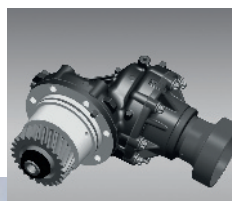


3.2 Drive Systems Segment



Mercedes-Benz



Intensive cooperation makes all-wheel drive possible

As a car manufacturer, Mercedes-Benz is characterized by performance, safety and comfort. The very first 4MATIC all-wheel drive system for the luxury car manufacturer's compact vehicles also embodies these characteristics. It is twice as efficient and half the weight of similar systems. Oerlikon Graziano developed the central power take-off unit (PTU) of the new gear system in close cooperation with Mercedes-Benz. In the high performance A-Class AMG model, the PTU transfers up to 360 hp from the transversely mounted front engine to the rear drive shaft. In the space of less than three years, Oerlikon Graziano went from first designs to series production with this innovative project. Oerlikon Graziano's engineering and high production standards will ensure that around 100 000 compact-vehicle drivers each year have the privilege of experiencing the Mercedes-Benz all-wheel drive.

1. Challenging business environment in key end markets.
2. Increase in order intake, but sales and profitability impacted by weak markets.
3. Construction of third plant in India started, to capture future growth potential in Asia.

Key figures

| in CHF million | 2013 | 2012 | Δ % |
|----------------|-------|-------|---------|
| Order intake | 792 | 766 | 3.4 % |
| Order backlog | 180 | 134 | 34.3 % |
| Sales | 734 | 826 | -11.1 % |
| EBIT | 26 | 70 | -62.9 % |
| EBIT margin | 3.5 % | 8.5 % | - |

Best-in-Class

BorgWarner: 11.5 % operating margin (2013)



Business performance

Global key markets slowed down significantly during the year 2013, providing meaningful challenges for the Drive Systems Segment and its customers. Although the demand for agricultural equipment, the Segment's largest end market, conveyed a resilient performance, significant declines in the heavy construction industry, for heavy-duty off-highway equipment, in infrastructure projects and in rail transportation markets in North America and China became perceivable. Equipment demand also slowed significantly in the global mining and US natural gas sectors, the Segment's most profitable markets. However, long-term global prospects in these markets remain favorable, and the Segment made inroads into the offshore oil drilling market in the US.

Project orders from the energy market caused order intake to rise by 3.4% to CHF 792 million from CHF 766 million a year ago. Due to the challenging market environment, sales declined by 11.1% to CHF 734 million compared to CHF 826 million in 2012. Order backlog increased to CHF 180 million, up 34.3% from CHF 134 million in 2012. EBIT amounted to CHF 26 million, down 62.9% year on year due to lower overall sales volume and disproportionately lower sales in the Segment's higher-margin products and services. The comprehensive mitigation actions and operational excellence initiatives, under way since the beginning of 2013, limited the negative effects, resulting in sequential improvements quarter for quarter

in 2013. The Drive Systems Segment reported an EBIT margin of 3.5% compared to 8.5% a year ago.

The resilience in the agriculture market and the weakness in other key markets of the Segment are also reflected in the geographical development. European sales slightly declined by 4% and represent 52% of total Segment sales. North America reported a sales decline of 24% and a proportion of 32% of total Segment sales. Asian sales decreased by 9%. The remaining 5% of sales are allocated to the rest of the world.

In 2013, the Drive Systems Segment signed close to CHF 1 billion in long-term agreements, including renewing and expanding two long-term agreements with key customers. A long-term contract worth up to CHF 600 million was renewed with a major global agriculture and off-highway equipment manufacturer. The contract comprises new product development programs, new applications and the development of new regions and will last until 2015. Secondly, a double-digit million euro long-term agreement with GIMA, a leader in the agriculture equipment market, was signed. The reinforced cooperation with GIMA expands the business between the two companies through 2016. Oerlikon Graziano provides GIMA with a wide range of high-quality engineered components.

Key topics

Optimizing the global manufacturing footprint

The Segment operates a global manufacturing footprint with facilities in the US, Europe and Asia. Utilization in the US facility was impacted by the weak market environment and required significant headcount adjustments and temporary plant shut-downs. The five sites in Italy, due to the resilience in the agriculture market and in the high-performance automotive applications, reported an adequate level of utilization. The Segment continued the expansion of its plant in Suzhou, China. The intention to take better advantage of business opportunities in the Chinese market was impacted by the weak market environment. In India, the two existing plants in Greater Noida and Belgaum reported high utilization levels. Export and domestic market sales provided encouraging growth, despite a slowdown in relative terms of the Indian economy. Consequently, the Segment started with the construction of a third plant in Sanand in the state of Gujarat, a hub for the Indian automotive industry.

Innovation

The Drive Systems Segment presented its innovative 4SED (4 Speed Electric Drive) to customers in Europe. This new compact, lightweight transmission boasts increased efficiency, seamlessly smooth shifting and a scalable design, making it suitable for a wide range of vehicle types. This innovative design will improve battery efficiency by around 15%.

Oerlikon and the international automotive supplier Continental entered into an agreement to jointly develop and market integrated motor and transmission systems for hybrid and electrical vehicles. The aim of this collaboration is to further improve the efficiency of electrified powertrains through integrated optimization of both the electric motor and the transmission. An integrated system-level optimization is expected to create significantly improved customer benefits.

Outlook

In 2014, the Drive Systems Segment expects a similar environment to 2013. Order intake and sales are expected to increase.