



## **Management Discussion and Analysis**

Schefenacker Aktiengesellschaft  
Esslingen

1<sup>st</sup> Quarter 2005

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## MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

You should read the following discussion with the more detailed information and the consolidated financial statements, including the notes thereto appearing elsewhere in this report and our previously published annual report which contains audited annual consolidated financial statements, risk factors and a description of our business. Our consolidated financial statements have been prepared in accordance with German generally accepted accounting principles ("GAAP").

The following management's discussion and analysis of financial condition and results of operations discusses the three months ended March 31, 2005 and 2004.

### Overview

#### *General*

We are a leading global manufacturer and supplier of rear vision systems, rear and interior lighting and premium automotive sound systems to automotive original equipment manufacturers, or OEMs. We supply our products to 14 of the 15 largest OEMs, including DaimlerChrysler, Ford, GM, Hyundai/Kia and Renault/Nissan, as well as other, smaller OEMs. In addition, we have long-standing relationships with many of our customers and continue to establish new relationships with other OEMs, such as Volkswagen. We have a reputation as a provider of innovative products to OEMs and continue to place a significant emphasis on product innovation and design. We supply products for a wide variety of vehicle models, and, with respect to many of these models, we are the only supplier used by the relevant OEMs to supply these products.

#### *Acquisitions and Disposals*

No major changes have occurred since December 31, 2004.

#### *Repositioning and Refinancing*

##### *Refinancing activities*

In 2002 and 2003 we experienced difficulties in meeting certain financial covenants under the credit facilities entered into to finance the Britax Acquisition and had to obtain waivers with respect to compliance with certain financial covenants, as well as deferrals of previously scheduled repayments. We therefore entered into negotiations to reorganize our financial structure, which resulted in February 2004 in the issuance of senior subordinated notes and new senior credit facilities. The net proceeds from the offering of the notes, issued in February 2004, together with borrowings of the new senior credit facilities, were used to repay most of our former indebtedness. In May 2005 we subsequently refinanced our borrowings under senior credit facilities through the entry into further new senior credit facilities. Fees and expenses related to these refinancing activities have affected our results over the periods discussed below.

##### *Operational restructuring*

In late 2003 we began the implementation of an operational repositioning plan consisting of a number of initiatives designed to improve our profitability and operational efficiency. While some of the operational repositioning initiatives have been successful, the overall effects on our profitability were below our planned results. Accordingly, our supervisory board decided a further operational restructuring program "Transition" in October 2004. Implementation of this program, started in January 2005 after thorough feasibility studies, includes the restructuring of all German production facilities as well as our locations in Selmer/USA, in Hungary (SAPU) and in Slovenia (SGA). It has five key areas:

- *Locations* – in addition to the transfers to lower cost countries that have occurred to date, the management has identified opportunities to further exploit low labor cost sites for production. In addition, we are seeking to simplify the supply chain network by a stronger focus of the different sites on specific products and technologies.
- *Purchase and logistics* – while continuing with our previous efforts, we are expanding our cost reduction efforts to new areas.
- *New product introduction* – We are seeking to improve our product introduction process, which not only shortens time to market but also has an impact on indirect cost. As an example, modification cost during the launch but also quality cost over the whole lifecycle can significantly be reduced by an optimal new product introduction process.

- *Organization* – through commonization, reasonable centralization and other organizational initiatives we are seeking to reduce overhead cost and administrative efforts.
- *Transparency* – we are implementing additional controlling and reporting processes and tools to gain optimal transparency on our performance in the various areas of our business performance.

### ***Effects of foreign currency denominated transactions***

Our results of operations are subject to the impact of changes in currency exchange rates on receivables and liabilities recorded by us with respect to transactions with third parties involving more than one currency. These typically arise when one of our operations enters into a transaction such as a purchase or sale transaction or a loan in a currency other than its reporting currency. If, for example, one of our subsidiaries whose reporting currency is euro borrows US dollars from a third party, the amount of US dollars borrowed would initially be recorded as a euro liability in the accounts of such subsidiary. The recorded amount of this euro liability would be determined, in accordance with German GAAP, by converting the actual US dollar liability into euro on the date of the initial borrowing. When the loan is eventually repaid, the difference between the amount of the initially recorded liability and the amount of euros required to repay the loan is reflected, as appropriate, as a gain or loss in the subsidiary's income statement.

Unrealized gains or losses may arise at the end of a given financial period when foreign currency denominated receivables and liabilities with respect to uncompleted transactions are revalued using the exchange rate at the balance sheet date. Realized gains or losses arise when a transaction is completed and the gain or loss in question is deemed to be "realized". German GAAP does not allow unrealized gains to be recorded with respect to foreign currency denominated receivables or liabilities but does, however, require unrealized losses to be recorded.

### **Explanation of Key Income Statement Items**

#### ***Sales***

Over 90% of our total sales are generated from our three primary product lines: rear vision systems, rear and interior lighting and premium automotive sound systems. We also generate a small amount of sales from the sale of tooling for automotive parts to OEM customers and other items. Our sales are driven by demand for the automobiles produced by our OEM customers. This in turn is driven by economic conditions generally and in the automotive industry specifically as well as technological and regulatory developments. The pricing of our products, as well as the translation effects caused by fluctuations in currency exchange rates, also affects the amount of our total sales.

We typically enter into master agreements with our other OEM customers for the supply of our products. These agreements usually contain non-binding indications of production volumes. However, actual production volumes may be significantly lower than these estimates due to a reduction in consumer demand, new delays or shorter product cycles, often without any compensation to customers. For programs currently under production, we are typically not entitled to price adjustments, or other compensation, when volumes differ from production estimates used during the quotation. However, when volumes differ significantly from the quotation, we can request price adjustments for the current project, as well as others, or attempt to leverage these shortfalls to win new contracts.

#### ***Cost of sales***

Our cost of sales consists of:

- direct materials costs,
- manufacturing costs, and
- direct labor and other personnel costs.

Direct materials costs represented approximately 61% of our total cost of sales in the three months ended March, 31, 2005 compared to 65% in the same period of 2004. Direct materials include all raw materials, parts and components that we use in the production of our products. Our principal direct materials are glass, audio components, plastic resins, actuators, plastic parts, electronics, paint and aluminum. Our contracts for the purchase of our direct materials typically contain provisions that set prices for up to one year,

although the prices of plastic resins and aluminum vary to some extent given that they are commodities.

Manufacturing costs represented approximately 28% of our total cost of sales in the three months ended March, 31, 2005 compared to 24% for the same period of 2004. Manufacturing costs principally include lease costs on certain property, depreciation on owned production assets, utility expenses, and repairs and maintenance. Depreciation of non-production assets is included in selling costs, general administrative costs and research and development costs, depending on the type and use of the asset.

Direct labor and other personnel costs represented approximately 11% of our total cost of sales in three months ended March, 31, 2005 and have been unchanged compared to the three months period ended March 31, 2004. Labor costs principally include the cost of salaried employees and hourly employees as well as benefits and pension expenses (to the extent attributable to labor costs included in cost of sales).

#### ***Selling costs***

Selling costs principally include sales organization expenses and distribution expenses, such as packaging materials, freight and sales commission expenses. This item also includes benefits and pension expenses to the extent attributable to our sales force. In accordance with German GAAP, selling costs also include charges for bad debts from customers.

#### ***Research and development costs***

Research and developments costs include all costs of inventing and developing products, with the exception of a portion that is capitalized in the cost of the product. To bring some of our more complex products to commercial production often requires several years of investment, either alone or jointly with our OEM customers. The extent to which we are able to recoup these expenses varies from customer to customer. See "Critical Accounting Policies" below.

#### ***General administrative costs***

General administrative costs principally include wage and salary expenses and administrative operating expenses such as audit and legal fees, tax consultant fees and insurance premiums. In the first three months of 2004 general administrative costs includes fees and expenses in connection with our 2004 refinancing activities. For our new refinancing transaction, which took place in May 2005, we expect additional fees and transaction costs of approximately €4-5 million in the second quarter of 2005.

#### ***Other operating income and expenses***

Other operating income and expenses principally includes scheduled amortization of goodwill, additions and reversals of accruals, gains and losses from the sale of assets, imbalances in assets and liabilities with respect to intercompany transactions, realized and unrealized effects of foreign currency denominated transactions, export subsidies, income from rent and insurance proceeds.

### **Critical Accounting Policies**

Our accounting and valuation policies are described in the notes to our consolidated financial statements. We believe the following represent our critical accounting policies:

#### ***Impairment of goodwill***

In addition to regularly scheduled amortization of goodwill, we test our goodwill annually and at the end of each quarter, if new information has become available, to determine whether there is any impairment to the value recorded in our financial statements. We utilize projections of future discounted cash flows for each of our reporting units in determining their fair value. The projections of future cash flows are estimates by management using the best information available at that time.

#### ***Tooling***

We support, coordinate and review the production of tooling for almost all of the products that we produce. Although such tooling is typically kept and used by us in our facilities, it may be owned either by one of our OEM customers or by us. Tooling owned by an OEM customer is accounted for in one way and tooling owned by us is accounted for in another. In each case the costs incurred by us during the development of such tooling are capitalized. These amounts are reviewed to determine whether they are impaired or not. Remaining amounts are eventually included in cost of sales or depreciated, depending on whether the tooling is owned by one of our

OEM customers or by us, as discussed further below.

**Tooling owned by an OEM customer.** Costs incurred during the development of tooling owned by one of our OEM customers are capitalized as they are incurred and booked as a current asset on our balance sheet under "Tools in process".

Once a tool that will be owned by an OEM is completed, the amounts that have been recorded during such tool's development under "Tools in process" are reclassified, affecting both our balance sheet and income statement. This reclassification leads to a trade receivable with a corresponding amount booked in our income statement as sales. The amount recorded in "Tools in process" is reflected under cost of sales.

The "completed contract method" under which revenues and trade receivables are recognized in connection with tools owned by an OEM customer and the products to be produced by them allows for the recognition of revenue only when the tool in question is accepted by the OEM customer and we are ready to begin production of the corresponding product. At the time that a contract is signed to provide the tooling and corresponding products to one of our OEM customers, we estimate the revenues and costs associated with the project. We review these estimates periodically and when the revenues and costs associated with an individual project indicate a loss, a provision is made. Factors that are considered in forecasting losses with respect to a contract include, among other things, cost overruns and non-reimbursable costs.

**Tools owned by us.** Costs incurred during the development of tooling owned by us are capitalized as they are incurred and booked as an asset on our balance sheet under "Payments on account and assets under construction". Sometimes an OEM will contribute to or otherwise subsidize the development of tooling owned by us. These contributions or subsidies, prior to the completion of the tooling they are related to, are recorded as an asset under "Cash on hand, bank balances and checks" on our balance sheet and an equivalent liability under "Payments received on account of orders".

Once a tool owned by us is completed, the amounts that have been recorded during its development under "Payments on account and assets under construction" are reclassified on our balance sheet under "Tools". At the same time, any corresponding liability in respect of contributions or subsidies received in respect of such tool from an OEM and previously recorded under "Payment received on account of orders" is reclassified on our balance sheet under "Deferred income".

Once we begin using the tool to produce the corresponding product, the tooling owned by us that appears on our balance sheet under the heading "Tools" is depreciated using the straight line method over the estimated useful life of the tool (usually three to five years). Based on the useful life of the tool, a pro rata portion of any deferred income is recorded in our income statement as sales. The remainder of the production cost of tooling owned by us that is not received as a cash contribution or subsidy (and booked under "Deferred income") is generally recouped from the OEM as an increase in the negotiated per-part purchase price.

### ***Research & Development***

We expense general research and development, R&D, costs such as those related to the development of new products, as incurred. We also incur pre-production R&D costs related to products that we supply to OEMs under long-term agreements for the supply of such products. We expense as incurred the R&D costs for which we do not receive any agreed reimbursement from the OEM.

### ***Warranties***

We generally offer warranties on our products that correspond to the length of the warranties extended by OEMs to their customers. These typically last for one to three years. We estimate the costs of future warranty claims for our current period product sales by using historical warranty claim information but also review current information when available.

Our agreements with our customers have sales prices that relate to a negotiated level of defective parts measured in parts per million, or PPM, and allow for a range within which the PPM may vary. If the amount of defective parts is higher than this range, it will require a compensating payment by us. If the amount of defective parts is lower than this range, it will require an additional payment from an OEM to us.

### **Results of Operations**

The following table sets forth, for the periods indicated, our financial data which has been derived from our financial statements

for the three months ended March, 31, 2005 and 2004:

	<b>Three months ended March 31,</b>			
	<b>2004</b>		<b>2005</b>	
	Amount	As a % of Sales	Amount	As a % of Sales
	(in millions of euro)		(in millions of euro)	
	<i>(unaudited)</i>		<i>(unaudited)</i>	
Sales.....	242.7	100.0	228.5	100.0
Cost of sales.....	(205.2)	84.5	(198.4)	86.8
Gross profit.....	37.5	15.5	30.1	13.2
Selling costs.....	(4.7)	1.9	(4.4)	1.9
Research and development costs.....	(8.5)	3.5	(8.4)	3.7
General administrative expenses.....	(33.4)	13.8	(15.3)	6.7
Net other operating expenses.....	(4.4)	1.8	(2.3)	1.0
Loss from associated companies.....	0.0	0.0	(0.5)	0.2
Other interest and similar income.....	0.1	0.0	0.1	0.0
Interest and similar expenses.....	(7.2)	3.0	(7.5)	3.3
Result from ordinary activities.....	(20.6)	8.5	(8.2)	3.6
Extraordinary result.....	0.0	0.0	(0.2)	0.1
Income taxes.....	(3.8)	1.6	(1.7)	0.7
Net loss of the group before minority interests.....	(24.4)	10.1	(10.1)	4.4
Minority interests.....	(0.5)	0.2	(0.4)	0.2
Net loss for the period.....	(24.9)	10.3	(10.5)	4.6

**Three months ended March 31, 2005 compared to three months ended March 31, 2004**

**Sales.** Sales decreased by €4.2 million, or 5.9 %, to €228.5 million for the three months ended March 31, 2005, from €242.7 million for the same period in 2004. Excluding the effect of exchange rate movements, overall sales would have decreased by €12.8 million or 5.3%.

For the three months ended March 31, 2005 sales of our rear vision systems products decreased by €2.1 million to €150.2 million from €162.3 million. Sales of our rear and interior lighting products decreased by €5.5 million to €38.2 million from €43.7 million. Sales of our premium automotive sound systems decreased by €3.9 million to €1.8 million from €5.7 million and sales of our tools and other product increased by €7.3 million to €8.2 million from €10.9 million.

Sales in North America declined from €43.0 million to €37.9 million primarily due to overall reduced volumes from Ford and negative foreign currency effects of €1.9 million from the continued appreciation of the Euro relative to the US-Dollar. Sales in Europe decreased by €7.7 million to €42.9 million for the three months ended March 31, 2005 compared to €50.6 million in the same period of 2004. The decrease in Europe primarily resulted from longer closures of production facilities of many of our OEM customers at the beginning of 2005 compared to the beginning of 2004. In addition we experienced reduced volumes from Renault due to a slow-down of production at Renault resulting from a fire at another supplier, and from the Mercedes Car Group due to its policy to reduce its inventory. Sales decreased in the Asia Pacific region by €1.8 million from €45.8 million to €44.0 million. This decline resulted from reduced volumes which were partially offset by a positive effect of foreign currency denominated transactions of €2.4 million relating to the appreciation of the Korean Won.

**Cost of sales.** Cost of sales decreased by €6.8 million, or 3.3%, to €198.4 million for the three months ended March 31, 2005, from €205.2 million for the same period in 2004. This decrease primarily resulted from lower sales and higher costs for tooling due to the increased sales of tools, which have a low gross-profit-margin, so that the cost of sales increased as a percentage of sales from 84.5% in

the three months ended March 31, 2004 to 86.8% in the three months ended March 31, 2005.

**Selling costs.** Selling costs decreased by €0.3 million, or 6.8%, to €4.4 million for the three months ended March 31, 2005, from €4.7 million for the same period in 2004. This decrease primarily reflected lower freighting costs of €0.2 million due to the lower sales.

**Research and development costs.** R&D costs were largely unchanged at €8.4 million for the three months ended March 31, 2005 compared to €8.5 million in the same period in 2004.

**General administrative costs.** General administrative costs decreased by €8.1 million, or 54.2%, to €5.3 million for the three months ended March 31, 2005, from €33.4 million for the same period in 2004. This decrease primarily resulted from the inclusion in the first quarter of 2004 of fees and expenses of €11.1 million relating to our 2004 refinancing activities compared to the inclusion in the first quarter of 2005 of €3.3 million fees and expenses relating to our operational restructuring program 'Transition' as well as for our new financial restructuring successfully completed in May 2005.

**Net other operating expenses.** Net other operating expenses consists of the items reported in our income statement in the lines "Other operating expenses" and "Other operating income". Net other operating expenses decreased by €2.1 million from net expenses of €4.4 million for the three months ended March 31, 2004 to net expenses of €2.3 million in the same period in 2005. This improvement was primarily due to a decrease in normal goodwill depreciation of €2.6 million to €3.7 million in 2005 compared to €6.4 million in the same period in 2004 reflecting the €102.2 million write down of goodwill that we made in the last quarter of 2004. This decrease was partially off-set by a decrease in the income from subsidies of €0.4 million to €0.5 million for the three months ended March 31, 2005 from €0.9 million for the same period in 2004.

**Interest and similar expense.** Interest and similar expense increased by €0.3 million, or 4.2% to €7.5 million for three months ended March 31, 2005, from €7.2 million in the three months ended March 31, 2004. The increase reflected higher interest expenses due to the issue of our senior subordinated notes in February 2004 which resulted in a higher rate of interest on our indebtedness.

**Income taxes.** Income taxes decreased by €2.1 million, or 55.3%, to €1.7 million for the three months ended March 31, 2005 from €3.8 million for the same period in 2004. This decrease reflects a tax refund in the UK.

**Net loss.** As a result of the above factors, net loss decreased by €4.4 million to a loss of €0.5 million for the three months ended March 31, 2004 from a loss of €4.9 million for the same period in 2004.

## **Liquidity and Capital Resources**

### **Liquidity**

Our liquidity requirements arise primarily to meet our ongoing debt service requirements and to fund our capital expenditures and working capital requirements. Our principal sources of funds are expected to be cash in hand, cash flow from operations, the revolving credit facility under our senior credit facilities and certain smaller regional bilateral credit lines. Our revolving credit facility provides for borrowings of up to €50 million, of which €5.0 million was undrawn at March, 31, 2005.

Although our sales are spread fairly evenly throughout the year, our working capital experiences significant seasonal variations. Based on the operating schedule of our OEM customers, which historically has slowed down during the summer and the end of the calendar year, we experience two troughs in our working capital cycle in the summer and at the year end. There is typically a substantial decrease in our working capital between September and December of between €30 million and €50 million. This is due to a number of factors including the shutdown of production facilities by our OEM customers in the last two weeks of December (which leads to a decrease in trade receivables as existing trade receivables are collected but not replaced by new orders).

### **Indebtedness**

Our outstanding indebtedness as of March 31, 2005 was €358.5 million. €200 million of this indebtedness consisted of senior subordinated notes which are due in 2014. €136.8 million of the indebtedness consisted of borrowings under our senior credit facilities and finance leases.

Our bilateral credit lines at March 31, 2005 were €9.9 million. They consist primarily of overdrafts and discounted bills.

The following table sets forth our outstanding indebtedness as of March 31, 2005:

	<u>in millions of</u> <u>euro</u>
Senior credit facilities:	
Term loans .....	92.5
New revolving credit facility.....	45.0
Senior subordinated notes.....	200.0
Accrued interest .....	2.3
Drawn bilateral credit lines.....	9.9
Overdrafts of current accounts .....	5.7
Capital leases and other indebtedness .....	3.1
Total .....	<u>358.5</u>

In May 2005 we successfully completed a refinancing transaction of our senior credit facilities which refinanced all of our outstanding term loan and our revolving credit facility. As a result, our current new senior credit facilities consist of €155 million in second priority term loans as well as an undrawn first priority revolving credit facility of €50 million.

The following table sets forth the sources and uses of funds for the refinancing effected by our new credit facilities:

<u>Sources</u>		<u>Uses</u>	
New second priority term loans.....	155.0	Repay existing indebtedness <sup>(2)</sup>	
New revolving credit facility <sup>(1)</sup>		Revolving credit facility <sup>(3)</sup> .....	50.0
		Term Loan .....	92.5
		Cash .....	4.5
		Estimated transaction fees .....	8.0
<b>Total Sources</b>	<u><b>155.0</b></u>	<b>Total</b>	<u><b>155.0</b></u>

<sup>(1)</sup> The new revolving credit facility provides for borrowings of up to €50 million.

<sup>(2)</sup> As of April 30, 2004, we had €360.8 million of total indebtedness, approximately €142.5 million of which will be repaid using the proceeds of the refinancing, and total cash of €4.5 million. As of March 31, 2005 we had €358.5 million of total indebtedness and total cash of €23.8 million.

<sup>(3)</sup> As of March 31, 2005 €45.0 million of this revolving credit facility was drawn.

### **Cash Flows**

**Cash flow from operating activities.** Cash flows from operating activities decreased by €14.2 million to a cash outflow of €69.1 million for the three months ended March 31, 2005, compared to a cash outflow of €54.9 million for the same period in 2004. This decrease primarily resulted from a decrease in the trade payables and other liabilities of €1.7 million in the first three months of 2005 compared to a decrease of €9.7 million in the same period in 2004. This decrease was partially offset by a lower loss of €0.5 million compared to €24.9 million in the same period in 2004.

**Cash flow from investing activities.** Cash outflows for investing activities increased by €2.1 million to a cash outflow of €13.0 million in the three months period ended March 31, 2005 from a cash outflow of €10.9 million. This increase primarily resulted from a higher cash outflow from investments in property, plant and equipment as well as intangible assets.

**Cash flow from financing activities.** Cash flows from financing activities decreased to a cash inflow of €5.4 million for the three months ended March 31, 2005 compared to a cash inflow of €20.5 for the same period in 2004. In connection with our 2004 refinancing we received in the first three months of 2004 a cash inflow of €25.0 million from the issuance of the senior subordinated notes and

borrowings under senior credit facilities. We used this cash-inflow in the first quarter of 2004 to repay our then outstanding syndicated loans of €304.5 million.

### **Market Risk**

We are exposed to various market risks, including adverse changes in commodity prices, interest rates and currency exchange rates as discussed below. Market risk is the potential loss arising from adverse changes in market rates and direct material prices.

Our policy is not to enter into derivatives or other financial instruments for trading or speculative purposes. However, we sometimes enter into financial instruments to manage and reduce the impact of short-term changes in currency exchange rates with respect to specific transactions and the impact of interest rate movements on our borrowings.

### ***Commodity Pricing Risks***

We are exposed to commodity price risks through our purchase of various raw materials, such as plastic resins and aluminum. The prices of plastic resins and aluminum vary to some extent given that they are commodities. We generally have more than one supplier in each of our manufacturing regions.

### ***Interest Rate Risks***

We are subject to interest rate risks related to our borrowings. Our €200 million of senior subordinated notes due 2014 are subject to a fixed annual interest rate of 9.5%. The new second priority term loans and the new revolving credit facility bear interest at variable rates. However the interest rates on the term loans have been partially secured until mid 2007 through the use of interest derivatives (swaps and caps).

The interest risks resulting from the relatively high share of borrowed capital are monitored via monthly reporting.

### ***Currency Rate Risks***

In the currency management area, the Group's two most important currencies are the euro and the US dollar. Schefenacker is subject to currency risks because business is also done in countries in which these currencies are not the local currency (especially the Australian Dollar and Korean Won). Schefenacker benefits to a large extent from natural hedge as the associated costs are also incurred in the local currency in which sales are made. The planned cash flow between the two most important currencies for the Group is monitored regularly. Currency risks beyond this scope are hedged using appropriate currency derivatives (e.g. swaps and options) in line with the instructions of the management board.

### **Summary of Significant Differences between German GAAP and US GAAP**

Our consolidated financial statements have been presented in conformity with German GAAP and differ in certain significant respects from financial statements prepared in conformity with US GAAP. The following is a brief description of certain differences between German GAAP and US GAAP which may be significant to the consolidated financial statements of the Company. This summary is not intended to provide a comprehensive listing of all differences between German GAAP and US GAAP.

### ***Basis of Presentation***

German GAAP and US GAAP differ in certain fundamental respects. Under German law a company's financial statements are prepared in a similar manner as those prepared for taxation purposes. German companies, therefore, often apply more conservative valuation methods in their financial statements reflecting the principle of prudence. In addition, German GAAP financial statements are generally prepared with creditor protection in mind, while US GAAP is based on providing information in a form that assists investor decision making.

### ***Financial statement presentation***

Under German GAAP, the balance sheet and the income statement are classified differently than under US GAAP. The balance sheet according to US GAAP is based on the liquidity of the account balances, with the most liquid item being presented first. Moreover

assets and liabilities are categorized into current and long-term items. German GAAP, on the other hand, requires companies to disclose their assets separately as either fixed or current assets, with liabilities presented as current and long-term similar to US GAAP.

**Goodwill**

Under German GAAP the difference between the cost of acquisition and the fair market value of the identifiable assets arising from an acquisition, goodwill, can be written off immediately to capital reserves or be capitalized and amortized over its useful life, usually between five and 15 years. In addition to regularly scheduled amortization of goodwill, existing goodwill is required to be tested for impairment at least annually and any impaired amounts written off as a charge in the income statement. However, after an impairment write-off has been made, it is permissible under German GAAP to write-up goodwill that has previously been written-off due to impairment if circumstances subsequently improve.

Under US GAAP pursuant to Statements of Financial Accounting Standards ("SFAS") No. 141 "Business Combinations" and SFAS No. 142 "Goodwill and other Intangible Assets" goodwill is no longer amortized. Existing goodwill is required to be tested for impairment annually and impaired goodwill is not allowed to be written back up. Moreover, the purchase price allocation performed according to US GAAP as it relates to the identification of other intangible assets is often more stringent in identifying and separating these intangibles from goodwill.

**Tangible fixed assets**

In accordance with German GAAP, tangible property, plant and equipment is depreciated using the straight-line method over the estimated useful life of the asset. Low-value assets are fully depreciated in the year of acquisition. The following useful lives are prescribed under German GAAP as well as German tax law:

	<b>Useful life in years</b>
Buildings and land improvements .....	10-50
Technical equipment and machines .....	5-10
Tools .....	3-5
Other equipment, furniture and fixtures.....	3-10

Property, plant and equipment are reviewed for impairment whenever events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. Measurement of an impairment loss for long-lived assets that are expected to be held and used is based on the fair value of the asset.

Under US GAAP, tangible fixed assets are generally depreciated on a straight-line basis over their estimated useful life. Long-lived assets are also reviewed for impairment whenever events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. An impairment is recognized in accordance with SFAS No. 144 "Accounting for the Impairment or Disposal of Long-Lived Assets" when a long-lived asset's carrying amount exceeds the sum of the estimated undiscounted future cash flows. The carrying value of such an impaired asset is written down to its fair value.

**Tooling**

Tooling costs for use by customers and which we own are classified as fixed assets under German GAAP. Tooling costs are classified as inventories when tools are to be owned by customers. In both cases they are valued at the manufacturing or purchased costs. Contributions received from customers for the production or purchase of company-owned tooling are disclosed as deferred income and are amortized over the term of the agreement made with the customer. See "—Critical Accounting Policies—Tooling" above.

In accordance with US GAAP, contributions received from customers for tooling costs are deducted from the capitalized tooling costs. The excess of contributions received from customers for the production or purchase of tooling not owned by us should be disclosed as deferred income and amortized over the terms of the supply agreement made with the customers.

### ***Foreign currency conversion***

Under German GAAP, foreign currency receivables are accounted for according to the lowest value principle, which employs the lower of the exchange rate as of the balance sheet date or the rate in effect when the receivable was booked, and foreign currency liabilities according to the highest value principle, which employs the higher of the exchange rate at the balance sheet date or the rate in effect when the liability was booked. As a result, only unrealized losses are anticipated, whereas unrealized profits from currency rate developments remain unaccounted for as of the balance sheet date.

According to US GAAP, receivables and payables are converted from the foreign currency and presented at the rate on the balance sheet date. Unrealized profits and losses are recognized in net income.

In the preparation of consolidated financial statements according to German GAAP, balance sheets of subsidiaries whose reporting currency is different from that of the parent company are converted using rates prevailing as of the balance sheet date except for equity, which is converted using historic rates. The difference is shown as a cumulative translation adjustment within the consolidated equity.

The profit and loss statement of such subsidiaries are converted using an appropriately weighted average exchange rate for the period. Net income is converted using rates as of the balance sheet date. The difference is shown either in other operating income or other operating expenses depending on whether it is positive or negative.

SFAS No. 52 "Foreign Currency Translation" states that the first step in the translation process according to US GAAP is to identify the functional currency for each entity included in the financial statements of the company. According to this Statement, the assets and liabilities of a foreign subsidiary are translated from the functional currency to the reporting currency using the exchange rate in effect as of the balance sheet date and revenues, expenses, gains, and losses are converted using an appropriately weighted average exchange rate for the period. If the functional currency of the foreign operation is its local currency, the adjustments from the translation into the reporting currency are reported as other comprehensive income (for example, cumulative translation adjustment) in shareholders' equity. If the functional currency of the foreign operation is not the same as its local currency, a re-measurement takes place and all adjustments arising from the re-measurement are included in net income.

### ***Capital leases***

In accordance with German GAAP, lease obligations may be capitalized under certain circumstances. However, the criteria applied under German GAAP are different to those under US GAAP.

US GAAP requires leased assets to be capitalized if they meet specific criteria as stated in SFAS No. 13 "Accounting for Leases" and be depreciated using the straight-line method over the useful life of the asset or the duration of the lease. Payment obligations relating to such leases are recorded as liabilities at their present value.

### ***Receivables from deliveries and services***

Under German GAAP, lump-sum allowances can be recorded in order to cover general credit and default risks in with respect to the realization of existing receivables.

US GAAP only permits allowances to be recorded on the basis of past collection experience and specific cases where collection is questionable based on the guidance set forth in SFAS No. 5 "Accounting for Contingencies".

### ***Deferred taxes***

German GAAP stipulates that deferred assets resulting from an existing tax loss carryover cannot be capitalized. However, German GAAP gives companies the option of including or not including deferred tax assets other than tax losses carryover in consolidated financial statements. Either deferred tax assets or deferred tax liabilities on consolidation measurements are mandatory for consolidated financial statements.

According to US GAAP, deferred assets resulting from tax loss carryovers must be capitalized. A valuation allowance is recognized on the deferred tax asset if, based on the weight of available evidence, it is more likely than not that some portion or all of the deferred tax asset will not be realized.

### ***Special items for investment subsidies***

In our balance sheet appears a position under the caption "Special Item for Investment Subsidies". German tax law permits investment subsidies to be recorded in the balance sheet, instead of recording them in the income statement, provided that such subsidies are recorded in the statutory balance sheet in this separate item between the equity and the liabilities.

US GAAP does not provide for a special reserve with an equity portion, because such a reserve results from measures adopted purely for German tax purposes.

### ***Pension obligations***

The calculation of pension obligations in accordance with German GAAP is carried out on the basis of the present value method, whereby among other things, probable future salary and contribution increases are not taken into account. German GAAP also requires pension provisions to be calculated using an interest rate of 6.0% as established under German law.

Pension obligations in accordance with US GAAP are calculated on the basis of the "Projected Unit Credit Method". The yardstick for measuring the defined benefit pension obligations is the "Projected Benefit Obligation", or PBO. The PBO is the present value of the pension rights earned as of the valuation date. This method takes into account current country-specific interest rates derived from the long-term capital market, future probable rates of salary increases and probable pension increases.

### ***Accrued liabilities***

Under German GAAP, accruals are accounted for within good business practice.

In accordance with US GAAP, contingent liabilities are recorded if a claim is "probable" and the amount of the accrual can be reliably estimated. When assessing the amount of the accrual, the most probable value should be recorded and, in the case of several values of equal probability, the lowest value should be shown.

### ***Restructuring***

Under German GAAP, the estimated costs of employee separation must be accrued when a restructuring plan is introduced.

In June 2002, the US Financial Accounting Standards Board (FASB) issued SFAS No. 146 "Accounting for Costs Associated with Exit and Disposal Activities", which was required to be adopted in 2003. The expected costs associated with the exit or disposal of business activities can only be accrued when a liability against a third party exists. This includes severance payments for employees, the cancellation of contracts, the shut-down of production facilities and the relocation of employees.

### ***Accounting for derivatives***

Under German GAAP, derivative financial instruments are only included in the financial statements to recognize unrealized losses. Under US GAAP, these derivatives are recorded as of the balance sheet date at their fair market value.

## INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

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SCHEFENACKER AG UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS  
AS OF AND FOR THE THREE MONTHS ENDED MARCH 31, 2004 AND 2005 UNAUDITED CONSOLIDATED BALANCE SHEETS

<u>ASSETS</u>	<u>As of March 31,</u>	
	<u>2004</u>	<u>2005</u>
	(€in millions)	
<b>Intangible assets</b>		
Franchises, industrial and similar rights and assets and licences in such rights and assets.....	1.4	1.9
Goodwill.....	295.7	160.1
<b>Total intangible assets</b> .....	<u>297.1</u>	<u>162.0</u>
<b>Property, plant and equipment</b>		
Land, land rights and buildings including buildings on third-party land.....	76.8	85.4
Technical equipment and machines.....	83.8	81.9
Tools.....	20.6	20.7
Other equipment, furniture and fixtures.....	15.1	12.8
Payments on account and assets under construction.....	23.1	18.9
<b>Total property, plant and equipment</b> .....	<u>219.4</u>	<u>219.7</u>
<b>Financial assets</b>		
Shares in associated companies.....	0.1	0.4
Equity investments.....	0.2	0.1
Long-term investments.....	0.0	0.1
Other financial assets.....	2.0	0.1
<b>Total financial assets</b> .....	<u>2.3</u>	<u>0.7</u>
<b>TOTAL FIXED ASSETS</b> .....	<u>518.8</u>	<u>382.4</u>
<b>Inventories</b>		
Raw materials, consumables and supplies.....	23.8	27.1
Work in process.....	8.5	7.0
Finished goods and merchandise.....	21.6	20.9
Tools in process.....	28.6	29.1
<b>Total inventories</b> .....	<u>82.5</u>	<u>84.1</u>
<b>Receivables and other assets</b>		
Trade receivables.....	132.8	120.2
Receivables from associated companies.....	2.3	0.9
Other assets.....	18.3	16.3
<b>Total receivables and other assets</b> .....	<u>153.4</u>	<u>137.4</u>
<b>Cash on hand, bank balances and checks</b> .....	<u>21.7</u>	<u>23.8</u>
<b>TOTAL CURRENT ASSETS</b> .....	<u>257.6</u>	<u>245.3</u>
<b>TOTAL PREPAID EXPENSES</b> .....	<u>0.8</u>	<u>1.7</u>
<b>DEFICIT NOT COVERED BY EQUITY</b> .....	<u>0.0</u>	<u>71.2</u>
<b>TOTAL ASSETS</b> .....	<u>777.2</u>	<u>700.6</u>

SCHEFENACKER AG UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS  
AS OF AND FOR THE THREE MONTHS ENDED MARCH 31, 2004 AND 2005 (Continued) UNAUDITED CONSOLIDATED  
BALANCE SHEETS

<b><u>EQUITY AND LIABILITIES</u></b>	<b>As of March 31,</b>	
	<b><u>2004</u></b>	<b><u>2005</u></b>
	<b>(€in millions)</b>	
<b>Equity</b>		
Subscribed capital .....	250.0	250.0
Capital reserves .....	123.9	123.9
Adjustment item for currency differences .....	(9.9)	(18.1)
Loss carryforward from the prior year .....	(240.8)	(422.6)
Net loss of the Group for the year .....	(24.9)	(10.5)
Adjustment item for minority interests.....	4.5	6.1
Deficit not covered by equity.....	0.0	71.2
<b>Total equity</b> .....	<b>102.8</b>	<b>0.0</b>
<b>Special item for investment subsidies</b> .....	<b>0.8</b>	<b>0.6</b>
<b>Accruals</b>		
Accruals for pensions and similar obligations .....	25.5	27.2
Tax accruals .....	13.9	14.3
Other accruals.....	41.1	58.2
<b>Total accruals</b> .....	<b>80.5</b>	<b>99.7</b>
<b>Liabilities</b>		
Bonds.....	202.6	200.0
Liabilities to banks .....	144.5	158.5
Payments received on account of orders .....	16.3	9.2
Trade payables .....	112.9	109.4
Liabilities to associated companies .....	0.6	0.3
Other liabilities.....	104.9	108.3
<b>Total liabilities</b> .....	<b>581.8</b>	<b>585.7</b>
<b>Deferred income</b> .....	<b>11.3</b>	<b>14.6</b>
<b>TOTAL EQUITY AND LIABILITIES</b> .....	<b>777.2</b>	<b>700.6</b>

SCHEFENACKER AG UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS AS OF AND FOR THE THREE MONTHS ENDED MARCH 31, 2004 AND 2005 (Continued) UNAUDITED CONSOLIDATED INCOME STATEMENT

	Three months ended	
	March 31,	
	<u>2004</u>	<u>2005</u>
	(€in millions)	
Sales.....	242.7	228.5
Cost of sales.....	(205.2)	(198.4)
<b>Gross profit</b> .....	<u>37.5</u>	<u>30.1</u>
Selling costs.....	(4.7)	(4.4)
Research and development costs .....	(8.5)	(8.4)
General administrative costs .....	(33.4)	(15.3)
Other operating income.....	3.1	2.6
Other operating expenses.....	(7.5)	(4.9)
Loss from associated companies .....	(0.0)	(0.5)
Other interest and similar income.....	0.1	0.1
Interest and similar expense.....	(7.2)	(7.5)
<b>Result from ordinary activities</b> .....	<u>(20.6)</u>	<u>(8.2)</u>
Extraordinary.....	0.0	(0.2)
Income taxes.....	(3.8)	(1.7)
<b>Net loss of the Group for the year before minority interests</b> .....	<u>(24.4)</u>	<u>(10.1)</u>
Minority interests .....	(0.5)	(0.4)
<b>Net loss of the Group for the year</b> .....	<u>(24.9)</u>	<u>(10.5)</u>
Loss carryforward from the prior year.....	(240.8)	(422.6)
<b>ACCUMULATED DEFICIT OF THE GROUP</b> .....	<u>(265.7)</u>	<u>(433.1)</u>

SCHEFENACKER AG UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS  
AS OF AND FOR THE THREE MONTHS ENDED MARCH 31, 2004 AND 2005 (Continued) UNAUDITED CONSOLIDATED  
STATEMENT OF CASH FLOWS

	Three months ended	
	<u>March 31,</u>	
	<u>2004</u>	<u>2005</u>
	(€ in millions)	
<b>Cash flow from operating activities</b>		
Net loss for the period .....	(24.9)	(10.5)
Amortization/depreciation of fixed assets .....	16.3	13.8
Increase/decrease in accruals .....	3.9	2.2
Other non-cash expenses/income.....	1.5	(8.3)
Gain/loss on the disposal of assets.....	1.6	(0.1)
Increase/decrease in inventories, trade receivables and other assets .....	(33.6)	(24.5)
Increase/decrease in trade payables and other liabilities .....	(19.7)	(41.7)
<b>TOTAL CASH FLOW FROM OPERATING ACTIVITIES .....</b>	<b>(54.9)</b>	<b>(69.1)</b>
<b>Cash flow from investing activities</b>		
Cash received from the disposal of property, plant and equipment/intangible assets .....	0.0	0.1
Cash paid for investments in property, plant and equipment/intangible assets .....	(10.0)	(13.1)
Cash received from the disposal of financial assets .....	0.0	0.0
Cash paid for investments in financial assets .....	(0.9)	0.0
<b>TOTAL CASH FLOW FROM INVESTING ACTIVITIES .....</b>	<b>(10.9)</b>	<b>(13.0)</b>
<b>Cash flow from financing activities</b>		
Additional capital payments from the shareholder.....	0.0	0.0
Cash paid to shareholders and minority interests .....	0.0	0.0
Cash received from the issue of loans .....	325.0	15.4
Cash paid for the redemption of loans .....	(304.5)	0.0
<b>TOTAL CASH FLOW FROM FINANCING ACTIVITIES.....</b>	<b>20.5</b>	<b>15.4</b>
<b>Cash and cash equivalents at the end of the period</b>		
Change in cash and cash equivalents .....	(45.3)	(66.7)
Change in cash and cash equivalents due to changes relating to exchange rates, consolidated group and cut-off date .....	0.7	1.2
Cash and cash equivalents at the beginning of the period.....	58.1	83.6
<b>TOTAL CASH AND CASH EQUIVALENTS AT THE END OF THE PERIOD .....</b>	<b>13.5</b>	<b>18.1</b>
<b>Composition of cash and cash equivalents</b>		
Cash and cash equivalents.....	21.7	23.8
Short-term liabilities due to banks .....	(8.2)	(5.7)
<b>TOTAL COMPOSITION OF CASH AND CASH EQUIVALENTS AT END OF THE PERIOD .....</b>	<b>13.5</b>	<b>18.1</b>

## SCHEFENACKER AG NOTES TO THE UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS FOR THE THREE MONTHS AS OF AND ENDING MARCH 31, 2004 AND 2005

### **Preliminary remarks**

The parent company Schefenacker Aktiengesellschaft, Esslingen ("Schefenacker AG" or "the Company"), was incorporated on June 13, 2000 and filed with the commercial register on August 1, 2000.

The consolidated financial statements of Schefenacker AG as of March 31, 2005 were prepared in accordance with the provisions of the German Commercial Code (HGB).

The cost-of-sales method was used to prepare the consolidated income statement.

The Group's interim consolidated financial statements are not subjected to any audits.

This interim report has been prepared in accordance with German Accounting Standard (GAS) No. 6.

### **Consolidated Companies**

The principles for determining the consolidated group in accordance with Secs. 294 et seq. HGB are the same as those used in the 2004 consolidated financial statements.

The consolidated group consists of Schefenacker AG, 13 companies registered in Germany and 25 firms domiciled outside Germany, each of which is controlled by Schefenacker AG.

No major changes have occurred since December 31, 2004.

### **Accounting and Valuation Policies**

The methods of consolidation, accounting and valuation of the consolidated financial statements as of December 31, 2004 have been retained in the interim consolidated financial statements for the three months ended March 31, 2005. A detailed description of these principles and methods can be found in the notes to the 2004 consolidated financial statements.

### **Significant Events**

In the first quarter 2005 we started to reorganize our financial structure, which we successfully completed in May 2005 by refinancing our senior credit facilities. Our new senior credit facilities consist of €155 million in second priority term loans as well as first priority revolving credit facility of €50 million, which is currently undrawn. The net proceeds were used to repay our then outstanding term loan and our then outstanding revolving credit facilities. In connection with this refinancing, bank fees and legal and consulting fees of €2.3 million were incurred in the first quarter.

In January 2005 Mr. Hans-Joachim Lange joined the Management Board of Schefenacker AG as our new Chief Executive Officer.

### **Investments in Research and Development**

The expenses for R&D include the usual pre-production cost for vision, lighting and audio systems as well as the R&D costs for advanced technologies. Research and development costs are recorded net of €0.4 million in subsidies received from OEMs.

## Sales

### Breakdown by product

	<b>January 1- March 31,</b>	
	<b>2004</b>	<b>2005</b>
	<b>(€in millions)</b>	
Vision systems.....	162.3	150.2
Lighting systems.....	43.7	38.2
Audio systems .....	25.7	21.8
LED.....	0.1	0.1
Tools .....	6.5	12.1
Other .....	4.4	6.1
	<u>242.7</u>	<u>228.5</u>

### Sales by region of production

	<b>January 1- March 31,</b>	
	<b>2004</b>	<b>2005</b>
	<b>(€in millions)</b>	
Europe.....	150.6	142.9
North America.....	43.0	37.9
Asia .....	45.8	44.0
Australia.....	3.3	3.7
	<u>242.7</u>	<u>228.5</u>

## Headcount

As of March 31, employee headcount was as follows:

	<b>March 31,</b>	
	<b>2004</b>	<b>2005</b>
Direct employees.....	3,569	3,439
Indirect employees .....	2,647	2,675
	<u>6,216</u>	<u>6,114</u>

## Statement of Stockholders' Equity

The equity of the Schefenacker Group developed as follows in 2005:

	December 31, 2004	Addition	Disposal	Reclassification	Currency differences	March 31, 2005
	(€in millions)					
Subscribed capital	250.0	0.0	0.0	0.0	0.0	250.0
Capital reserve	123.9	0.0	0.0	0.0	0.0	123.9
Revenue reserves	0.0	0.0	0.0	0.0	0.0	0.0
Cumulative translation adjustment	(18.5)	2.9	0.0	0.0	(2.5)	(18.1)
Loss carryforward	(240.8)	0.0	0.0	(181.8)	0.0	(422.6)
Net loss for the year	(181.8)	(10.5)	0.0	181.8	0.0	(10.5)
Adjustment item for minority interests	5.6	0.4	0.0	0.0	0.1	6.1
	<u>(61.6)</u>	<u>(7.2)</u>	<u>0.0</u>	<u>0.0</u>	<u>(2.4)</u>	<u>(71.2)</u>

## Segment reporting

The detailed description of the principles for the segment reporting can be found in the notes to the 2004 consolidated financial statements. According to GAS 6 the sales and the segment result (EBIT) of the business segments are disclosed in this interim report.

### *Segment information by business segment*

	Mirrors	Lights	Sound	Other activities	Total segments	Consolidation reconciliation	Schefenacker Group
	(€in millions)						
Sales							
External sales*	156.9	43.2	21.9	6.5	228.5	0.0	228.5
Segment result (EBIT)	5.7	(0.7)	4.1	(5.6)	3.5	(3.9)	(0.4)

\* including sales of tools