

Dr Hartmut Mehdorn
Chairman of the Board

For the attention of

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20 October 2006

Dear Mr XX,

As discussed, please find below a few examples as to why DB needs additional capital resources if it is to remain a European champion in the transport market in the long run.

Since the railway reform, DB has extremely successfully continued to develop from a national railway authority into an internationally active mobility company. Simultaneously, it has fulfilled the duties of its shareholder arising out of the railway reform.

- DB has increased rail traffic. Passenger traffic has risen from 65.2 billion passenger-kilometres in 2004 to 78 billion in 2006; and rail freight volume has jumped from 70.6 billion tonne-kilometres in 1994 to 105 billion in 2006.
- Meanwhile, the profitability of the group as a whole and its productivity in the rail transport sector have considerably improved.
- No other country has a level of competition in the rail sector comparable to Germany's.
- At the same time, over the past few years DB has steadily expanded its international business.

Since DB is successfully streamlining its domestic business and has gained the necessary international expertise, it is very well placed to play an important role in rail markets opening up in Europe and in the booming markets of Asia and America.

However, owing to the imminent opening up of markets in the rail sector and strong trends towards consolidation in the transport and logistics market, if we are to continue resolutely pursuing our adopted strategy we will need substantial further investments on top of those we have already made or have firmly planned.

– By 2010 or 2011 at the latest, where commercial long-haul traffic is concerned, DB must expect SNCF to compete with it on lucrative routes in Germany. If DB is to counter this expected offensive and be in a position to exploit any opportunities arising from the opening up of markets for long-haul traffic from 2010, it must invest substantially in ICE trains that are suitable for deployment in France. An investment in 30 internationally deployable ICE trains would cost roughly €900 million.

– The rising volume of container traffic (the market for combined transport is currently enjoying double-digit growth every year) is upping the importance of hinterland transport of maritime containers in Germany. If rising volumes of freight are to be increasingly transported by rail, investments in marshalling yards and also, to a considerable degree, rolling stock, rail ports and depots will be required. An opening may also arise for business involving maritime terminals in northern ports. This would necessitate investments totalling €1.5-2 billion.

– From our Eastern European neighbours in particular, who frequently lack the funds they need to invest as well as appropriate know-how or critical mass, we are receiving more and more requests to take full control of integrated state-owned railways in return for guarantees to keep them operating in the long term. These offers are of great interest to DB because in this way its existing infrastructure and transport networks can be expanded and new, strategically important markets can be opened up. DB's integrated organisation is especially important here, since we constitute a potential one-stop-shop for anything from port terminal operation to hinterland transport of maritime containers or regional transport. These planned acquisitions will increase rail's importance in combined transport in Europe even further. To this end, corresponding investments of €1-3 billion will be required over the coming years.

– Together with the Russian railways, we are developing a Trans-Siberian land bridge between Asia and Europe. In so doing, we are constructing an alternative to intercontinental maritime transport. Our talks in China are underscoring the great economic and strategic importance of this project. Our share in the investment will be in the region of €1-2 billion.

– The freight forwarding and logistics market, which is enjoying annual growth rates of over 8%, is extremely fragmented and is currently in a major consolidation phase. The world's five largest logistics companies command a combined market share of less than 10%. DB, the second largest logistics operator, has a market share of just 2.3%. Considerable economies of scale in the logistics sector mean that size entails a tremendous competitive advantage. To remain competitive in this market in the long run and ensure that Germany remains a world leader in the logistics sector, acquisitions worth a total of approximately €2 billion are necessary.

– Finally, DB will have considerable opportunities for growth from some key calls for tender for urban traffic anticipated in major European cities like Prague, Lyon or Stockholm. Owing to DB's proven competence in operating major urban railways, DB has every prospect of winning some of these calls for tender. An investment in the region of €1-2 billion will be required here.

Although DB will probably not implement all these plans concurrently and will also be able to finance many investments out of the free cash flow it expects to have at its disposal over the years to come, a shortfall of some €2-3 billion remains, which would have to be covered by privatisation proceeds.

The investments described above, which would for the most part be realised in Germany, will not only help to make sure that DB becomes a European champion, but would also go some way towards safeguarding employment in Germany. An internationally strong DB creates quality jobs in the domestic market, and experience shows that companies with headquarters in Germany assume a higher degree of responsibility for jobs and investments at home. Jobs and tax revenues from the supply industry also depend directly on the choice of location.

Please don't hesitate to contact me if you have any further queries or require any additional information.

Best regards,

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