

## Status Report

Research and Development

Outlook



## Directors' Status Report

Hella KGaA Hueck & Co., as the parent company of the Group, provides typical Group services for the affiliated companies in the centralized units of Development, Purchasing and Sales and Financing. In addition, as the largest development, production, and sales company of the Group, it is also closely involved in the worldwide activities and in the development of all the Group's companies.

Therefore, this Status Report on the company pursuant to § 315 (3) in conjunction with § 298 (3) of the German Commercial Code (HGB) is combined with the Status Report on the Group as a whole.

### General Economic Conditions

Sales and production by the automotive industry were both up 2 percent worldwide in 2003. Most of this overall positive balance was again due to the Asian – particularly Chinese – automotive industry. As during the previous year, sales were up as much as 35 percent in China. Demand for passenger cars alone grew by 74 percent. Production also rose by 84 percent. China now occupies fourth place when it comes to automotive production, which underlines its increasing importance for the world market.

There was also growth in the Central and Eastern European countries. Sales in those countries were up by 7 percent and production rose by 2 percent. In contrast, there is still a downward trend in Western Europe, where sales figures dropped 1 percent and production figures declined by 0.5 percent.

A reversal of last year's negative trend could not be observed throughout the entire NAFTA region. Overall sales were 1 percent less than the previous year's level and down as much as 6 percent in the passenger car segment. Production also declined by 3 percent on the North American continent.

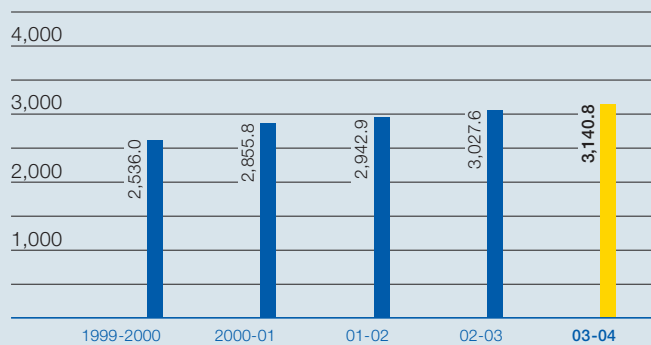
### Sales and Returns

In spite of the stagnating economic situation, sales by the Hella Group rose 3.7 percent from € 3,027.6 million to € 3,140.8 million. The lion's share of the increase went to subsidiaries in the Asia-Pacific region, where sales were up by 21.4 percent. Sales in Europe outside of Germany also rose by 19.7 percent. In contrast, sales figures for the American companies declined, as was the case during the previous year. That trend is primarily on account of exchange rates as well as the decline in returns from operational business.

	2003-04	(+/-)	Share	2002-03
Germany	1,848.5	(-1.0 %)	58.9 %	1,868.0
Europe outside Germany	809.5	(+19.7 %)	25.8 %	676.4
America	310.4	(-9.0 %)	9.8 %	341.2
Asia-Pacific	172.4	(+21.4 %)	5.5 %	142.0
<b>Group Sales</b>	<b>3,140.8</b>	<b>(+3.7 %)</b>		<b>3,027.6</b>

Other corporate earnings rose by € 33.8 million or 36.7 % as opposed to the previous year. That increase is primarily a result of the sale of securities of Hella KGaA and also of other returns.

#### Sales, Hella Group (in million €) \*



\* Graph not verified

The material input ratio rose from 50 percent to 54.3 percent. Shifts in the product mix and outsourcing projects are the main reasons for this. While more upmarket headlamps that contain a great deal of electronics were sold, fewer simpler headlamps were built than planned. The material input ratio is significantly higher for the top-of-the-line headlamps and lamps. One important element of the outsourcing program is the external supplying of plastic cover lenses to our lighting locations in Slovenia and Slovakia. Another major reason for the increase in material costs is the relatively high number of startups during the past fiscal year.

Personnel costs rose from € 857.5 million to € 888.2 million, around 3.6 percent. A fact which means that the increase in personnel costs corresponded to the rise in sales. It should be noted that personnel costs include provision of reserves for employee early retirement and compensation schemes, amounts totaling € 17 million. Without those restructuring expenses, personnel costs would have been € 871.2 million, achieving a ratio of 27.7 percent.

#### Percent of Sales

Hella Group (in million €) *	2003-04	(+/-)	2002-03
Automotive Sales	3,092.4	(+ 3.0 %)	3,001.1
Automotive industry	2,341.3		2,265.2
Motor vehicle trade	751.1		735.9
Other Sales	48.4	(+ 82.6 %)	26.5
<b>Consolidated Sales</b>	<b>3,140.8</b>	<b>(+ 3.7 %)</b>	<b>3,027.6</b>

\* Graph not verified

There were 23,895 employees worldwide as of the balance sheet date of May 31, 2004. That is a 4.8 increase in the number of employees this year.

<b>Worldwide Employment Structure</b>	<b>05/31/2004</b>	<b>Change</b>
Germany	12,908	+1.1 %
Europe outside Germany	5,880	+8.9 %
America	2,785	-0.3 %
Asia-Pacific	2,322	+25.9 %
<b>Permanent Employees Worldwide</b>	<b>23,895</b>	<b>+4.8 %</b>

Other expenditure of the Group rose by € 53.6 million on the previous year's level. The main reasons for the increase were the costs of implementing additional SAP modules totaling € 11 million and expenses for the use of external employees, particularly in the area of Development.

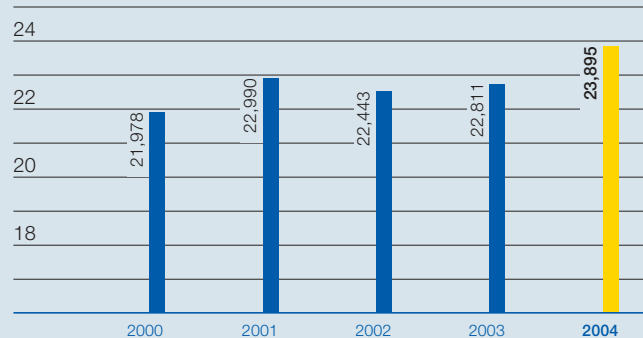
A total of € 245.6 million was invested in tangible assets, such as property, plants and equipment this fiscal year. That amounted to a 9.2 percent increase when compared with the previous year's level of € 224.9 million.

Capital expenditure can be broken down as follows:

<b>(in million €)</b>	
Land and buildings	19.7
Technical equipment and machines	132.3
Other equipment, factory and office equipment	40.6
Advance payments and construction work in progress	53.0
<b>Total Investments</b>	<b>245.6</b>

About half of all investments were made by the German companies. In the area of technical equipment and machines, around € 69 million was invested in Hella KGaA and the German subsidiaries, approximately € 41 million was invested in the European region, and approximately € 11 million went to the Asia-Pacific region.

#### **Hella Group Employees (in thousands) \***



\* Graph not verified

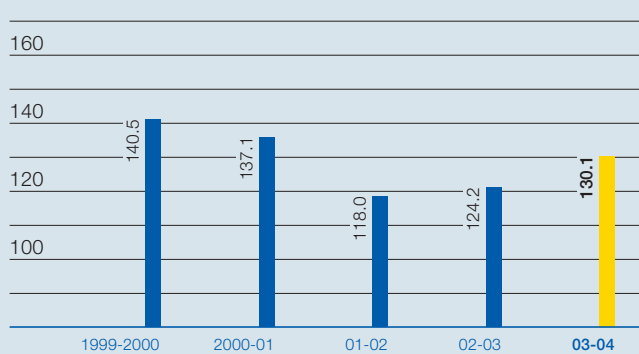
Most of the capital expenditure for technical equipment and machinery was also invested in Germany and the rest of Europe (total about € 34 million). The same applied to advance payments and construction work in progress, for which investments in Germany and Europe alone totaled almost € 31 million. The American volume of investment in this asset entry was about € 12 million. It should also be remembered that three new factories began operation in Slovakia during the past fiscal year, while a tool-building subsidiary and a new production facility started operating in China.

The previous fiscal year saw depreciation values for the Group rising by 4.2 percent to a total of € 188.7 million. However, the depreciation expense ratio remained constant at about 6 percent.

The operational result of € 133.8 million, which reflects the change in consolidation of the joint venture with Behr (full consolidation during the previous year, now proportional consolidation), managed to attain the previous year's level (€ 132.7 million) in spite of a continued difficult economic environment. However, that result is offset by considerable

spending on necessary restructuring measures. For example, we had to make significant capacity adjustments in our largest lighting plant in Lippstadt. In order to achieve such changes while at the same time showing the maximum amount of social responsibility, we implemented, and indeed with success, an early retirement and compensation payment scheme. When that special expenditure is taken into account, our profit from ordinary operations declined from € 120.2 million to € 75.6 million or by about 37 percent. The effects of such additional structural costs will continue to be felt in subsequent years.

**Ratio of Investments to Depreciation, Hella Group (%) \***



\* Graph not verified

### Financial Position

The Group's financial position can be described as follows:

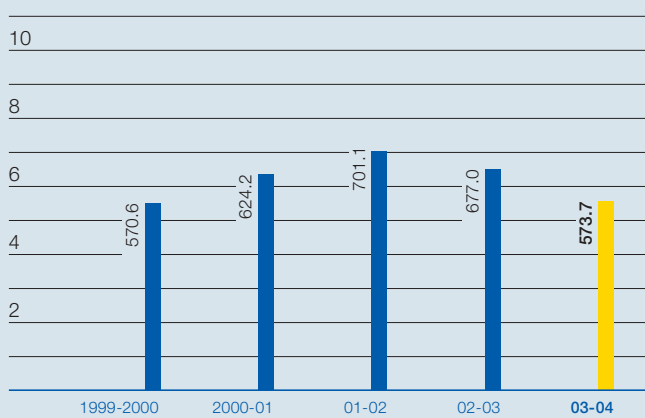
The Group's balance sheet total rose by € 9.2 million or 0.5 percent to € 2,044.6 million.

Tangible assets rose from € 666.8 to € 712.5 million. That is 34.8 percent of the balance sheet total.

Financial assets rose from € 193.2 million to € 197.7 million. They include among other things a 5 percent investment in the South Korean supplier, Samlip Industrial Co. Ltd., a firm with which Hella KGaA is already operating several joint ventures. We have also further increased our involvement with our network partner Leoni. We fully participated in the increase in the share capital of Leoni AG after the balance sheet date.

Inventories went up from € 412.6 million to € 438.8 million. That increase can be mainly attributed to two effects. Firstly, around € 14 million in assets made up the inventory that is being contributed to leasing contracts in the coming fiscal year and, secondly, advance payments to suppliers rose from € 6.1 million to € 10.3 million. Our Optimax logistics project is running according to plan. Inventory reductions were achieved on various counts but the ensuing benefits were unfortunately somewhat eroded as a result of the startup of new factories and the associated creation of additional inventories. In the area of Working Capital, we will again make greater efforts to achieve a considerable reduction.

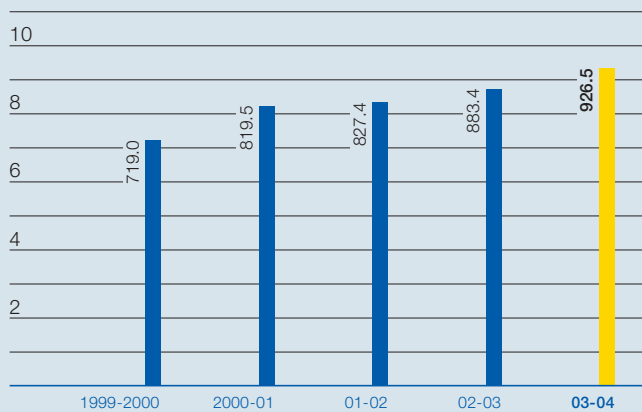
### Equity Capital, Hella Group (in million €) \*



\* Graph not verified

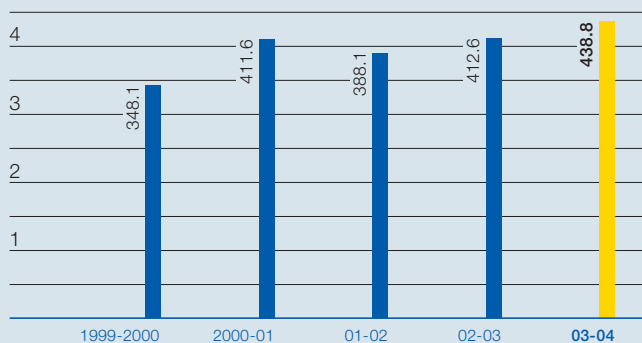
On the liabilities side of the balance sheet, equity capital declined by 15.3 percent or € 103.3 million in spite of the positive result. This is related to several factors, including the conversion of the company form from a limited partnership (KG) to a partnership limited by shares (KGaA). The change in the legal form could, in future, have increased the burden of gift and inheritance taxes when transferring shares in the company. These adverse tax consequences were allowed for by the giving of gifts of a considerable number of shares in the company well in advance. And this was financed with retained income. In order to compensate for that reduction in equity capital in the coming years as quickly as possible, the general partners have declared that no dividends will be paid for the year under review or during the next four fiscal years. The reduction in retained income was more than offset in terms of cash by a € 175 million loan with a 30-year repayment term. Given this term, we consider these funds to be an adequate replacement for the equity capital. The equity capital ratio is currently 28.1 percent or, after cash adjustment, 31.6 percent. As a result of the aforementioned measures, we anticipate that we will again achieve our unchanged target value of 40 percent over the next few years.

**Fixed Assets, Hella Group (in million €) \***



\* Graph not verified

**Inventories, Hella Group (in million €) \***



\* Graph not verified

<b>R &amp; D Expenditure, Hella KGaA (in million €) *</b>	<b>2003-04</b>	<b>2002-03</b>	<b>2001-02</b>	<b>2000-01</b>	<b>1999-2000</b>
Lighting systems	55.8	69.4	63.3	56.8	53.9
Electronics	102.1	87.5	75.7	68.2	57.9
Vehicle modules **	–	–	–	–	5.3
Aftermarket products	13.8	11.0	10.1	8.9	5.5
Miscellaneous	–	–	1.3	0.5	1.7
<b>Total</b>	<b>171.7</b>	<b>167.9</b>	<b>150.4</b>	<b>134.5</b>	<b>124.3</b>
As a % of sales	9.6 %	9.5 %	9.5 %	8.6 %	8.1 %

\* Graph not verified \*\* Independent company

We were one year early in almost completely redeeming certificates of participation to the amount of €69 million, certificates which were to mature in December 2004. We have increased the total volume by around €19 million. Most of the new certificates of participation now run until May 2010.

We have also replaced our normal one-year bilateral line of credit by a five-year syndicated credit arrangement totaling €600 million. Thanks to those capital measures and taking into account our restructuring costs, Moody's has confirmed our investment rating to be of a stable nature.

Accruals rose from €397 million to €417 million as a result of accruals for our early retirement and compensation schemes as well as thanks to a considerable increase in accruals for warranties.

### Research and Development

With a view to enhancing and further increasing our company's innovative potential, enormous investments were made in research and development during this fiscal year, too. As was the case for the previous year, most investments were carried out for Hella KGaA.

A total of €171.7 million was spent on research and development during the past fiscal year. As during the previous year, that expenditure amounted to about 5.5 percent of sales and is also about 2 percent over the previous year's level. The majority of our outlay on research and development was for the business divisions Light and Electronics. This accounted for almost 92 percent of total research and development expenditure during the past fiscal year.

We are continuing at a swift pace with the establishment of research and development sites near production locations. In addition to further expansion of existing locations in Europe, two new development centers have been opened in China.

### Outlook

At present we estimate an increase in sales of 1.7 percent for the current fiscal year. We expect the operational result to remain at the level of the past fiscal year. That result includes additional restructuring costs that did not bring about accruals. We see additional risks, not all of which were reflected in our planning, regarding the potential increase in the price of plastics following the rise in oil prices. Price hikes as a result of higher steel prices will also affect us.

The trend for the price of electronic components is not yet clear. We are still exposed to unchanging price pressure from our customers; all manufacturers have launched programs of this type. However, we assume that we have sufficiently taken the effects of such programs into account in our planning.

Higher pre-financing for development and tool costs are still hitting us hard, but they were included in our planned interest costs for the current fiscal year.

However, the aforementioned additional risks are offset by opportunities that are also not fully reflected in our planning. We are therefore confident – not least due to measures that have been taken and as a result of further cost reductions – of being able to keep the operational result at the level of the previous year.

There have been no further events of particular significance to report since the end of the fiscal year.

Lippstadt, October 4, 2004



**Dr. Jürgen Behrend**



**Dr. Rolf Breidenbach**

Consolidated Balance Sheet

Development of Consolidated Fixed Assets

