# Interim Report | 1st Quarter 2006

SALZGITTER AG
Stahl und Technologie

# Salzgitter Group in Figures

| | | 1st Quarter 2006 | 1st Quarter 2005 | Δ |
|---|---|---|---|---|
| **Sales (consolidated)** | € million | **1,983** | 1,765 | 12 % |
| Steel Division | € million | **606** | 574 | 6 % |
| Tubes Division | € million | **398** | 313 | 27 % |
| Trading Division | € million | **866** | 797 | 9 % |
| Services Division | € million | **93** | 81 | 14 % |
| Others/Consolidation Division | € million | **20** | 0 | |
| thereof flat rolled products | € million | **988** | 874 | 13 % |
| thereof sections | € million | **216** | 189 | 14 % |
| thereof tubes | € million | **519** | 420 | 24 % |
| thereof export share | % | **56** | 52 | |
| **Income form ordinary operations (EBT)** | € million | **50** | 254 | -80 % |
| **EBT from operations (before hedging transactions)** | € million | **199** | 254 | -22 % |
| **Net income for the year** | € million | **36** | 174 | -79 % |
| **Balance sheet total** | € million | **5,809** | 4,747 | 22 % |
| **Non-current assets** | € million | **1,943** | 2,087 | -7 % |
| **Current assets** | € million | **3,866** | 2,660 | 45 % |
| Inventories | € million | **1,425** | 1,303 | 9 % |
| **Equity**[1] | € million | **2,038** | 1,440 | 42 % |
| **Liabilities** | € million | **3,771** | 3,307 | 14 % |
| Non-current liabilities | € million | **2,074** | 1,924 | 8 % |
| Current liabilities | € million | **1,697** | 1,382 | 23 % |
| thereof due to banks | € million | **196** | 195 | 1 % |
| **Capital expenditure**[1] | € million | **35** | 34 | 2 % |
| **Depreciation and amortization**[1] | € million | **50** | 49 | 1 % |
| **Employees** | | | | |
| Personnel expenses | € million | **241** | 236 | 2 % |
| Workforce (period average) | | **17,020** | 17,298 | -2 % |
| **Key figures** | | | | |
| Earnings before interest and taxes (EBIT)[2] | € million | **56** | 259 | -78 % |
| EBIT before depreciation and amortization (EBITDA) | € million | **106** | 308 | -66 % |
| Earnings per share (undiluted) | € | **0.62** | 2.79 | -78 % |
| Return on capital emplyed (ROCE)[3) 4) 5)] | % | **8.8** | 52.0 | |
| Cash flow | € million | **-113** | 23 | |

Disclosure of financial data in compliance with IFRS

1) Excluding financial assets

2) EBT plus interest paid (excluding interest element in allocations to pension provisions)

3) EBIT in relation to the total of shareholders' equity (without calculation of accrued and deferred taxes), tax provisions, interest-bearing liabilities (excluding pension provisions) and liabilities from financial leasing, forfaiting and asset-backed securitization

4) Annualized 5) ROCE from operations in Q1 2006: 31.9 %

# Summary

**Steel, Tubes and Trading post record sales and excellent results in the first quarter of 2006**

Boosted by a market for rolled steel, which developed much more favorably than envisaged a few months ago, and the persistently robust demand for tubes, the **Salzgitter Group** raised sales to a new record high in the first three months of the financial year 2006. The operating result before tax stayed below the record profit of the year-earlier period.

In the second half of 2005, the situation on the European steel markets was characterized by deteriorating spot market prices due to inventory levels of consumers and traders running at excessively high levels. Consequently, the start into the new year 2006 was initially modest. The decline in sales prices in short-term business was nonetheless halted by the steady increase in order activity, which had set in since the beginning of the fourth quarter of 2005. In the course of March and April, the situation brightened swiftly and the initial skepticism concerning the trend of steel year 2006 gave way to a much more upbeat assessment of further business developments. Climbing spot market prices across the board for almost all steel products were supporting this view. The gratifyingly high volume of shipments boosted total and external sales of the **Steel Division** in the first three months of 2006. While earnings before tax remained below the record profit of the first quarter of 2005, they nonetheless exceeded the very satisfactory level of the previous quarter.

The international steel tubes industry continued its excellent performance in the first quarter of 2006. Rising oil and gas prices kept the demand of the energy sector at a consistently high level. The very satisfactory order level of the chemicals and mechanical engineering industries, as well as a strengthening construction industry, also had a positive impact on the steel tubes market. The unabated boom led to a perceptible increase in the shipments of the **Tubes Division**. The excellent pre-tax profit was boosted considerably in a comparison with the year-earlier figure, adjusted to take account of changes in the seamless tubes shareholding structure.

In the first three months of 2006, the **Trading Division** benefited from brisk global demand for steel and from the gradual recovery in the domestic economy. Both the external sales and the pre-tax profit of the Trading Division grew in the first quarter of 2006. The **Services Division** also performed well. The result of **"Consolidation and others"** was burdened by an expenditure for the partial hedging of the value increase of the participation in Vallourec S.A., and was therefore negative.

**Forecast:** On the basis of the information currently available and estimates concerning trends in the procurements and sales markets as well as the general framework conditions, and taking account of the effects of the profit improvement program, the **Salzgitter Group's operating pre-tax result is expected to reach at least € 600 million** in the current year. This forecast is, of course, net of the special effects arising from hedging transactions which are, by nature, not foreseeable as they depend on the development of the share price of Vallourec S.A. Express reference is made to the fact that opportunities and risks arising from currently unforeseeable trends in sales prices, input materials and capacity level developments, as well as changes in the currency parity, may considerably affect performance in the course of the remaining financial year 2006. The resulting fluctuation in the consolidated pre-tax result may, as experience has shown, be within a considerable range.

# Management Report

## Economic environment

In the first quarter of 2006, the **global economy** was able to match its growth rate of the past two years despite the rise in oil prices. In the USA and China in particular, the upswing remained stable despite expectations to the contrary. Whereas in China capital expenditure and exports were the main drivers of the economic trend, domestic demand proved to be the mainstay of the economy in the US, as in the past. Similarly, the gross domestic product rose in Southeast Asia, Russia and in South America as well. The International Monetary Fund sets overall global economic growth in 2006 at the level of 2005 (+4.9 %, up from +4.8 % in 2005).

The economic recovery of the **euro zone** also continued in the first three months of 2006. This development was mainly driven by investment activities picking up momentum and the export sector, which benefited from a slight depreciation in the euro as against the dollar in comparison with previous year. Despite higher employment levels in most European countries, private consumption expanded only moderately due to the slight increase in disposable income and rising energy costs. For 2006 as a whole, growth in the euro zone is expected to amount to +2.1 % (2005: +1.4 %).

In the first quarter of 2006, the **German economy** took a surprisingly sharp upturn. Supported by persistently buoyant exports, capital expenditure and industrial production expanded. The resulting positive impact on the employment situation also caused domestic demand to rise. According to leading economic institutes, however, part of the growth in consumption is due to upfront buying before the planned increase in VAT on January 1, 2007. Domestic demand is currently also underpinned by the upbeat assessment of business expectations. Accordingly, the Ifo business climate index reached its highest level for seven years at the end of March. With a growth rate of +1.8 % predicted for the whole year, against +0.9 % in the previous year, the German economy in 2006 is likely to see its strongest growth since the boom year of 2000.

**Business situation within the Group**

| | | Q1 2006 | Q1 2005 |
|---|---|---|---|
| External sales | € million | **1,983** | 1,765 |
| EBITDA | € million | **106.0** | 308.4 |
| EBIT[1)] | € million | **56.4** | 259.1 |
| Earnings before taxes (EBT) | € million | **50.2** | 253.5 |
| EBT from operations (before hedging transactions) | € million | **198.9** | 253.5 |
| Net income | € million | **35.7** | 173.5 |
| ROCE[2) 3) 4)] | % | **8.8** | 52.0 |
| Capital expenditures[5)] | € million | **35** | 34 |
| Depreciation and amortization[5)] | € million | **50** | 49 |
| Cashflow | € million | **-113** | 23 |
| Net position to banks[6)] | € million | **803** | 21 |
| Equity ratio | % | **35** | 30 |
| Core workforce | as of 31/03/ | **17,020** | 17,298 |
| Apprentices, students, trainees | as of 31/03/ | **868** | 837 |

1) EBT plus interest paid (excluding interest element in allocations to pension provisions)

2) EBIT in relation to the total of shareholders' equity (without calculation of accrued and deferred taxes), tax provisions, interest-bearing liabilities (excluding pension provisions) and liabilities from financial leasing, forfaiting and asset-backed securitization

3) Annualized 4) ROCE from operations in Q1 2006: 31.9 %

4) Excluding financial assets

6) Including securities, structured investments and collateral for hedging transactions

Boosted by a market for rolled steel, which developed much more favorably than envisaged a few months ago, and the persistently robust demand for tubes, the Salzgitter Group raised both sales and the operating results of its divisions in the first three months of 2006 as against the last quarter of 2005.

Consolidated **external sales** of € 1.98 billion generated in the first three months of 2006 were 12 % higher as compared with € 1.77 billion in the first quarter of 2005 and, at the same time, posted a new record high for quarterly sales. All divisions, especially the Tubes Division, contributed to this pleasing performance.

The **operating pre-tax result** net of special effects arising from hedging transactions came to € 198.9 million and thus remained below the record profit of the first quarter of 2005. The greatest contributors to profit were the Steel Division, followed by the Tubes and Trading Divisions.

Including expenditure of € 148.7 million, requiring disclosure under the international accounting standards, for the partial hedging of an increase in the value of the 17.2 % participation in Vallourec S.A. (which came to more than € 1 billion on the reporting date and may not be disclosed under consolidated assets) the **Group's pre-tax profit** stood at € 50.2 million in the first quarter (Q1 2005: € 253.5 million). For the purpose of hedging the value of the participation against stock price losses, option contracts with a term of up to 36 months were closed at the start of the first quarter for just under a third of the Vallourec shares held. In order to finance the options, participation in the price gains of these shares above a certain level was waived. Under the prevailing IFRS rules, the relinquished portion in price gains of the Vallourec shares must be disclosed as accrued expenses. In contrary to that, disclosure of the much higher gain in the participation, which also varies according to the Vallourec share price, is not permitted under IFRS rules.

# Management Report

**After-tax profit** posted € 35.7 million (Q1 2005: € 173.5 million). Return on capital employed (**ROCE**) came to 8.8 % and, net of the afore-mentioned special effect, reached a remarkable 31.9 % (Q1 2005: 52.0 %).

The **balance sheet total** of the Salzgitter Group rose 7 % to € 5.81 billion in the first three months of 2006 (31/12/2005: € 5.41 billion). With **non-current assets** virtually unchanged (31/03/2006: € 1.94 billion; 31/12/2005: € 1.90 billion), **current assets**, especially trade receivables which were driven by sales, rose 10 % to € 3.87 billion (31/12/2005: € 3.51 billion). Tax prepayments levied under the former group structure in 2005 and 2006 led to income tax assets increasing by € 111 million owing to the fact that the new structure of the Group (see section on "Events of significance") had not yet been incorporated by the end of March. The opposing changes of "Other receivables and other assets" versus "Cash and cash equivalents" reflect the furnishing of the interest-bearing collateral of € 137 million in the context of the partial Vallourec hedging.

On the equity and liabilities side, there was a moderate increase in **equity** (31/03/2006: € 2.04 billion; 31/12/2005: € 2.01 billion) along with a price-induced rise in trade payables of € 100 million and other liabilities of around € 200 million, mainly due to the recording of the expenditure arising from the option transactions explained above.

**Investments in tangible assets** (including intangible assets) were recorded at € 35 million in the reporting period (Q1 2005: € 34 million). Of this amount, € 23 million was accounted for by the Steel Division, in particular for the Continuous Pickling Line 2 project as well as for the modernization and the conversion of the cold rolling mill. The Division pressed ahead with work on the new power station concept "Kraftwerk 2010".

**Operating cash flow** was negative due to partially refundable tax payments and the provision of collateral (Q1 2006: € -113 million; Q1 2005: € +21 million). Including securities and structured investments and taking account of the interest-bearing collateral, the **net position due to banks** came to € +803 million as per March 31, 2006 (31/12/2005: € +822 million; 31/03/2005: € +21 million).

The **core workforce** of the Salzgitter Group stood at 16,979 employees as per March 31, 2006. The reduction in staff numbers by 57 as against March 31, 2005, was mainly due to employees entering into the non-active phase of age-related part-time employment and the deconsolidation of Eupec PipeCoatings France S.A., Joeuf (France), which was formerly consolidated proportionately. A breakdown by division shows the following changes: Steel -66, Tubes -33, Trading -24, Services +63 and Holding +3.

## Segment Reporting

| € million | Q1 2006 | Q1 2005 |
|---|---|---|
| **Consolidated sales** | | |
| Steel | **606** | 574 |
| Tubes | **398** | 313 |
| Trading | **866** | 797 |
| Services | **93** | 81 |
| Consolidation and others | **20** | 0 |
| **Group** | **1,983** | 1,765 |
| | | |
| **Income from ordinary operations** | | |
| Steel | **104.4** | 166.4 |
| Tubes | **62.2** | 77.2 |
| Trading | **30.1** | 26.3 |
| Services | **5.7** | 3.4 |
| Consolidation and others | **-152.2** | -19.8 |
| **Group** | **50.2** | 253.5 |

## Steel Division

| | | Q1 2006 | Q1 2005 |
|---|---|---|---|
| Order bookings | kt | **1,690** | 1,150 |
| Order backlog as of 31/03/ | kt | **1,254** | 1,105 |
| Crude steel production | kt | **1,421** | 1,392 |
| LD steel (SZFG) | kt | **1,183** | 1,165 |
| Electric steel (PTG) | kt | **238** | 227 |
| Rolled steel production | kt | **1,389** | 1,323 |
| Shipments | kt | **1,452** | 1,245 |
| Rolled steel | kt | **1,397** | 1,202 |
| Processed products | kt | **55** | 43 |
| Sales[1)] | € million | **836** | 786 |
| External sales | € million | **606** | 574 |
| Earnings before taxes (EBT) | € million | **104.4** | 166.4 |
| Core workforce | as of 31/03/ | **6,968** | 7,115 |

[1)] Incl. sales to other corporate divisions

In the second half of 2005, the situation on the **European steel markets** was still characterized by deteriorating spot market prices owing to the high inventory levels held by consumers and traders. Therefore, developments in the new year were initially off to a modest start. The decline in sales prices in short-term business was nonetheless halted by the steady increase in order activity, which had set in since the beginning of the fourth quarter of 2005. At this point in time, the inventory levels of end consumers and steel traders had already normalized and, in the case of some products, were even lower than average. In the course of March and April,

# Management Report

the situation brightened swiftly and the initial skepticism about the trend of steel year 2006 gave way to a much more upbeat assessment of future business developments. Climbing spot market prices across the board for almost all steel products were a contributing factor supporting this view. Only in the segment of commodity products (which, by their nature, are much more exposed to competition from imports from other non-EU countries) was initially no more than a stabilization of the situation. All in all, however, imports within the EU remained at a comparatively low level, as demand and selling prices developed positively in the regions outside the EU as well.

At the start of the year, the situation on the **raw materials procurement markets** was impacted by uncertainty about how costs would develop, as the leading steel companies at this time were conducting rotational negotiation rounds with suppliers of iron ore and coking coal. Whereas in March lead negotiation agreements brought the price of coking coal slightly down (ca -8 % on a USD basis), negotiations with iron ore suppliers were still ongoing at the beginning of May without any agreement in sight. An anticipated further increase in iron ore prices ranged from 10 % on the consumer side to 25 % on the producer side. The sea freight rates to be considered in relation with these two types of raw material had risen again by the end of March, but were still far below the previous year's level. The procurement costs of scrap have also begun to climb slightly since the start of the year and, at the end of the quarter, ranged on average at a level of around € 200 per ton. Speculative investment funds and a continuing high industrial demand led to a surge in zinc prices. Quotations for this metal, which is traded on the spot market of the London Metal Exchange, peaked at USD 2,690 per ton in March, thus trebled since mid-year 2005.

**Salzgitter Flachstahl GmbH** (SZFG) began the year with a clear recovery in orders on hand and, during the whole period under review, experienced gratifyingly strong order intake, resulting in high plant capacity utilization. Price increases of € 20 per ton had been announced for the first quarter which, however, were not fully realized. Towards the middle of the reporting period, a further price increase of between € 20 and € 50 per ton was announced for the second quarter which the market readily accepted in view of the perceptible improvement in demand. In the course of spring, a number of new contracts running from one year to several were renegotiated with major customers with the result that the sales price situation of SZFG developed positively but, seen overall, was still considerably below the average level of the first three months of 2005. Sales posted by Salzgitter Flachstahl GmbH increased in the first quarter year on year, driven by the considerably improved shipment volume. Although pre-tax earnings were substantially below the record level of the year-earlier period, they nonetheless exceeded the figure of the fourth quarter of 2005.

At the start of the year 2006, the plate market continued to pick up momentum. As the inventories of traders and consumers had normalized prior to this date, accompanied by a parallel improvement in the order position of plate processors, **Ilsenburger Grobblech GmbH** (ILG) saw order activity recover. This was reflected in the order intake that was above the already high level of the previous year's quarter and which, at the same time, enabled an improvement in average sales prices. In the commodity plate segment this advantageous situation was only supportive of price improvements to a limited extent, as imports in this product segment undercut the sales price levels of western European manufacturers. However, the full-scale plant capacity utilization of ILG through to the end of the first half-year had been secured at an early point in time. Shipments and sales again reached the most satisfactory levels of the previous year's period; the very presentable pre-tax profit fell short of the outstanding year-earlier figure owing to higher costs but nonetheless reflected a rising trend.

Low inventories and a recovery in the order position of steel construction after years of recession in the building industry as a whole resulted in order intake at **Peiner Träger GmbH** peaking in March at a level not seen for years. The dimension surcharges having been adjusted as early as the first quarter, increases in basic prices were announced for June. Shipments and sales of PTG rose significantly in a year-on-year comparison, and earnings before tax came to around the level of the previous year's period.

**HSP Hoesch Spundwand und Profil GmbH** improved both sales and shipments in comparison with the first quarter of 2005, although business came under more competitive pressure from higher imports and exchange rates, which meant that breakeven was missed marginally. At **Salzgitter Bauelemente GmbH**, sales fell short of the previous year's level owing to price levels despite a higher volume of shipments. The company generated a pre-tax profit.

**Salzgitter Europlatinen GmbH** lifted shipments, sales and profit over the first quarter of 2005 owing to sales growth rates of its automotive industry customers, which exceeded expectations.

In the first quarter of 2006, **shipments** of rolled steel and processed products of the Steel Division rose 17 % as against the relatively weak year-earlier period. As the average sales price level across all products was substantially below that of the first quarter of 2005, **total sales** grew by "only" 6 %. **External sales** with customers outside the Group also advanced 6 %. The **pre-tax result** of the segment was higher than in the last quarter of 2005, but remained substantially below the record result of the previous year's period owing to a far lower average sales price level.

**Order intake**, which climbed 47 % as against the first quarter of 2005, reached record levels, with the result that orders on hand continued to grow despite the concurrent most satisfactory volume of shipments. As per March 31, 2006, **order backlog** was 13 % higher year on year.

The **core workforce** of the Steel Division comprised 6,968 employees on March 31, 2006. This corresponds to 147 staff less as compared with the first quarter of 2005 and 66 less as against December 31, 2005. The cause of this decline in the first quarter of 2006 was due to employees entering into the active phase of age-related part-time employment and thus switching to Salzgitter Service und Technik GmbH in the Services Division.

### Tubes Division

| | | **Q1 2006** | Q1 2005 |
|---|---|---|---|
| Order bookings | € million | **358** | 417 |
| Order backlog as of 31/03/ | € million | **1,168** | 1,104 |
| Sales[1] | € million | **515** | 415 |
| External sales | € million | **398** | 313 |
| Earnings before taxes (EBT) | € million | **62.2** | 77.2 |
| Core workforce | as of 31/03/ | **4,202** | 4,261 |

[1] Incl. sales in own segment (excluding intra-company sales in the DMV Group and the EP Group) and to other corporate divisions

The **international steel tubes industry** continued to perform extremely well in the first quarter of 2006. Rising oil and gas prices kept the demand of the energy sector at a consistently high level. In the course of the remaining year, leading German economic institutes expect oil prices to fall to around USD 60 per barrel but nonetheless remain way above the long-standing average. The very satisfactory order level of the chemicals and mechanical engineering industries, as well as a recovering construction industry, also had a positive impact on the steel tubes market.

## Management Report

As a result of the positive market environment, the companies belonging to the Tubes Division saw very favorable business conditions in the first three months of the financial year 2006, which had the following impact on the individual product segments:

Boosted by strong demand, Europipe (EP) and Salzgitter Großrohre (SZGR), both companies operating in the **large-diameter pipes** segment, raised shipments, sales and pre-tax profit considerably as against the previous year’s quarter. Whereas order activity stagnated at SZGR, EP substantially expanded its order intake.

In the **medium line pipes** segment, Mannesmann Line Pipe and Röhrenwerk Gebr. Fuchs, companies operating on the market under the brand name Mannesmann Fuchs Rohr, reported a growth in sales and earnings before tax as against the first quarter of 2005. As per March 31, 2006, order intake and shipments were also higher year on year.

The **precision tubes** product segment, which comprises MHP Mannesmann Präzisrohr and Mannesmann Robur, also benefited from the persistently upbeat market environment. In comparison with the first quarter of 2005, Shipments, sales and earnings before tax improved; the order intake stabilized on a satisfying level.

Turnover of the **stainless steel tubes** producer Mannesmann DMV Stainless (DMV) expanded in the first quarter of 2006 due to higher shipments and increased sales prices. The main cause of the rise in prices was the considerably higher cost level for input materials. Earnings before tax and order intake remained unchanged from the previous year’s level. (For details on the restructuring of the DMV Group please see the section on “Events of significance”.)

Boosted by the large-diameter and medium line pipe segments, **external sales** of the Division climbed 27 % to € 398 million. Owing to the further improvement in the operating result of the consolidated tubes companies, in particular of both large-diameter pipe manufacturers, as well as brisk business in the seamless tubes business of the associated company Vallourec S.A., **pre-tax earnings** in the first quarter of 2006 came in at € 62.2 million, which was again an excellent result (Q1 2005: € 77.2 million, including € 42.9 million from the shareholding in Vallourec & Mannesmann Tubes S.A., which was sold at the end of June 2005). On a comparative basis, the profit of the tubes business was thus considerably boosted. Consolidated **order intake** normalized and **orders on hand** remained at a very high level.

With employees numbering 4,202 as per March 31, 2006, the **core workforce** had fallen by around 33 employees as compared with December 31, 2005, and by 59 members of staff as against March 31, 2005, the main cause being the deconsolidation of Eupec PipeCoatings France. DMV hired temporary staff owing to the healthy order level.

## Trading Division

| | | Q1 2006 | Q1 2005 |
|---|---|---|---|
| Shipments | kt | **1,527** | 1,463 |
| Sales[1)] | € million | **969** | 922 |
| External Sales | € million | **866** | 797 |
| Earnings before taxes (EBT) | € million | **30.1** | 26.3 |
| Core workforce | as of 31/03/ | **1,710** | 1,698 |

[1)] Incl. sales in own segment and to other corporate divisions

In the first quarter of 2006, the **market environment** for international steel trading was predominantly favorable for the companies of the Trading Division. The German construction industry, which is showing signs of recovery, provided important stimulus for domestic steel traders, while demand on the international markets remained high, boosted by the bright economic outlook. Against this backdrop, and in conjunction with the partly limited availability of some product types, the spot market prices for steel climbed again over the course of the quarter.

In the period under review, **Salzgitter Mannesmann Handel Gruppe** (SMHD Group) raised shipments, sales and pre-tax profit as against the previous year’s period. The main drivers for this pleasing trend were once again the **international trading** companies. In the first quarter, these companies invoiced for a major project in the Middle East. Business in the Middle East and Africa performed well, with the result that Salzgitter Mannesmann International GmbH, the company responsible for the regions outside NAFTA, achieved new quarterly benchmarks in shipments and sales. The North American trading companies benefited from higher margins and a larger share of high-priced products, although the companies did not hold the level of the first quarter of 2005 in terms of shipments and sales. Salzgitter Stahlhandel GmbH, the domestic **stockholding steel trader**, raised sales and profit considerably thanks to the economic recovery in Germany, and even succeeded in almost achieving the outstandingly good level of the first quarter 2004 shipments.

In the first quarter of 2006, **Universal Eisen und Stahl GmbH**, which trades in plate, recorded a slight trend towards normalization. Shipments, sales and earnings before tax fell marginally short of the previous year's outstanding figures.

Despite an increase in shipments and sales, the steel service centers **Hövelmann & Lueg** and **Robert** reported a decline in their margins and results in comparison to the excellent figures for the first quarter of 2005, caused by price hikes on the purchasing side, in particular for zinc-coated material.

Boosted primarily by the development of the SMHD Group, **external sales** of the Trading Division rose by 9 % to a new quarterly record high of € 866 million in the first three months of 2006. **Pre-tax profit** in the reporting period was up 14 % year on year. The pleasing increase in profit of the SMHD Group compensated for the development at the other companies.

As per March 31, 2006, the **core workforce** of the Trading Division numbered 1,710, which is a reduction of 24 staff members as per December 12, 2005, and an increase of 12 as against March 31, 2005. The changes fell within the scope of normal fluctuation in personnel.

# Management Report

## Services Division

| | | Q1 2006 | Q1 2005 |
|---|---|---|---|
| Sales[1)] | € million | **236** | 224 |
| External sales | € million | **93** | 81 |
| Earnings before taxes (EBT) | € million | **5.7** | 3.4 |
| Core workforce | as of 31/03/ | **3,981** | 4,068 |

[1)] Incl. sales in own segment and to other corporate divisions

The Services Division expanded its business activities in the first quarter of 2006 thanks to the favorable market environment and the associated good capacity utilization in the other divisions.

**Total sales** of the Services Division grew 5 % in the reporting period. The raw materials trading company DEUMU expanded sales mainly on the basis of the price trend of steel scrap, new metals and ferro alloys. In addition, increased charge rates due to rising cost and a higher usage of internal services had a positive impact on sales of other companies. The pleasing performance of DEUMU lifted the external sales of the segment by 14 %.

**Earnings before tax** in the reporting period stood at € 5.7 million, which is 68 % higher than the previous year's figure, adjusted to take account of the new Group structure. With the exception of Salzgitter Automotive GmbH (SZAE), all companies of the division reported positive results. SZAE, which halved its pre-tax loss through the stringently implemented restructuring program, was a major contributor to improvements in segment earnings along with DEUMU, Hansaport and Salzgitter Mannesmann Forschung, which raised their profits thanks to improved general conditions.

As per March 31, 2006, the **core workforce** of the Services Division had risen by 63 employees to 3,981 as against March 31, 2005, mainly due to taking over trainees at SZST, as well as the reallocation of employees from the other divisions entering into the active phase of age-related part-time employment. In comparison to March 31, 2005, the core workforce was reduced by 87 members of staff. This was mainly attributable to employees entering into the non-active phase of age-related part-time employment.

In order to show connection to the Salzgitter Group with its brand image rooted in the steel and technology segments, the unconsolidated company Oswald Hydroforming GmbH & Co. KG changed its name to Salzgitter Hydroforming GmbH & Co. KG as per February 23, 2006.

**Outlook**

As before, both the current general environment and the situation of the **Salzgitter Group** can be regarded as very satisfactory. The economic recovery in Germany and Europe is likely to have a positive impact on the individual segments in the next few quarters of 2006.

The sales price increases in the **Steel Division** implemented on April 1, and those announced for July 1, will to a large extent compensate for the impact of the rises in raw material and energy prices in the current year, and in some cases for the residual effect of last year's cost surges. The sales prices of rolled steel products, however, are still currently below the level of the first half of 2005. Brisk demand in all rolled steel product segments should ensure good plant capacity utilization in the months ahead.

Capacity in the **Tubes Division** is also expected to continue running at a good level. The high order level has secured capacity levels in some plants even until the end of the year and, in some cases, beyond.

The **Trading Division** is also set to develop well in the coming months. Stimulus will come from an increase in domestic and international demand for rolled steel and tubes products and, in addition, from synergies relating to procurement and shipment which are being developed further within the Salzgitter Group.

The **Services Division** is likely to maintain its generally satisfactory performance seen in the first quarter.

On the basis of the information currently available and estimates concerning trends in the procurements and sales markets as well as the general framework conditions, and taking account of the effects of the profit improvement program, the **Salzgitter Group's operating pre-tax result is expected to reach at least € 600 million** in the current year. This forecast is, of course, net of the special effects arising from hedging transactions which are, by nature, not foreseeable as they depend on the development of the share price of Vallourec S.A. Express reference is made to the fact that opportunities and risks arising from currently unforeseeable trends in sales prices, input materials and capacity level developments, as well as changes in the currency parity, may considerably affect performance in the course of the remaining financial year 2006. The resulting fluctuation in the consolidated pre-tax result may, as experience has shown, be within a considerable range.

# Management Report

**Events of significance**

For the purpose of **hedging the value of the Vallourec participation** against price losses, option contracts with a term of up to 36 months were closed at the start of the first quarter for just under a third of the Vallourec shares held. In order to finance the option, participation in the price gain of these shares above a certain level was waived. Under the prevailing IFRS rules, the relinquished portion in price gains of the Vallourec shares has to be disclosed as accrued expenses. Owing to the increase in the share price of Vallourec after the option structure had been set in place, there were accrued expenses in the amount of € 148.7 million at the end of the first quarter of 2006. At the same time, non-disclosable hidden reserves of the Vallourec participation rose by more than € 500 million to above € 1.1 billion. At the end of the second quarter, price gains in the Vallourec share are likely to necessitate accrued expenses being raised in an amount similar to the first quarter – provided that the Vallourec share on June 30, 2006, has remained at the price level quoted at the start of May 2006. On this basis, the hidden reserve of the whole participation would be above € 1.5 billion.

As regards the **action to rescind** brought against the resolution passed by the General Meeting of Shareholders on November 17, 2005, pertaining to the spin-off and transfer agreement and the request for acceptance submitted by Salzgitter AG, the District Court of Braunschweig resolved on March 6, 2006, that the action is not an obstacle to registration of the spin-off in the Commercial Register. In the meantime, the resolution has become valid under the law and the spin-off entered into the Commercial Register on April 24, 2006. The new Group structure has therefore become effective under the law and also has a tax effect on the annual financial statements of the financial year 2005.

On February 23, 2006, **Oswald Hydroforming** GmbH & Co. KG, Crimmitschau, adopted the new company name Salzgitter Hydroforming GmbH & Co. KG and started the operation of it's fourth hydroforming press.

The name of "Mannesmannröhren-Werke 4. Verwaltungsgesellschaft mbH", Mülheim an der Ruhr, was changed officially upon entry into the Commercial Register on February 15, 2006. It is trading under the name of "**Mannesmann DMV Stainless GmbH**" and is, since March 2006, the new management holding company of the DMV Group.

Preparations for the takeover of **Flachform** Stahl GmbH, Schwerte, by Hövelmann & Lueg GmbH are still underway. Following the due diligence process conducted in January, the draft of a purchase agreement has meanwhile been exchanged with Arcelor. Once the contractual negotiations have been concluded and the approval of the antitrust authority obtained, the plan is to take over Flachform, as scheduled, on July 1, 2006.

In addition, Salzgitter is currently in the process of carefully considering **acquisition options**, both in Germany and abroad.

# Consolidated Balance Sheet

| Assets in T€ | 31/03/2006 | 31/12/2005 |
|---|---|---|
| **Non-current assets** | | |
| Intangible assets | | |
| Goodwill | **1,224** | 1,224 |
| Other intangible assets | **20,975** | 22,184 |
| | **22,199** | 23,408 |
| Property, plant and equipment | **1,383,693** | 1,403,534 |
| Financial assets | **80,466** | 78,269 |
| Associated companies | **332,727** | 301,493 |
| Deferred tax assets | **119,764** | 88,712 |
| Other receivables and other assets | **3,660** | 4,008 |
| | **1,942,509** | 1,899,424 |
| **Current assets** | | |
| Inventories | **1,425,411** | 1,439,009 |
| Trade receivables | **1,116,652** | 880,237 |
| Other receivables and other assets | **385,882** | 227,595 |
| Income tax assets | **193,865** | 82,373 |
| Cash and cash equivalents | **744,324** | 884,897 |
| | **3,866,134** | 3,514,111 |
| | | |
| | **5,808,643** | 5,413,535 |

| Equity and liabilities in T€ | | |
|---|---|---|
| **Equity** | | |
| Subscribed capital | **161,615** | 161,615 |
| Capital reserve | **295,343** | 295,343 |
| Retained earnings | **1,658,528** | 1,641,221 |
| Unappropriated retained earnings | **72,375** | 64,500 |
| | **2,187,861** | 2,162,679 |
| Treasury shares | **-160,277** | -160,283 |
| | **2,027,584** | 2,002,396 |
| Minority interests | **10,089** | 9,232 |
| | **2,037,673** | 2,011,628 |
| **Non-current liabilities** | | |
| Provisions for pensions and similar obligations | **1,717,055** | 1,724,589 |
| Deferred tax liabilities | **48,549** | 40,338 |
| Income tax liabilities | **68,164** | 68,164 |
| Other provisions | **149,778** | 149,785 |
| Financial liabilities | **90,500** | 96,467 |
| | **2,074,046** | 2,079,343 |
| **Current liabilities** | | |
| Other provisions | **246,590** | 231,744 |
| Financial liabilities | **155,230** | 132,759 |
| Trade payables | **610,017** | 510,362 |
| Income tax liabilities | **132,746** | 98,953 |
| Other liabilities | **552,341** | 348,746 |
| | **1,696,924** | 1,322,564 |
| | | |
| | **5,808,643** | 5,413,535 |

# Consolidated Income Statement

| in T€ | 1st Quarter 2006 | 1st Quarter 2005 |
|---|---|---|
| Sales | 1,983,410 | 1,764,779 |
| Increase or decrease in finished goods and work in process and other own work capitalized | -5,628 | 132,214 |
| | 1,977,782 | 1,896,993 |
| Other operating earnings | 53,954 | 42,109 |
| Cost of materials | 1,320,410 | 1,238,670 |
| Personnel expenses | 240,788 | 235,652 |
| Amortization and depreciation | 49,578 | 49,266 |
| Other operating expenses | 387,496 | 195,544 |
| Income from shareholdings | -263 | 92 |
| Income from associated companies | 31,234 | 55,582 |
| Financing income | 9,303 | 3,711 |
| Financing expenses | 23,583 | 25,818 |
| **Profit on ordinary activities** | 50,155 | 253,537 |
| Income taxes | 14,477 | 78,005 |
| Other taxes | | 2,031 |
| **Consolidated net income for the year** | 35,678 | 173,501 |

| **Application of profits in T€** | | |
|---|---|---|
| Consolidated net income accruing to Salzgitter AG shareholders | 35,678 | 173,501 |
| Profit carried forward from previous year | 64,500 | 26,400 |
| Minority interest | 857 | 394 |
| Appropriation to other retained earnings | -26,946 | -166,507 |
| **Unappropriated retained earnings** | 72,375 | 33,000 |

| | | |
|---|---|---|
| **Undiluted earnings per share (in €)** | 0.62 | 2.79 |
| **Diluted earnings per share (in €)** | 0.62 | 2.78 |

# Cash Flow Statement

| in T€ | 1st Quarter 2006 | 1st Quarter 2005 |
|---|---|---|
| **Profit on ordinary activities** | **50,155** | 253,537 |
| Deprecreciations, write-downs (+)/write-ups (-) on fixed assets | **49,263** | 49,266 |
| Paid income taxes | **-112,030** | -14,439 |
| Other non-payment-related expenses (+)/income (-) | **43,333** | -24,799 |
| Interest expenses | **23,583** | 25,818 |
| Increase (-)/decrease (+) on the disposal of fixed assets | **-15,489** | -3,001 |
| Increase (-)/decrease (+) in inventories | **12,456** | -222,399 |
| Increase (-)/decrease (+) in trade receivables and other assets not attributable to investment or financing activities | **-433,400** | -113,013 |
| Payment-related increase (+)/decrease (-) in provisions | **-59,398** | -52,079 |
| Increase (-)/decrease (+) in trade payables and other liabilities not attributable to investment or financing activities | **328,331** | 124,309 |
| **Cash flow from operating activities** | **-113,196** | 23,200 |
| Cash inflow from the disposal of tangible and intangible fixed assets | **7,354** | 3,872 |
| Cash outflow on investments in tangible and intangible fixed assets | **-33,635** | -41,153 |
| Cash inflow from the disposal of financial assets | **6,080** | 4,015 |
| Cash outflow on investments in financial assets | **-1,698** | -12,985 |
| **Cash flow from investment activities** | **-21,899** | -46,251 |
| Cash inflow (+)/outflow (-) as a result of sales and repurchases of own shares | **12** | 0 |
| Cash inflow (+)/outflow (-) as a result of the issue of bonds, take-up of loans and other financial liabilites | **-2,418** | -3,638 |
| Interests paid | **-3,072** | -3,531 |
| **Cash flow from financing activities** | **-5,478** | -7,169 |
| Cash and cash equivalents available at the beginning of the period | **884,897** | 245,871 |
| Change in cash and cash equivalents | **-140,573** | -30,220 |
| **Cash and cash equivalents available at the end of the period** | **744,324** | 215,651 |

# Statement of Changes in Equity

| in T€ | Subscribed capital | Capital reserve | Purchase/ Repurchase of own shares | Other retained earnings | Reserve from currency translation |
|---|---|---|---|---|---|
| **Status January 1, 2005** | **160,899** | **292,670** | **-9,453** | **990,236** | **-144,393** |
| Net income for the year | | | | | |
| Dividend | | | | | |
| Exercise of warrant-linked bonds | 307 | 1,145 | | | |
| Disposal of own shares | | | 1,556 | | |
| Currency translation | | | | | 1,969 |
| Change in value pursuant to IAS 39 | | | | | |
| Change in value from hedging transactions | | | | | |
| Group transfers to retained earnings | | | | 166,507 | |
| Deferred taxes on changes without effect on income | | | | | |
| Others | | | | 106 | |
| **Status March 31, 2005** | **161,206** | **293,815** | **-7,897** | **1,156,849** | **-142,424** |
| | | | | | |
| **Status December 31, 2005** | **161,615** | **295,343** | **-160,283** | **1,819,755** | **-19,571** |
| Net income for the year | | | | | |
| Disposal of own shares | | | 6 | | |
| Currency conversions | | | | | -1,265 |
| Change in value pursuant to IAS 39 | | | | | |
| Group transfers to retained earnings | | | | 26,946 | |
| Others | | | | -1,766 | |
| **Status March 31, 2006** | **161,615** | **295,343** | **-160,277** | **1,844,935** | **-20,836** |

## Statement of Changes in Equity

| Valuation reserve IAS 39 from hedging transactions | Valuation reserve IAS 39 from available for sale | Other equity changes without effect on income | Consolidated net income | Equity (excl. minority interests) | Minority interests | Equity |
|---|---|---|---|---|---|---|
| **-4,428** | **5,963** | **-74,536** | **26,400** | **1,243,358** | **11,819** | **1,255,177** |
| | | | 173,107 | 173,107 | 394 | 173,501 |
| | | | | 0 | -2,315 | -2,315 |
| | | | | 1,452 | | 1,452 |
| | | 7 | | 1,563 | | 1,563 |
| | | | | 1,969 | | 1,969 |
| | -2,210 | | | -2,210 | | -2,210 |
| 9,655 | | | | 9,655 | | 9,655 |
| | | | -166,507 | 0 | | 0 |
| | | -1,601 | | -1,601 | | -1,601 |
| | | 2,600 | | 2,706 | | 2,706 |
| **5,227** | **3,753** | **-73,530** | **33,000** | **1,429,999** | **9,898** | **1,439,897** |
| | | | | | | |
| **1,948** | **7,332** | **-168,243** | **64,500** | **2,002,396** | **9,232** | **2,011,628** |
| | | | 34,821 | 34,821 | 857 | 35,678 |
| | | 7 | | 13 | | 13 |
| | | | | -1,265 | | -1,265 |
| -4,812 | -2,933 | | | -7,745 | | -7,745 |
| | | | -26,946 | 0 | | 0 |
| | | 1,130 | | -636 | | -636 |
| **-2,864** | **4,399** | **-167,106** | **72,375** | **2,027,584** | **10,089** | **2,037,673** |

# Statement of Income and Accumulated Earnings

| in T€ | 1st Quarter 2006 | 1st Quarter 2005 |
|---|---|---|
| **Changes recorded directly under equity** | | |
| Changes resulting from currency translation | **-1,265** | 1,969 |
| Changes in the value of the reserve from hedging transactions | | |
| Changes in current value reported immediately in equity | **3,512** | 769 |
| Realization of settled hedging instruments with effect on income | **-6,376** | 8,886 |
| Changes in the value of financial assets in the available-for-sale assets category | | |
| Changes in current value reported immediately in equity | **-6,122** | -4,315 |
| Realization of settled hedging instruments with effect on income | **3,190** | 2,105 |
| Deferred taxes on changes without effect on income | **311** | -1,601 |
| Other changes without effect on income | **819** | 2,600 |
| | | |
| | **-5,931** | 10,413 |
| | | |
| **Consolidated net income for the year** | **35,678** | 173,501 |
| | | |
| **Total profit pursuant to IAS 1.97 in conjunction with IAS 19.93B** | **29,747** | 183,914 |
| | | |
| Total profit due to Salzgitter AG shareholders | **28,890** | 183,520 |
| Total profit due to minority interests | **857** | 394 |
| | **29,747** | 183,914 |

# Selected Notes to the Consolidated Financial Statements

**Principles of accounting and consolidation, balance sheet reporting and valuation methods**

1. The consolidated financial report of Salzgitter AG, Salzgitter, for the reporting period from January 1 to March 31, 2006, has been prepared as a condensed report with selected notes. The report has been drawn up as before in accordance with the International Reporting Standards (IFRS) published by the International Accounting Standards Board (IASB) in consideration of requirements contained in IAS 34 for condensed interim reports.

2. In comparison with the annual financial statements as at December 31, 2005, the following changes have been made in the accounting, valuation, calculation and consolidated methods in the interim financial statements for the period ended March 31, 2006:
   - The Eupec PipeCoatings S.A., Joeuf (France), which so far has been included proportionately (50 %), has been excluded from the group of consolidated companies. Mannesmann DMV Stainless, located in Mülheim an der Ruhr, has been included in the group of consolidated companies for the first time.
   - Since January 1, 2006, “Other taxes” are reported in the position “Other operating expenses”. Due to the marginal effect on the income statement, an adjustment of the reference period figures has been omitted.
   - Basis for the calculation of the Cash Flow Statement is no longer “Consolidated net income for the period” but “Profit on ordinary activities for the period”. Income taxes paid are reported separately.

**Selected explanatory notes on the income statement**

1. Sales by division are shown in the segment reporting section. In contrast to the quarterly financial statements as at March 31, 2005, in which the Group comprised the five divisions Steel, Trading, Services, Processing and Tubes, following the realignment of the Group the companies of the Processing Division were being reallocated to the Steel and Services Divisions. Furthermore, Salzgitter Großrohre GmbH was taken out of the Steel segment and reassigned to the Tubes segment. The figures for the first quarter of 2005 have been adjusted to take account of the new structure of the segments.

   Furthermore, Salzgitter Mannesmann GmbH (SMG) has been reclassified from the Tubes Division to ”Consolidation and others” and will be recorded together with Salzgitter AG in that segment. SMG has long-term contracts governing prematerial supplies to enterprises outside the group of consolidated companies. This explains the recording of sales in the position. Due to the marginal effect, an adjustment of the reference period figures has been omitted.

2. Earnings per share are calculated pursuant to IAS 33. The **undiluted earnings per share** based on the weighted number of shares of Salzgitter AG came to € 0.62 in the period under review.

   Dilution of the earnings per share occurs if the average number of shares is increased by the addition of the potential shares to be issued on the basis of the options and conversion rights. There were no such options and conversion rights outstanding as of March 31, 2006. Therefore, **diluted earnings per share** equaled undiluted earnings per share and amounted to € 0.62.

# Investor Relations

**The capital market and the performance of the Salzgitter stock**

In the first quarter of 2006, the upbeat trend in the **stock markets** held steady. Buoyed by the gradual improvement in the economic climate, which finally culminated in an official upward revising of expectations for the economy, the DAX climbed 10 % until the end of March, with temporary phases of consolidation. During the same period, the MDAX increased by 19 %.

After the turn of the year, the **Salzgitter share** continued to perform well, following on from the most gratifying trend already observed in 2005. The share benefited from the steady improvement in the market environment of the steel industry, as well as from the sustained price rally of the listed French tubes manufacturer Vallourec S.A. in which Salzgitter AG holds a stake of 17.2 %. Over the course of the first three months of 2006, the share price rose to a new all-time high of EUR 66.00 on March 27. Following the release of the Annual Report 2005 on March 30, 2006, there were temporary phases of profit taking. The share closed the first quarter at EUR 60.75. Based on a price at year-end 2005 of EUR 45.61, the quarterly performance came to 33 %, which again significantly outperformed the growth of the DAX and MDAX.

The average **daily turnover** of the Salzgitter share on German stock exchanges of around 472,000 units in the first quarter of 2006 reflects the persistently brisk interest shown by the capital market. As against the previous year's figure, average turnover rose by 52 %. The trading volumes achieved in the last 12 months and a **free float market capitalization** of EUR 2,523 million have resulted in Salzgitter AG taking place 8 and 9 in the respective categories of the MDAX ranking of Deutsche Börse AG, which means that its weighting in the MDAX has increased.

As part of its **capital market communication** activities, Salzgitter AG has made company presentations at an investor conference and at a road show in Frankfurt since the start of 2006. In addition, a number of investors and financial analysts visited the plants in Salzgitter and Mülheim. The results of the financial year 2005 were presented and commented on at the extremely well attended analyst conferences in Frankfurt and London, which took place after the annual report had been published at the end of March.

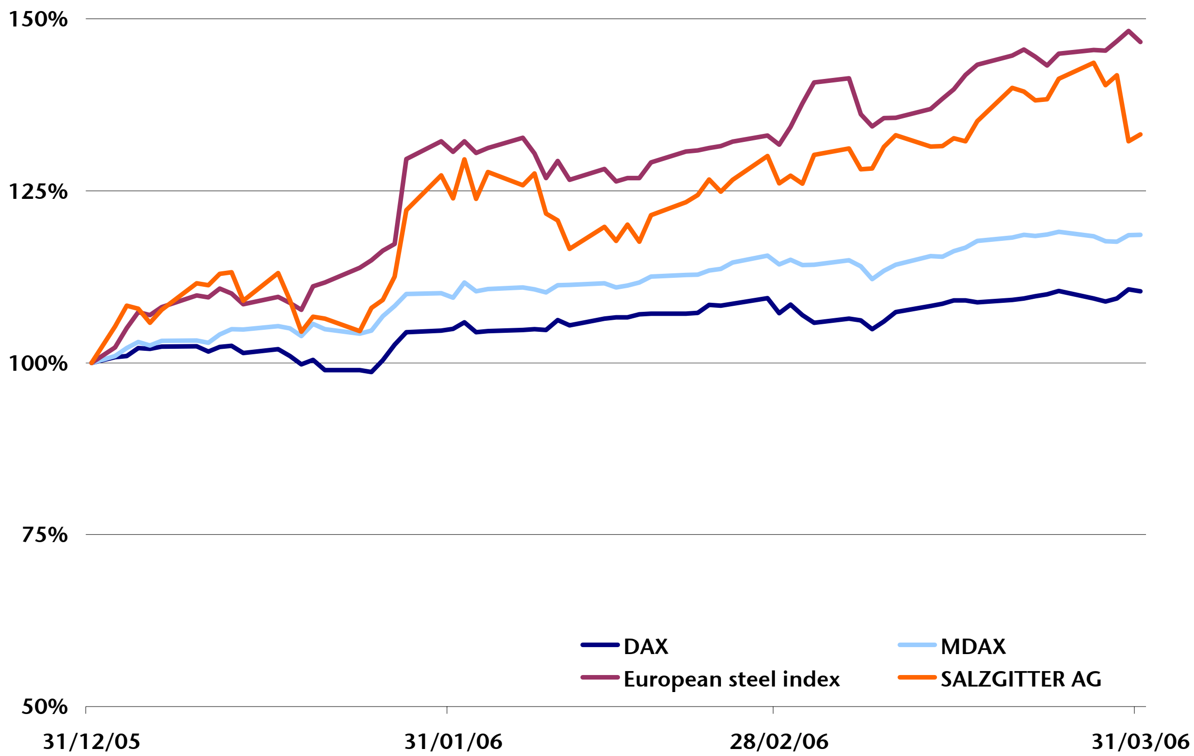
Since the start of the financial year, a total of 53 company reports and recommendations on the Salzgitter share have been published by 23 banks and financial publications with the following current **ratings** (status as per March 31, 2006): 12 buy/outperform, 6 hold/neutral, 5 sell/underperform.

**Information for investors**

| | | **Q1 2006** | Q1 2005 |
|---|---|---|---|
| Nominal capital as of 31/03 | € million | **161.6** | 161.2 |
| Number of shares as of 31/03 | million | **63.2** | 63.1 |
| Number of shares outstanding as of 31/03 | million | **56.9** | 62.1 |
| Market capitalization as of 31/03[1)2)] | € million | **3,456.5** | 1,022.4 |
| Price as of 31/03[1)] | € | **60.75** | 16.46 |
| High 01/01/ - 31/03/[1)] | € | **66.00** | 17.81 |
| Low 01/01/ - 31/03/[1)] | € | **45.21** | 14.17 |
| Security identification number | 620200 | | |
| ISIN | DE0006202005 | | |

[1)] All data based on prices from XETRA trading
[2)] Calculated on the basis of the respective closing price at the end of the quarter multiplied by the number of shares outstanding as of 31/03

**Performance of Salzgitter AG vs. European steel index, DAX and MDAX**




Sources: Xetra closing prices DBAG, Datastream STEELEU

### Treasury shares

As per March 31, 2006, Salzgitter AG held 6,321,297 own shares. In comparison with the status as per December 31, 2005, the number had decreased by 231. In line with the authorization given by General Meeting of Shareholders held on May 26, 2005, 225 shares at an average price of € 54.56 were used in lieu of payment for the services of third parties during the reporting period. 6 shares were issued to members of the workforce for free or as a bonus.

### Financial calendar

| | |
|---|---|
| June 08, 2006 | Ordinary Shareholders' Meeting |
| August 10, 2006 | Interim report for the first half 2006 |
| August 10, 2006 | Analyst conference in Frankfurt/Main |
| August 11, 2006 | Analyst conference in London |
| November 14, 2006 | Interim report for the first nine months 2006 |
| December 31, 2006 | End of financial year 2006 |

### Legal disclaimer

Some of the statements made in this report possess the character of forecasts or may be interpreted as such. They are made upon the best of information and belief and by their nature are subject to the proviso that no unforeseeable deterioration occurs in the economy or in the specific market situation pertaining to the Division companies, but rather that the underlying bases of plans and outlooks prove to be accurate as expected in terms of their scope and timing. The company undertakes no obligation to update any forward-looking statements. The official financial report for the period under review in this document is the German-language hardcopy version of the Salzgitter AG Interim Report. In case of ambiguity between this document and any other version of the interim report, information provided in the German-language hardcopy version shall supersede information provided in any other form.

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