467	100.0	
DMG (Thailand) Co. Ltd., Bangkok, Thailand [17]	THB K	3,719	76	100.0	
DMG Austria GmbH, Klaus, Austria [16]			1,400	100.0	
DMG Malaysia SDN BHD, Puchong/Kuala Lumpur, Malaysia [16]	MYR K	2,047	457	100.0	
DMG Nippon K.K., Yokohama, Japan [16]	JPY K	46,366	333	100.0	
DMG Benelux B.V., Veenendaal, Netherlands [16]			19,010	100.0	
DMG Paris S.a.r.l., Les Ulis, France [18]			3,588	100.0	
DMG (Schweiz) AG DECKEL MAHO GILDEMEISTER, Dübendorf, Switzerland [18]	CHF K	9,094	5,847	100.0	
DMG (U.K.) Ltd., Luton, Great Britain [18]	GBP K	1,988	2,894	100.0	
DMG Benelux BVBA - SPRL., Zaventem, Belgium [18]			1,385	100.0	
DECKEL MAHO GILDEMEISTER Iberica S.L., Berriz, Spain [18]			525	100.0	
DMG Czech s.r.o., Brno, Czech Republic [18]	CZK K	86,870	2,997	100.0	
DMG Polska Sp.z o.o., Pleszew, Poland [18]	PLN K	7,013	1,813	100.0	

Affiliated companies

		Equity [1]		Participation quota	Profit / loss for the accounting period 2005 [1]
		National currency	€ K	in %	in € K
Production plants, sales and service companies, procurement/components					
DMG America Inc., Charlotte, USA [18]	USD K	12,521	10,580	100.0	
DMG Chicago Inc., Schaumburg, USA [19]	USD K	808	683	100.0	
DMG Houston Inc., Houston, USA [19]	USD K	823	695	100.0	
DMG Los Angeles Inc., Los Angeles, USA [19]	USD K	1,432	1,210	100.0	
DECKEL MAHO GILDEMEISTER Brasil Ltda., São Paulo, Brasil [18]	BRL K	1,605	582	100.0	
DMG Canada Inc., Toronto, Canada [12]	CAD K	106	77	100.0	
DECKEL MAHO GILDEMEISTER México, S.A. de C.V., Monterrey, Mexico [12]	MXN K	2,685	213	100.0	
DMG Technology Trading (Shanghai) Co. Ltd., Shanghai, China [12]	CNY K	7,567	792	100.0	
DMG DECKEL MAHO GILDEMEISTER (India) Pvt. Ltd., Bangalore, India [12]	INR K	50,513	948	100.0	
DMG Machinery Taiwan Ltd., Taichung, Taiwan [12]	TWD K	92,649	2,379	100.0	
DMG Korea Ltd., Seoul, Korea [12]	KRW K	2,490,779	2,091	100.0	
DMG Service Drehen GmbH DECKEL MAHO GILDEMEISTER, Bielefeld [4/5/12/13]			1,500	100.0	
DMG Service Fräsen Pfronten GmbH, Pfronten [4/5/12/13]			1,559	100.0	
DMG Service Fräsen Seebach GmbH, Seebach [4/5/12/13]			1,171	100.0	
DMG Gebrauchtmaschinen GmbH DECKEL MAHO GILDEMEISTER, Geretsried [4/5/12/13]			7,517	100.0	
DMG Gebrauchtmaschinen Czech s.r.o., Zlin, Czech Republic [20]	CZK K	11,693	403	100.0	
DMG Trainings-Akademie GmbH DECKEL MAHO GILDEMEISTER, Bielefeld [4/5/12/13]			271	100.0	
DMG MICROSET GmbH, Bielefeld [4/5/12]			668	100.0	
a & f Stahl- und Maschinenbau GmbH, Würzburg [4/5/12/13]			1,112	100.0	
Other					
MITIS Grundstücks-Vermietungs Gesellschaft mbH & Co. Objekt Bielefeld KG, Düsseldorf [21]			-	98.0	
DMG Marketing & Services SND BHD, Selangor, Malaysia [12]	MYR K		-	40.0	
BIL Leasing GmbH & Co 736 KG, Munich [22]			-		
BIL Leasing GmbH & Co 748 KG, Munich [23]			-		
Zarzad Blokow Mieszkalnych Spolka z o.o., Pleszew, Poland [24]	PLN K	294	76	100.0	
Chemnitzer Grundbesitz Limited, Birmingham, Great Britain [25]	GBP K	17	25	94.9	

1) The figures correspond with the financial statements prepared in accordance with local regulations; they do not show the respective companies' contribution to the Consolidated Financial Statements. Foreign currencies with respect to equity were translated at the market price on reporting date.
2) Management and profit and loss transfer agreement with GILDEMEISTER Aktiengesellschaft
3) Participating interest of GILDEMEISTER Italiana S.p.A.
4) The domestic subsidiary has complied with the conditions required by Section 264 para. 3 HGB (German Commercial Code) regarding the application of the exemption regulations and therefore waives the disclosure of its annual financial statements and relating documents.
5) The domestic subsidiary has complied with the conditions required by Section 264 para. 3 HGB (German Commercial Code) regarding the application of the exemption regulations and therefore waives the preparation of a management report.
6) Participating interest of GILDEMEISTER Beteiligungen Aktiengesellschaft
7) Management and profit and loss transfer agreement with GILDEMEISTER Beteiligungen Aktiengesellschaft
8) Participating interest of DECKEL MAHO Geretsried GmbH
9) Management and profit and loss transfer agreement with DECKEL MAHO Geretsried GmbH
10) Participating interest of DECKEL MAHO Pfronten GmbH
11) Management and profit and loss transfer agreement with DECKEL MAHO Pfronten GmbH
12) Participating interest of DMG Vertriebs und Service GmbH DECKEL MAHO GILDEMEISTER
13) Management and profit and loss transfer agreement with DMG Vertriebs und Service GmbH DECKEL MAHO GILDEMEISTER
14) Participating interest of DMG Stuttgart Vertriebs und Service GmbH DECKEL MAHO GILDEMEISTER
15) Management and profit and loss transfer agreement with DMG Stuttgart Vertriebs und Service GmbH DECKEL MAHO GILDEMEISTER
16) Participating interest of DMG Europe Holding GmbH
17) Participating interest of DMG Asia Pacific Pte. Ltd.
18) Participating interest of DMG Benelux B.V.
19) Participating interest of DMG America Inc.
20) Participating interest of DMG Gebrauchtmaschinen GmbH DECKEL MAHO GILDEMEISTER
21) Percentage in voting shares 49.0%, Special Purpose Entity of GILDEMEISTER Aktiengesellschaft
22) Special purpose entity of DMG Frankfurt am Main Vertriebs und Service GmbH DECKEL MAHO GILDEMEISTER, Bad Homburg, excluding capital share
23) Special purpose entity of DMG Stuttgart Vertriebs und Service GmbH DECKEL MAHO GILDEMEISTER, Leonberg, excluding capital share
24) Participating interest of FAMOT Pleszew S.A., Pleszew, Poland
25) Participating interest of DMG Berlin Vertriebs und Service GmbH DECKEL MAHO GILDEMEISTER, Berlin

Corporate Directory

• Supervisory Board seats pursuant to Sect. 100 AktG
* Membership with comparable domestic and international control bodies of business enterprises

Supervisory Board

Hans Henning Offen,
Großhansdorf, born 1940, Chairman,
Independent Industry Consultant,
- • Lindner Hotels AG, Düsseldorf, member of the Supervisory Board since 30 August 2005
- * Schwarz Beteiligungs GmbH, Neckarsulm, member of the Advisory Board
- * Familienstiftung Schwarz, Neckarsulm, member of the Supervisory Board
- * Kaufland Stiftung & Co. KG, Neckarsulm, member of the Supervisory Board
- * Lidl Stiftung & Co. KG, Neckarsulm, member of the Endowment Board
- * Heckler & Koch GmbH, Neckarsulm, member of the Advisory Board since 16 July 2004, Chairman of the Advisory Council since 10 December 2004
- * Alpha-Stiftung, Dresden, Endowment Board since 26 April 2005
- * LD-Stiftung, Dresden, Endowment Board since 26 April 2005

Gerhard Dirr,
Vils, Austria, born 1964,
Deputy Chairman, Chairman of the Works Council at DECKEL MAHO Pfronten GmbH, Pfronten, until 31 January 2006,
Head of Facility Management at DECKEL MAHO Pfronten GmbH, Pfronten, since 1 February 2006

Wulf Bantelmann,
Bielefeld, born 1947,
Chairman of the Works Council at GILDEMEISTER Drehmaschinen GmbH, Bielefeld

Günther Berger,
Munich, born 1948,
Independent Industry Consultant,
- • Rathgeber AG, Munich, member of the Supervisory Board

Harry Domnik,
Bielefeld, born 1953,
1st Secretary of the IG Metall headquarters, Bielefeld,
- * ThyssenKrupp Umformtechnik GmbH, Ludwigsfelde, member of the Supervisory Board

Alfred Geißler,
Pfronten, born 1958,
head of Engineering/Development,
Senior Executives' representative,
member of the Supervisory Board until 1 June 2005

Dr.-Ing. Jürgen Harnisch,
Essen, born 1942,
Independent Industry Consultant,
- • ThyssenKrupp Automotive AG, Bochum, member of the Supervisory Board
- • ThyssenKrupp Technologies AG, Essen, member of the Supervisory Board
- • Fahrzeug-Werke LUEG AG, Bochum, member of the Supervisory Board
- * ThyssenKrupp Budd Company, Troy/Michigan, USA, member of the Boards of Directors
- * ThyssenKrupp Presta AG, Eschen, Liechtenstein, member of the Supervisory Board
- * Huf Hülsbeck & Fürst GmbH & Co. KG, Velbert, Chairman of the Supervisory Board
- * Presswerk Krefeld GmbH & Co. KG, Krefeld, member of the Supervisory Board

Ulrich Hocker,
Düsseldorf, born 1950,
Legal counsel, Chief manager
Deutsche Schutzvereinigung für Wertpapierbesitz e.V. (German association of securities owners) (DSW), Düsseldorf,
- • E.ON AG, Düsseldorf, member of the Supervisory Board
- • Feri Finance AG, Bad Homburg, member of the Supervisory Board
- • KarstadtQuelle AG, Essen, member of the Supervisory Board
- • ThyssenKrupp Steel AG, Duisburg, member of the Supervisory Board since 9 December 2005
- • ThyssenKrupp Stainless AG, Duisburg, member of the Supervisory Board since 25 November 2005
- * Phoenix Mecano AG, Kloten, Schweiz, President of the Administrative Board
- * Gartmore Capital Strategy Fonds, St. Helier, Jersey, member of the board until 23 February 2005
- * Gartmore SICAV, Luxemburg, member of the board since 10 May 2005

Prof. Dr.-Ing. Walter Kunerth,
Zeitlarn, born 1940,
Independent Industry Consultant,
- • Götz AG, Regensburg, Chairman of the Supervisory Board
- • Paragon AG, Delbrück, Chairman of the Supervisory Board
- * Autoliv Inc., Stockholm, Schweden, Member of the Board of Directors

Dr.-Ing. Manfred Lennings,
Essen, born 1934,
Independent Industry Consultant
- Deutsche Post AG, Bonn,
  member of the Supervisory Board
- ENRO AG, Essen,
  member of the Supervisory Board
- IVG Immobilien AG, Bonn,
  member of the Supervisory Board
  until 31 May 2005
* Bauunternehmung E. Heitkamp GmbH,
  Herne, member of the Supervisory Board
* Deilmann-Haniel GmbH, Dortmund,
  member of the Supervisory Board
* Heitkamp-Deilmann-Haniel GmbH, Herne,
  member of the Supervisory Board

member of the Supervisory Board
until 20 May 2005

Prof. Dr.-Ing. Uwe Loos,
Stuttgart, born 1946,
Independent Industry Consultant
- Dorma Holding GmbH + Co. KGaA,
  Ennepetal, member of the Supervisory Board
- EDAG Engineering + Design AG, Fulda,
  member of the Supervisory Board
* Trumpf GmbH + Co. KG, Ditzingen,
  member of the Supervisory Board,
  member of the Administrative Board
* Claas KGaA mbH, Harsewinkel,
  member of the shareholders' committee
* Bharat Forge LTD, Pune, Indien,
  Non Executive Independent Director
* SSB Antriebstechnik GmbH, Salzbergen,
  Chairman of the Advisory Council
* CDP Bharat Forge GmbH, Ennepetal,
  member of the Advisory Council

member of the Supervisory Board
since 20 May 2005

Peter Oxfart,
Creuzburg, born 1943,
Chairman of the Works Council at
DECKEL MAHO Seebach GmbH, Seebach,
until 31 January 2005

member of the Supervisory Board
until 31 January 2005

Günther-Johann Schachner,
Peiting, born 1952,
member of the Executive Board at
IG Metall Frankfurt,
1st Secretary of IG Metall headquarters,
Weilheim

Rainer Stritzke,
Seebach, born 1957,
design engineer,
member of the Works council at
DECKEL MAHO Seebach GmbH, Seebach,

member of the Supervisory Board
since 1 February 2005

Norbert Zweng,
Eisenberg, born 1957,
head of Logistics at DECKEL MAHO
Pfronten GmbH, Pfronten,
Senior Executives' representative,

member of the Supervisory Board
since 2 June 2006

The Executive Board

Dipl.-Kfm. Dr. Rüdiger Kapitza,
Bielefeld,
Chairman

Prof. Dr.-Ing. Raimund Klinkner,
Bielefeld,
Deputy Chairman

Dipl.-Kfm. Michael Welt,
Pfronten
- Staufen Akademie
  Beratung und Beteiligung AG,
  Bad Boll, Deputy Chairman of the
  Supervisory Board until 29 April 2005

Bielefeld, 28 March 2006
GILDEMEISTER Aktiengesellschaft

The Executive Board

Dr. Rüdiger Kapitza | Prof. Dr.-Ing. Raimund Klinkner | Dipl.-Kfm. Michael Welt

Audit Report

We have audited the consolidated financial statements prepared by the GILDEMEISTER Aktiengesellschaft, Bielefeld, comprising the balance sheet, the income statement, statement of changes in equity, cash flow statement and the notes to the consolidated financial statements, together with the group management report for the business year from January 1, 2005 to December 31, 2005. It should be understood that auditing the content of the "Entsprechenserklärung", in particular section 161 German Stock Corporation Law (AktG) in the group management report, is not object of our audit. The preparation of the consolidated financial statements and the group management report in accordance with IFRSs, as adopted by the EU, and the additional requirements of German commercial law pursuant to section 315a paragraph 1 HGB are the responsibility of the parent company`s management. Our responsibility is to express an opinion on the consolidated financial statements and on the group management report based on our audit.

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

Our audit has not led to any reservations.

In our opinion, based on the findings of our audit, the Consolidated Financial Statements comply with IFRS, as adopted by the EU, the additional requirements of German commercial law pursuant to section 315a paragraph 1 HGB and give a true and fair view of the net assets, financial position and results of operations of the Group in accordance with these requirements. The group management report is consistent with the consolidated financial statements and as a whole provides a suitable view of the Group's position and suitably presents the opportunities and risks of future development.

Berlin and Frankfurt am Main, 28 March 2006

KPMG Deutsche Treuhand-Gesellschaft
Aktiengesellschaft
Wirtschaftsprüfungsgesellschaft

Rehnen	Droste
Auditor	Auditor

Multiple Year Overview / Group Overview

GILDEMEISTER group		HGB 1999	HGB 2000	IFRS 2001	IFRS 2002	IFRS 2003	IFRS 2004	IFRS 2005	Change against prev. year in %
Sales revenues	€ K	**690,363**	**923,298**	**1,145,390**	**1,032,814**	**977,763**	**1,051,500**	**1,125,897**	**7**
Domestic	€ K	408,987	483,363	567,900	491,719	475,688	502,892	501,946	0
International	€ K	281,376	439,935	577,490	541,095	502,075	548,608	623,953	14
% International		41%	48%	50%	52%	51%	52%	55%	6
Total work done	€ K	**700,012**	**912,884**	**1,198,623**	**1,046,599**	**995,709**	**1,053,143**	**1,146,233**	**9**
Personnel costs	€ K	171,405	212,544	274,152	270,156	270,577	282,524	295,926	5
Depreciation	€ K	14,946	25,492	34,952	37,757	36,430	29,339	31,369	7
Financial result	€ K	-11,903	-18,681	-23,387	-24,672	-24,414	-29,833	-31,069	4
Profit/loss on ordinary activities	€ K	**34,452**	**44,192**	**54,737**	**-7,496**	**10,261**	**12,021**	**25,365**	**111**
Annual profit/loss	€ K	**32,663**	**38,079**	**25,785**	**-18,710**	**-3,579**	**5,577**	**13,530**	**143**
Adjusted results									
EBITDA	€ K	**61,302**	**88,365**	**113,076**	**54,933**	**71,105**	**71,193**	**87,803**	**23**
EBIT	€ K	**46,356**	**62,873**	**78,124**	**17,176**	**34,675**	**41,854**	**56,434**	**35**
EBT	€ K	**34,452**	**44,192**	**54,737**	**-7,496**	**10,261**	**12,021**	**25,365**	**111**
Result before shares to other shareholders	€ K	**33,586**	**39,667**	**24,672**	**-19,057**	**-3,732**	**5,534**	**13,719**	**148**
Fixed assets	€ K	**98,234**	**210,486**	**247,634**	**276,281**	**270,569**	**262,500**	**262,353**	**0**
Intangible assets	€ K	18,676	80,179	85,099	101,356	99,795	98,912	100,928	
Tangible assets	€ K	79,452	130,300	162,225	170,550	174,482	163,348	161,191	
Financial assets	€ K	106	7	310	443	224	239	234	
Current assets	€ K	**320,830**	**490,050**	**629,792**	**622,082**	**604,343**	**708,148**	**699,063**	**-1**
Inventories	€ K	124,973	160,420	249,771	250,768	264,365	276,565	288,777	
Receivables incl. deferred tax assets + prepaid expenses	€ K	182,270	305,534	364,743	353,625	328,553	371,285	388,366	
Liquid funds	€ K	13,587	24,096	15,278	17,689	11,425	60,297	21,920	
Equity [1]	€ K	**107,174**	**195,687**	**231,177**	**193,824**	**187,593**	**250,540**	**265,782**	**6**
Subscribed capital	€ K	56,398	75,087	75,087	75,087	75,087	112,587	112,587	
Capital provisions	€ K	12,568	48,734	48,734	48,734	48,734	68,319	68,319	
Revenue provisions	€ K	19,793	39,068	83,055	70,003	63,772	68,597	85,014	
Accumulated profit/loss	€ K	13,202	18,455	24,301	0	0	0	0	
Shares to other shareholders	€ K	**5,213**	**14,343**	**10,773**	**1,193**	**1,198**	**1,037**	**-138**	**-113**
Outside capital	€ K	**311,890**	**504,849**	**635,476**	**703,346**	**686,121**	**720,108**	**695,634**	**-3**
Participating certificate capital	€ K	0	0	0	0	0	0	0	
Special account for investment allowances	€ K	1,632	1,219	0	0	0	0	0	
Provisions	€ K	81,472	113,928	139,302	148,386	133,958	123,456	125,407	
Payables incl. deferred tax liabilities + deferred income	€ K	228,786	389,702	496,174	554,960	552,163	596,652	570,227	
Balance sheet total	€ K	**419,064**	**700,536**	**877,426**	**898,363**	**874,912**	**970,647**	**961,416**	**-1**
Employees (annual average)		3,142	3,936	4,918	4,912	4,849	4,932	5,090	3
Employees (31 Dec.)		3,175	4,447	5,030	4,821	4,823	4,984	5,083	2
Trainees		165	190	204	224	205	190	189	-1
Total employees		**3,340**	**4,637**	**5,234**	**5,045**	**5,028**	**5,174**	**5,272**	**2**

GILDEMEISTER group		HGB 1999	HGB 2000	IFRS 2001	IFRS 2002	IFRS 2003	IFRS 2004	IFRS 2005	Change against prev. year in %
Efficiency ratios									
Profit on sales (EBIT) = EBIT / Sales revenues	%	6.7	6.8	6.8	1.7	3.5	4.0	5.0	26
Profit on sales (EBT) = EBT / Sales revenues	%	5.0	4.8	4.8	-0.7	1.0	1.1	2.3	97
equity return [1] = Annual profit/loss /equity (as of 01 Jan) [3]	%	40.0	35.5	11.4	-8.1	-1.8	3.0	5.4	82
Return on total assets = EBT + interest on outside capital / average total capital	%	12.1	11.5	9.7	2.2	4.1	4.8	6.1	27
ROI – Return on Investment = EBT / average total capital	%	8.9	7.9	6.6	-0.8	1.2	1.3	2.6	102
Sales per employee = sales revenue / average number of employees (exc. trainees)	€ K	219.7	234.6	232.9	210.3	201.4	213.2	221.2	4
EBIT per employee = EBIT / Capital Employed	€ K	14.8	16.0	15.9	3.5	7.2	8.5	11.1	31
ROCE – Return on capital employed[1] = EBIT / Capital Employed	%	14.8	12.0	12.0	2.6	5.2	6.1	8.1	33
Value added	€ M	218.1	275.7	352.6	287.5	305.4	324.5	352.5	9
Value added per employee	€ K	69.4	70.0	71.7	58.5	63.0	65.8	69.3	5
Balance sheet ratios									
Capitalisation ratio of fixed assets = fixed assets / total assets	%	23.4	30.1	28.2	30.8	30.9	27.0	27.3	1
Working intensity of current assets = current assets / total assets	%	75.9	69.3	68.6	65.1	65.2	69.9	69.3	-1
Equity ratio = equity / total capital	%	25.6	27.9	26.3	21.6	21.4	25.8	27.6	7
Ratio of outside capital to total capital = outside capital / total capital	%	74.4	72.1	73.7	78.4	78.6	74.2	72.4	-2
Assets and liabilites structure = fixed assets / current assets	%	30.9	43.4	41.2	47.2	47.5	38.7	39.4	2
Capital structure = equity / outside capital	%	34.4	38.8	35.8	27.5	27.3	34.8	38.2	10

to be continued >>

GILDEMEISTER group		HGB 1999	HGB 2000	IFRS 2001	IFRS 2002	IFRS 2003	IFRS 2004	IFRS 2005	Change against prev. year in %
Ratios pertaining for financial position									
Cash ratio = liquid funds (from balance sheet) short-term liabilities (up to 1 year)	%	5.8	7.0	3.5	3.6	2.2	19.0	5.6	-71
Ratio of financial current assets to short-term liabilities = (liquid funds + short-term receivables) / short-term liabilities (up to 1 year)	%	81.2	91.5	80.7	67.1	59.1	117.1	96.5	-18
Current ratio = (liquid funds + short-term receivables + inventories) + short-term liabilities (up to 1 year)	%	134.3	137.9	130.2	111.4	106.1	195.6	161.3	-18
Net indebtness = amounts owed to banks + bills payable liquid funds - current investments	€ M	124.4	214.9	278.0	319.5	342.1	314.0	305.1	-3
Gearing[1)] = net indebtness / equity before shares held by other shareholders	%	116.1	109.8	120.3	164.8	182.4	125.9	114.7	-9
Working Capital = current assets - short-term borrowed capital	€ M	136.5	226.4	283.2	176.0	136.7	340.5	305.0	-10
Net Working Capital = inventories + payments on account - customer prepayments + trade debtors trade creditors	€ M	217.9	318.9	402.1	386.5	377.7	390.2	399.5	2
Capital Employed = equity + provisions + net indebtness	€ M	313.0	524.5	648.5	661.7	663.7	688.0	696.3	1
Structural analysis ratios									
Turnover rate of raw materials and consumables = cost for raw materials and consumables / inventories of raw materials and consumables		6.3	5.9	6.9	6.8	5.8	5.0	5.5	10
Turnover rate of stocks = sales revenues / inventories		5.5	5.8	4.6	4.1	3.7	3.8	3.9	3
Turnover rate of receivables = sales revenues (incl. 16% VAT on domestic revenues) average trade debtors		5.2	4.7	4.4	3.7	3.8	4.2	4.2	1
Total capital-sales ratio = sales revenues / total capital		1.6	1.3	1.3	1.1	1.1	1.1	1.2	8
DSO (Days sales outstanding) = average trade debtors / (sales revenues (incl. 16% VAT on domestic revenues)) x 365		70.0	77.7	83.6	97.6	96.1	87.3	86.2	-1

GILDEMEISTER group		HGB 1999	HGB 2000	IFRS 2001	IFRS 2002	IFRS 2003	IFRS 2004	IFRS 2005	Change against prev. year in %
Productivity ratios									
Intensity of materials = cost of materials / gross performance	%	55.0	53.1	54.0	54.5	52.8	52.6	53.1	1
Intensity of staff = staff costs / gross performance	%	24.5	23.3	22.9	25.8	27.2	26.8	25.8	-4
Cash flow & investments									
Cash flow from current operations	€ M	23.9	-5.0	31.5	47.7	28.7	12.8	27.2	112
Cash flow from investment activity	€ M	-38.7	-144.7	-70.7	-71.9	-32.3	-20.1	-24.4	21
Cash flow from financing activity	€ M	20.1	161.0	31.3	27.6	-1.8	57.0	-41.7	-173
Free cash flow = cash flow from current operations + cash flow from investment activity (exc. cash flow from financial investments)	€ M	-8.2	-39.4	-29.7	-0.8	-3.7	-6.4	3.2	150
CapEx (Capital Expenditure)	€ M	37.6	39.5	80.2	73.2	36.4	21.8	26.8	23
Share & Valuation									
Market capitalisation	€ M	147.6	235.3	269.2	109.2	237.4	225.2	253.8	13
Company value = Market capitalisation + amounts owed to banks + bills of exchange + other liabilities + pension provisions - liquid funds	€ M	319.3	506.8	619.9	496.1	643.8	609.8	636.0	4
Earnings per share[2)] = result after minority interests / number of shares	€	0.76	0.91	0.85	-0.66	-0.13	0.15	0.32	148
Price earnings ratio (PER) = market capitalisation / EBT		4.3	5.3	4.9	-14.6	23.1	18.7	10.0	-47
Company value-EBITDA-ratio = company value / EBITDA		5.2	5.7	5.5	9.0	9.1	8.6	7.2	-15
Company value-EBIT-ratio = company value / EBIT		6.9	8.1	7.9	28.9	18.6	14.6	11.3	-23
Company value-sales ratio = company value / sales		0.5	0.5	0.5	0.5	0.7	0.6	0.6	-3

[1)] Under HGB incl minority interests; under IFRS excl. minority interests, from 2004 onwards incl. minority interests.
[2)] Under HGB in acc. with DVFA/SG; the share capital was split 1:10 in 1999; the figures for the previous years were adjusted accordingly.
[3)] Without consideration of the capital increased accomplished at 16 June 2005.

Commercial Glossary

Fixed Assets
Assets intended for use on a continuing basis for the purpose of an undertaking's activities

Acquisition
The acquisition of companies or operations either through the transfer of shares or the transfer of all or certain assets and liabilities of a company or through a combination of both. The legal independence of the partners may be preserved.

Basel II
Revised capital framework of the Basel Committee for Banking Supervision, consisting of representatives of the central banks and bank supervisory authorities. The objective of Basel II is a) an improved assessment of credit risks, and b) to arrange the banks' capital requirements in line with the credit risks of the borrower. This means, the higher the loan loss risk of the borrower, the higher must be the bank's equity capital. This change directly affects the lending policy of the banks.

Capital increase through a rights issue
Capital increase, where shareholders are entitled to buy new shares in accordance with their share in the previous share capital.

Cash flow
Flow of financial funds from current business activities over a period, adjusted by significant charges and income not affecting payment.

Corporate Governance
The responsible management and control of companies geared towards the creation of long-term value

DAX
Stock index calculated at the Frankfurt stock exchange. The DAX is calculated from the prices of the 30 leading German shares.

EBITDA
Earnings before interest, taxes, depreciation and amortisation

EBIT
Earnings before interest and taxes
(Earnings before interest and taxes).

EBT
Earnings before taxes

Equity
Funds made available to a company by its owners through deposit and/or contribution or from retained earnings

Equity return
Annual profit to equity ratio

EMO
"Exposition mondiale de la Machine Outil". The EMO is seen as the main trade fair in metal working and is the largest trade fair for machine tools worldwide. It takes place in two successive years in Hanover, and in the third year in Milan.

Eurostoxx 50
This index consists of the 50 major shares
(the so-called Blue Chips) from the EU countries.

Free cash flow
Free funds that are available to the company, arising from the cash flow balance from current operations and the investment activity. Investments in the financial assets are not taken into account in this respect.

Free float
Part of the share capital in portfolio investments

Outside capital
Summarising term for provisions, creditors and deferred income shown on the liabilities side of a balance sheet

FTSE-100
Abbreviation for the Financial Times Stock Exchange 100 stock index. It includes the 100 major quoted securities in Great Britain.

Gearing
Net indebtedness to equity ratio

Return on total investment
Profit before taxes and interest on outside capital to average total capital ratio

Goodwill
Percentage of the purchase price of a company which exceeds the value of the assets calculated as fractional values

IFRS/IAS
International Financial Reporting Standards. Internationally applicable accounting standards to ensure international comparability of group accounts and to meet information requirements of investors and other readers of annual accounts by providing a higher degree of transparancy. The individual sections of the IFRS are called IAS (International Accounting Standards).

Flow of funds analysis
Statement of the movement of liquid funds/flow of funds taking into account the sources and application of funds during the financial year

Syndicated loan (facility)
A loan granted by several banks (syndicate), where the total risk (e.g. from credit standing, capital tie-up) is distributed among the banks and the credit limit applicable to each bank is not exceeded.

Deferred tax
Inter-period differences between calculated taxes on profit or loss from a commcerial and tax balance sheet, with the object of showing tax expenditure in accordance with the correct commercial reuslt

Local content
Percentage of goods purchased in the country of the production plant (in contrast to imported components) in the value of a product.

Market capitalisation
This is the current price of a listed company. It is determined by the share's market value multiplied by the total number of shares.

Merger
Joining of two or more companies that, up to then, used to be legally and economically independent organisations, where at least one of the companies will lose its independent legal status.

MDAX
Index for medium-sized companies from traditional industries; as index for selected securities ranking directly below the DAX. It includes 50 securities listed in the "Prime Standard" segment.

NIKKEI Index
Major Japanese stock market index.

Prepaid expenses and deferred income
Payments in the reporting period that affect the profit or loss of a period after the balance sheet date

ROCE
Return on capital emloyed: EBIT to equity, provisions and net indebtedness

ROI
Return on investment: earnings before taxes to average total capital ratio

SDAX
Index for 50 smaller companies, so-called small caps following the securities included in the MDAX stock market index in terms of orderbook business and market capitalisation.

Hedging transaction
Hedging against interest rate and/or currency risks from one or more underlying transactions; the hedging can be performed through the use of derivative financial instruments.

S&P 500 Index
A major US-American stock market index, comprising of 400 industrial shares, 40 utilities, 20 securities of transport corporations and 40 securities of financial institutions.

Current assets
Assets for the short-term operation of the business

Corporate bond
Bond issued by a company with a fixed term and usually fixed interest payments, usually with the aim of raising long-term large-volume capital (debt finance) in the national and international capital markets.

Working capital
Working capital is determined by current assets minus short-term liabilities.

Technical Glossary

Advanced Materials
Materials with special characteristics, such as abrasion resistance, resistance to heat or chemicals, etc., which makes them suitable for the use in wide variety of applications. However, the economic machining of these materials usually requires the use of special technologies, e.g. ultrasonic or laser technology. Advanced materials include technical ceramics (zirconium oxide, silicon carbide, aluminium oxide), glass (quartz glass, Zerodur, Macor), composites (carbon or mineral fibre), metal carbide, hardened steel (hardness > 53/54 HRC) or precious stones such as ruby or sapphire.

Benchmark
External or in-house comparison of companies or departments with the help of selected key figures.

Cavity
A cavity is a small hollow mould.

CDK Set
At sites where complex procurement processes are (as yet) not possible or profitable, so-called completely knocked down sets are used for the assembly of multistage products. CKD sets include all component parts and sub-assemblies of a product and only require assembly processes for the construction of the end product.

coSupply®
coSupply® represents the comprehensive partnerhip approach for powerful supply partnerships at GILDEMEISTER, characterised by the three functions: “communication”, “cooperation” and “competence” and striving for enhanced competitiveness.

CTV
The CTV product line includes universally arranged lathes with a vertically placed head spindle and highly dynamic linear drive technology, providing integrated handling of components and the option for automated integrated machining in serial production.

CTX
The two CTX product lines provide a differentiated programme of CNC universal lathes with a variety of innovative options for numerous machining tasks.

DMC U
The DMC U product line provides universal CNC machining centres equipped with a pallet switching system for 5-sided / 5-axis machining in fully automated serial production of complex parts.

DMC H
The DMC H product line provides horizontal machining centres with high dynamics and precision for a wide range of uses, from fast serial production to heavy cutting with highest precision.

DMC V
The DMC V product line provides vertical machining centres with high dynamics and precision for high demands in both the tools manufacture and mould making industries and for small-lot and medium-sized serial production.

DMF
The DMF product line provides traversing column machines with large machining areas, effective pendulum machining in two separate work areas, high cutting performance, dynamics and precision with fast traverse speeds of the traversing column.

DMG Netservice
Interactive online remote access to the control of machines for customer and user support in programming and fault analysing.

DMP
The DMP product line includes vertical machining centres for production milling with especially high dynamics and short non-productive times through linear direct drives and a new type of tool change design.

DMU
This products line with its well developed programme of CNC universal milling machines for 5-sided machining offers a good starting point into modern milling.

DMU eVolution/DMU P
This product line includes CNC universal milling machines for integrated 5-sided / 5-axis machining in one setting. The machines combine precision with high productivity and offer a wide range of installation sizes and innovative options including combined milling and turning machining.

duoBLOCK®
The patented duoBLOCK® construction combines the advantages of a traversing column structure with those of a portal construction and thanks to its thermo-symmetrical design ensures maximum precision, rigidity and dynamics.

E-Commerce
This terms represents the whole range of electronic Internet-supported communication between the company, suppliers and customers. Its essential element is the paperless exchange of business information. Applications range from relaying information through to sales to world-wide simultaneous auctions between partners via the Internet.

Entry-machines
In turning and milling, the entry machines market segment is served primarily by high precision robust machine tools for small and medium batch production. Entry machines stand out because of their economic efficiency, flexibility and low purchase price.

ERP-System BaaN
Standard application software for Enterprise Resource Planning (for example SAP/R3, BaaN); It is intended to be used in, and adapted to, a variety of organisational conditions and business processes in various industries and companies. It continuously supports processes, for example in materials and merchandise management or finances.

GMC/GM
The GMC/GM product line includes CNC multi-spindle turning centres and multi-spindle automatic lathes. GMC machines offer state-of-the-art control technology with 3D programming and integrated spindle engines than can, on request, be equipped with linear drives on the X-axes to achieve the highest dynamics and precision.

GMX
The turning and milling centres of the GMX product line integrate state-of-the-art milling and turning technology into high-precision 6-sided integrated machining of complex workpieces.

Laser technology

Laser technology or laser beam machining is an eroding process for machining metallic materials and materials that are not easily machinable, such as high-tech ceramics, silicon or metal carbide using a spot-beam with a high energy level. With this process it is possible to create filigree contours and the finest cavities, and to perform laser fine cutting or drilling tasks in the 2-D and 3-D areas.

Lasertec

The machines from the LASERTEC product line offer high-quality, fast and economic options for high-precision machining of filigree workpieces and finest cavities, including those made from materials that are difficult to machine. The modular design of this line allows for a wide variety of applications for 3D laser erosion, laser fine cutting and laser drilling and for the combined production with high-speed milling machining.

Linear drive technology

Linear drive technology uses a contactless, electromagnetic driving principle that does not rotate as in traditional methods, but has a linear moving direction. Mechanical intermediate elements are therefore no longer necessary so that the engine itself moves the machine axes with high precision and acceleration with hardly any wear.

monoBLOCK®

Unlike a traditional construction, where the machine frame consists of several components (bed, stand, etc.). The core of a machine in monoblock construction is formed by a rigid and compact basic body

NEF

The NEF product line offers an operator-friendly entry-level CNC universal lathe for modern turning technology at an affordable price. Thanks to their universal design, the machines are suitable for piece part manufacture and small-lot production.

Negative angles

A large swivel range between the tool and the workpiece allows for easier machining of complex workpiece geometries. Those parts of the tool axis swivel range to the workpiece that exceed 180° are described as the negative angle. Among other things, this allows undercuts without having to reset.

PQA

The GILDEMEISTER system of Preventative Quality Assurance, which enables intensive cooperation across all departments for the early identification of faults in our products (before start of production).

PULL

PULL stands for Produktions- und Logistik-Leistung (performance of production and logistics) and has represented the GILDEMEISTER production system since June 1998. In line with examples from the motor industry (Toyota production system, TPS) it combines different components and individual measures with the aim of increasing efficiency in production and in the production-related areas, such as materials planning, receipt of goods and stock of goods, in one continual improvement process.

PULLplus

The GILDEMEISTER value-added system PULLplus is the improvement of the production system PULL. It combines the idea of waste minimisation with a value-added based approach to all areas of the company. The adaptation to best-practice methods is carried out in a continuous improvement process.

SKD

SKD sets represent an intermediate step in the conversion of assembly processes, previously completed with the aid of CKD sets, to regular, complex procurement processes. Semi knocked down sets include major components and subassemblies, which only require assembly processes and, to a limited extent, local procurement processes to complete the end product.

Spheroidal graphite iron
(modular gray cast iron) cast iron alloy with spheroidal graphite. The higher quality spheroidal graphite iron has steel-like mechanical features, which means that a higher complexity of parts, less wall thickness and, as a result, less weight than with traditional grey cast iron is possible.

SPRINT
This product line provides single-spindle machines for CNC automatic turning for the flexible economic integrated machining of short lathe work of up to 65mm in diameter.

SPEED
The SPEED line offers CNC Swisstype automatic lathes equipped with linear drive technology for highly productive machining of long lathe work with highest precision, as used in medical technology or the clock-and-watch-making industry.

Torque-Motor
The torque motor is, due to its compact construction, stronger than traditional electric motors. It operates similarly to a rolled-up linear drive. The torque motor does not require any additional mechanical transmission components (such as gears) and therefore stands out due to its high control quality.

TWIN
The TWIN product line provides two-spindle turning centres with independent turning spindles for demanding integrated machining of chuck, shaft and rod parts.

Ultrasonic
The Ultrasonic product line consists of machines for ultrasound-supported, economic machining of ‘advanced materials’, such as ceramics, glass, silicon, composites, metal carbide, hardened steel, sapphire or mother-of-pearl. The ultrasonically energised main spindles interfere with the traditional machining process (for example milling) through a high-frequency oscillating motion. Compared with traditional machining processes, this machine design results in a productivity that is up to five times higher, longer tool lifes and at the same time better surface quality, and, with regard to the processed workpiece geometries, a substantially higher flexibility.

Workflow
Work flows are organisation-wide processes based on a division of labour, where the required tasks are coordinated by either people or software systems.

30 March 2006	Press conference on Financial Statements
30 March 2006	Publication of Annual Report 2005
31 March 2006	DVFA-Analysts' conference
09 May 2006	First Quarterly Report 2006 (1 January to 31 March)
19 May 2006	General meeting of shareholders at 10am in the Town Hall Bielefeld
22 May 2006	Distribution of dividend
04 August 2006	Second Quarterly Report 2006 (1 April to 30 June)
07 November 2006	Third Quarterly Report 2006 (1 July to 30 September)
14 February 2007	Press release on provisional figures for the financial year 2006
25 May 2007	General meeting of shareholders at 10am in the Town Hall Bielefeld

Subject to alteration

Forward-looking statements

The information in this press release includes forward-looking statements that are based on current estimates of the management on future developments. These statements are subject to risks and uncertainties relating to factors that are beyond GILDEMEISTER's ability to control or estimate precisely, such as future market and economic conditions, the behaviour of other market participants, the successful integration of acquisitions, the realisation of expected synergy effects and the actions of governmental regulators. Should one of these factors of uncertainty or other unforeseeable events occur or should the assumptions on which these statements are based prove incorrect, the actual results might differ materially from the results expressed in, or implied by, these statements. GILDEMEISTER disclaims any intention or special obligation to update any forward-looking statement to reflect any change in events or developments occured after the date of this press release. Forward-looking statements should not be construed as guarantor or assurance of future developments or events included therein.

This Report is available in German and in English; both versions can be downloaded from the Internet at www.gildemeister.com or viewed in its interactive online version. Further copies of this Report and additional information on GILDEMEISTER can be obtained free of charge on request.

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MONTFORT WERBUNG

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