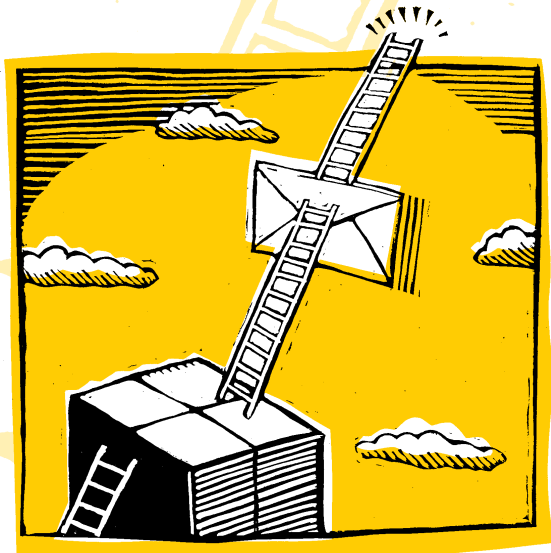


Annual Report 1997



C O R P O R A T E P R O F I L E

Deutsche Post AG is a diversified international service provider in the communications, transport and logistics markets.

As the largest postal services provider in Europe, we offer commercial as well as private customers a broad spectrum of high-quality services that range from the traditional delivery of letters and parcels to electronic mail, all the way to an integrated, custom-tailored offering of complete logistics solutions.

In optimizing its core business, Deutsche Post employs state-of-the-art technology. Our goal is to increase continually our corporate value and – in the interest of all involved – generate high value added. Within the scope of the “Infrastrukturauftrag” (infrastructure services mandate) by the state, Deutsche Post provides postal services at adequate prices throughout the entire country.

Our most important corporate goals are:

- to reinforce our market leadership in domestic postal services;
- to open foreign markets for postal services, particularly in Europe;
- to maintain market leadership in service quality, also as measured against international standards.

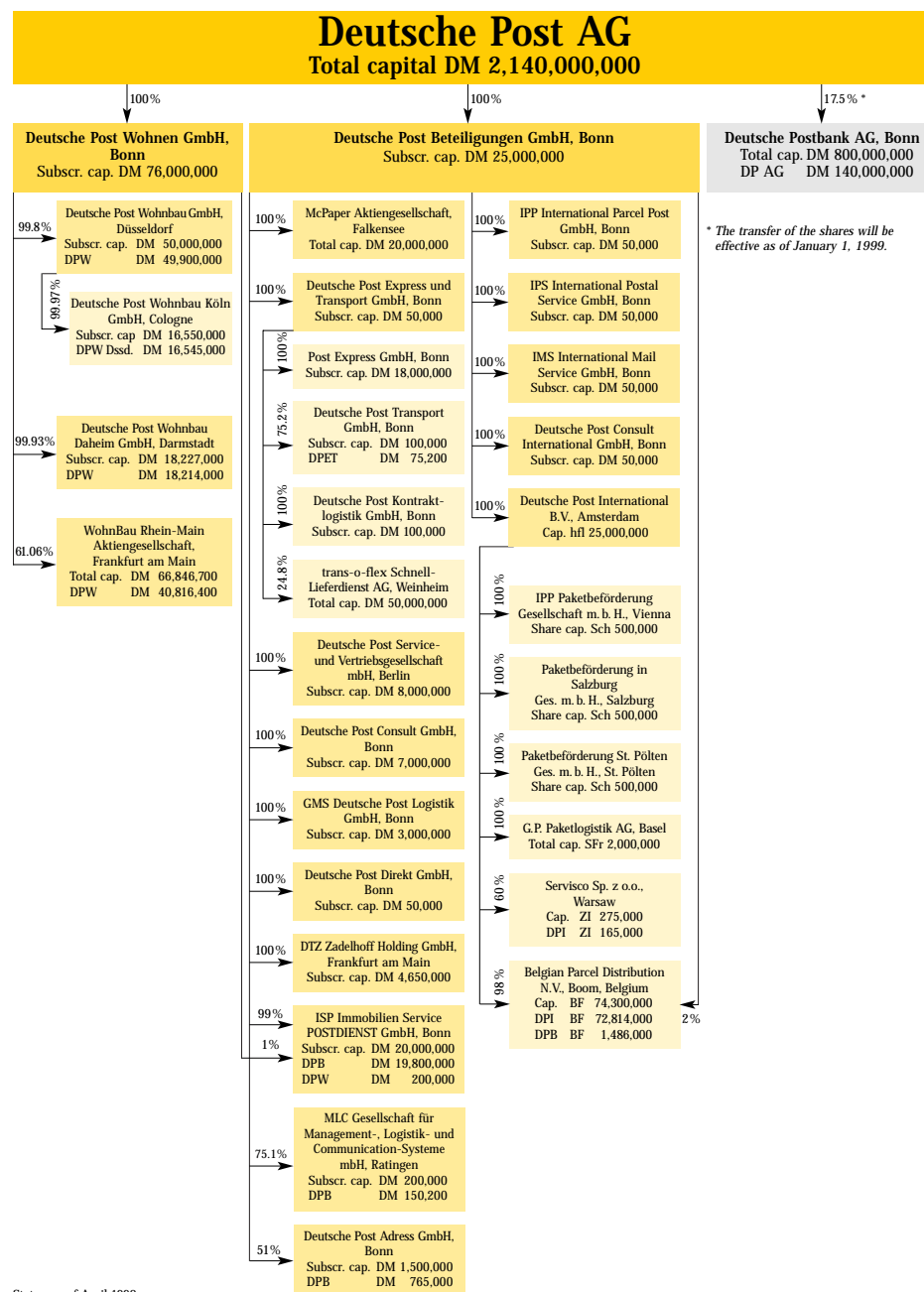
FINANCIAL HIGHLIGHTS

Deutsche Post AG	1996	1997	
Net revenue	(DM millions) 26,702	27,136	+1.6 %
Profit on ordinary activities	(DM millions) 576	752	+30.6 %
Cash flow according to DVFA/SG formula	(DM millions) 1,921	2,244	+16.8 %
Unappropriated retained earnings/accumulated loss (-)	(DM millions) -617	103	
Balance sheet total	(DM millions) 19,370	21,346	+10.2 %
Shareholders' equity	(DM millions) 5,195	5,687	+9.5 %
Capital expenditures in property, plant and equipment	(DM millions) 1,879	1,929	+2.7 %
Depreciation of property, plant and equipment	(DM millions) 1,426	1,469	+3.0 %
Equity ratio (%)	26.8	26.6	-0.2 %
Return on equity* (%)	6.5	9.3	+2.8 %
Number of employees** as of December 31	284,889	266,823	-6.3 %
Personnel expenses as % of total	68.4	68.2	-0.2 %

* Income from ordinary business activities, minus other taxes

** Including trainees

Principal Subsidiaries and Associated Companies



1

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** Including trainees

Foreword by the Chairman of the Board of Management

1997 was a successful and eventful year for Deutsche Post.

With profit on ordinary activities growing to DM 752 million – an increase of 30 percent over the previous year – we continued to improve both performance as well as financial results.



*Dr. Klaus Zumwinkel,
Chairman of the
Management Board
Deutsche Post AG*

Signposts

The year was marked by a number of events that will have a definite impact on the image of Deutsche Post in coming years.

In early summer, Deutsche Post and Postbank signed a cooperation agreement ensuring, for the long-term, a high and predictable utilization of the Deutsche Post's branch network.

In December, the new Postal Act was finally passed, giving Deutsche Post and all its competitors the regulatory certainty necessary for shaping a modern and internationally competitive postal sector in Germany. That act makes Germany a pace-setter in the liberalization of Europe's postal markets. The burden that results from Deutsche Post's "Infrastrukturauftrag" (infrastructure service mandate) is balanced by price and product flexibility granted us for a five-year transition period.

Our divisions

In 1997, we continued to make good progress toward achieving leadership in postal service quality in both Germany and Europe. Today, 93 percent of all letters mailed within Germany reach their destination the next day: 99 percent are received within two days. This translates into an average delivery time of 1.1 days – one of the best in Europe.

These improvements were possible primarily by adding more letter processing centers. By the end of 1998, all 83 of our planned letter processing centers will be operational, enabling us to deliver the mail even faster with still greater reliability.

Quality of services and focus on customer needs are top priorities in our Freight Mail division. The opening of 33 new, strategically located freight processing centers has had an enormous impact: our transport network was streamlined, the number of transport tours was reduced and sorting processes were extensively automated. Today, the average time for a parcel from posting to delivery is only 1.2 days. In 1997, for the first time in years, Deutsche Post was able to increase sales and accomplish a turnaround in revenue performance. Our Freight Mail division is targeted to be profitable by the year 2000 – despite the “burden of the past”, carried over from the days of the former Bundespost, a burden which our competition does not have to bear.

In 1997, a large part of the DM 1.9 billion capital expenditures in property, plant and equipment was applied to set up letter processing centers. In coming years, the capital expenditures will be even larger in establishing a modern, customer-oriented postal network at attractive locations. Having completed most of the corporate restructuring and reorganization which began in 1990, we can now concentrate on our growth strategy.

Because we offer our customers more than just plain transport services, Deutsche Post is already successful in the highly competitive logistics and communications markets. In 1997, we added new services to our traditional value-added chain of products – Acceptance, Transportation, Sorting and Delivery. As solutions provider we offer our customers innovative services, custom-made programs of cooperation and new logistics products. ePost, to cite one example, mailed 83.5 million letters last year – nearly three times the number in 1996.

Systematic orientation toward the customer

Current and anticipated future customer needs are guiding us in our efforts to develop and refine our services offering. In respect to Deutsche Post's strategic positioning, internationalization is given highest priority. In 1997 we significantly expanded our business in Europe. We installed our own parcel transport operations in the business-to-business segment through acquisitions in Belgium, Poland and Switzerland and through installing our own operation in Austria. By expanding our physical network – through acquisition, participations and cooperation agreements – we aim to become market leader in the European parcel mail market.

Along with the ongoing improvement in our service quality and the expansion of our product range, we improved our cost structures, particularly for personnel. By the end of 1997, mostly through attrition and normal job turnover, we had reduced staff level by some 18,000 to about 267,000.

IPO in sight

Our strategic objectives are to increase Deutsche Post's competitive strength, to secure a strong position in the global logistics market and to maximize the value of the corporation, especially in view of the IPO planned for the year 2000. In the pursuit of these objectives and for mastering tasks and challenges ahead, we rely on the support and trust of our customers. Our thanks for the exceptional result achieved in 1997 go above all to our employees who performed their task with great dedication and made a vital contribution to the success of our corporation.

The Board of Management



MEMBERS OF THE BOARD OF MANAGEMENT

Dr. Helmut Benno Staab
Marketing and Sales of Letter Services,
“Pressepost”, Postal Philately

Dr. Günter W. Tumm
Express Courier Parcel Services, International Post

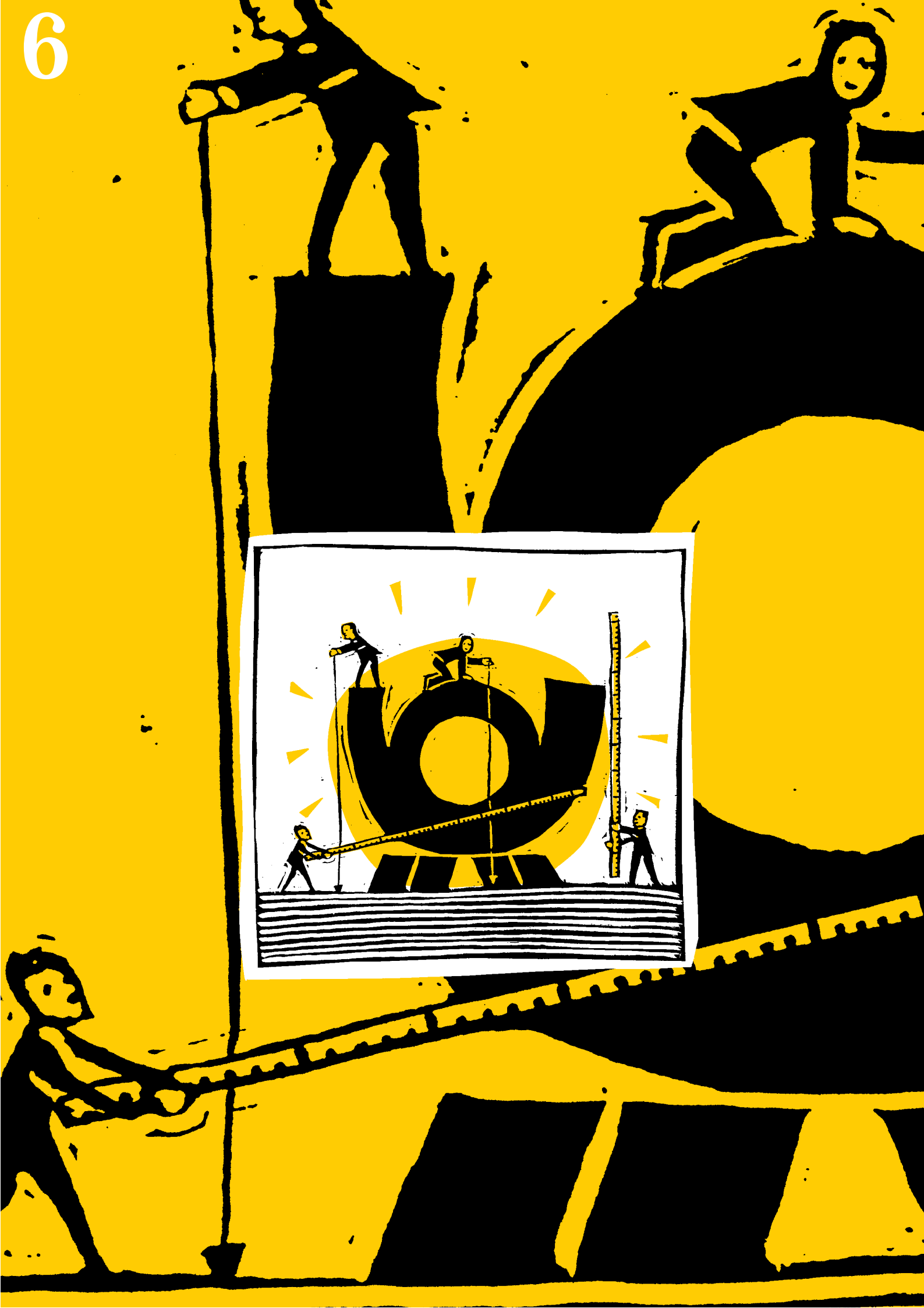
Dr. Klaus Zumwinkel
Chairman of the Management Board

Wolfhard Bender
Production of Letter Services, Legal Affairs

Dr. Hans-Dieter Petram
Postal Branches, Real Estate Property,
Purchasing

Horst Kissel
Personnel

Dr. Edgar Ernst
Finance



Management Report

*Deutsche Post in 1997:
improved results, progress
toward long-term goals*

Growing competition in non-restricted business segments and stagnating sales in sectors with intensive needs for postal services, such as the mail-order industry, put a strain on business environment for Deutsche Post during 1997. In spite of this, we were able to increase net revenue and improve our results once again. Profit on ordinary activities, positive since 1994, rose for the third year in a row. As a result, we have made good progress toward achieving our goal of generating an adequate return.

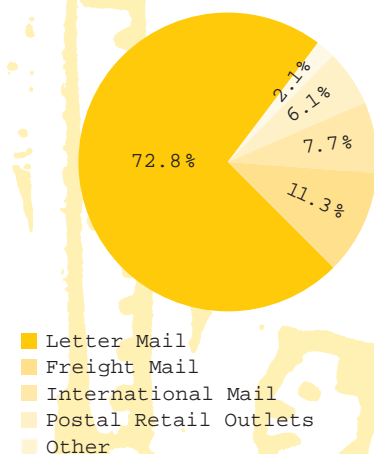
Business volume continues to grow

Net revenue rose by DM 434 million to DM 27,136 million.

As in past years, our Letter Mail division continued to generate the largest share of total revenue. Revenue rose by 2.9 percent to DM 19,757 million. Despite growing competition from electronic communications, the Letter Mail segment booked DM 13,630 million in revenue for the year, a gratifying 2.2 percent increase. The fast-growing segment "Infopost" (printed matter and direct mail) recorded above-average growth once again in 1997 with revenue rising by 5.5 percent to DM 4,635 million. Revenue in the "Pressepost" (periodicals and newspapers shipped at reduced rates) segment grew by 0.7 percent to DM 1,492 million.

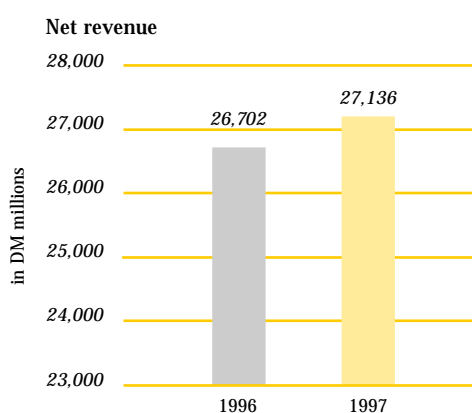
We managed to stabilize revenue in the Freight Mail division by keeping prices unchanged. Business generated by new customers was an important factor in this accomplishment. However, we expect revenue – for us at an unsatisfactory level – to improve as consumer demand picks up again. The International Post division also reported stagnating revenue as a result of pricing pressure and declining volume of mail from private customers.

Breakdown of total turnover
by division

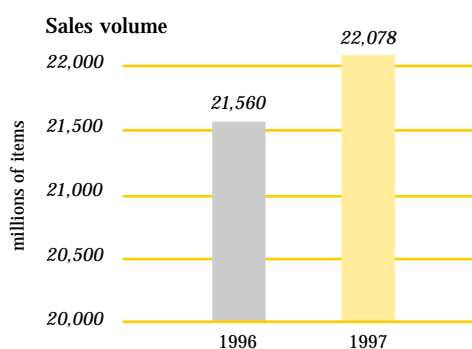


**Net revenue according to division
in DM millions**

	1996	1997	+/-	
<i>Letter Mail</i>	19,210	19,757	547	2.9%
<i>Freight Mail</i>	3,088	3,065	-23	-0.7%
<i>International Post</i>	2,081	2,079	-2	-0.1%
<i>Postal Branches</i>	1,743	1,660	-83	-4.8%
<i>Other</i>	580	575	-5	-0.9%
Total revenue	26,702	27,136	434	1.6%



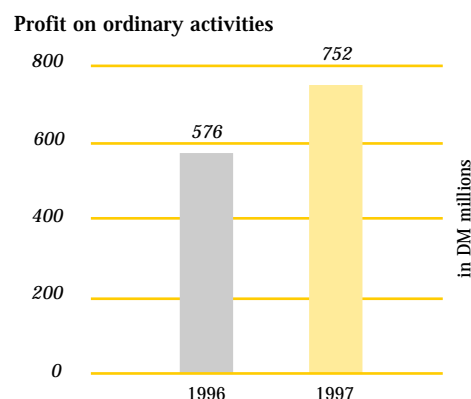
Sales volume also varied by division and within divisions. Total shipment volume, including transactions conducted by postal branches, grew by 2.4 percent to 22,078 million items. As in past years, the Letter Mail division, with a 2.4 percent volume increase, again made an above-average contribution. The fastest growth within this division – namely 5.4 percent – was achieved by the “Infopost” segment. Sales volume reported by Freight Mail, International Post and Postal Branches remained stable at the respective previous year’s level.



Marked increase in profit

Profit on ordinary activities rose by a strong 30.6 percent to DM 752 million during 1997, compared to DM 576 million in 1996. Increased revenue as well as cost-cutting measures contributed to this significant rise in profits. The main contributing factor on the expense side was personnel cost (wages, salaries and other emoluments) which over fiscal 1996 fell significantly by DM 915 million to DM 12,187 million for the year. Other operating expenses also decreased, namely by DM 707 million to DM 3,387 million.

Pension expenses, including social security contributions and other benefits, rose by DM 584 million to DM 7,435 million, primarily due to a DM 621 million provision for indirect pension obligation. In addition, we accrued DM 1,789 million for extraordinary expenses for indirect pension obligations – previously listed in the Notes. Indirect pension commitments, which are made to employees of Deutsche Post through the VAP (Versorgungsanstalt der Deutschen Bundespost) and the DPBS (Deutsche Post Betriebsrenten-Service e.V.) and which are not yet accrued, amounted to DM 5,010 million as of December 31, 1997.



Selected expense items in DM millions	1996	1997	+/-	
Cost of materials	3,262	3,637	375	11.5
Personnel expenses	19,953	19,622	-331	-1.7
Wages, salaries and other emoluments	13,102	12,187	-915	-7.0
Social security contributions, pension expenses and other benefits	6,852	7,435	584	8.5
Other operating expenses	4,094	3,387	-707	17.388

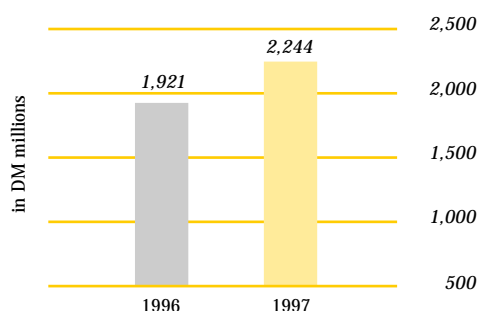
The extraordinary expenses were partly offset by the sale of shares in the Gemeinnützige Deutsche Wohnungsbaugesellschaft mbH which generated DM 876 million in proceeds and reduced the extraordinary loss to DM 913 million.

In fiscal 1997, the corporation reported for the first time positive retained earnings of DM 103 million.

Enhanced financial strength

The company's financials continued to improve according to plan. Cash flow according to DVFA/SG formula increased by 16.8 percent to DM 2,244 million (1996: DM 1,921 million), that is, 8.3 percent of total revenue.

Net cash flow according to DVFA/SG formula



Net cash used for investing activities fell by DM 181 million to DM 311 million during 1997. This was mainly due to an above-average increase in proceeds from the sale of fixed assets totaling DM 1,715 million for the year, DM 213 million more than in fiscal 1996. Capital expenditures could, in turn, be completely funded by net cash provided by operating activities. The decrease by DM 753 million to DM 1,093 million in net cash provided by operating activities during fiscal 1997 was primarily due to an increase in receivables from the Deutsche Post Pensions-Service e.V., which the Federal Government must settle.

Statement of cash flows (selected items)
in DM millions

	1996	1997	+/-
Cash flow according to DVFA/SG formula	1,921	2,244	323
Net cash provided by operating activities	1,846	1,093	-753
Net cash used for investing activities	-493	-311	181
Net cash used for financing activities	-1,318	-657	661
Cash and cash equivalents	1,982	2,107	125

The DM 657 million in net cash used for financing activities pertains mainly to the repayment of debts.

Due to the favorable cash inflow we were able to further strengthen our financial position as planned. Cash and cash equivalents increased by DM 125 million to DM 2,107 million. Our net funding position has continually improved since January 1, 1995, when Postreform II (second reform of German posts and telecommunications) went into effect.

This solid financial strength will enable us to finance further corporate growth using primarily our own resources.

Strengthened capital structure

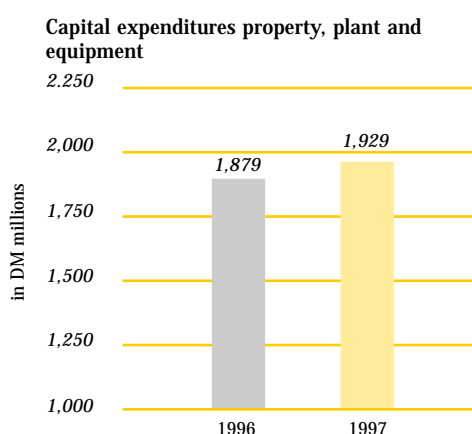
Deutsche Post's balance sheet total rose by 10.2 percent to DM 21,346 million in 1997. A major reason for this increase was the DM 2,410 million accrual of indirect pension obligations vis-à-vis our employees.

The increase in shareholders' equity with corresponding increase in assets raised the balance sheet total. In connection with the signing of our cooperation agreement with Postbank, Deutsche Post's annual shareholders' meeting voted on July 10, 1997, to increase share capital by DM 140 million. The Federal Government subscribed the new shares, paying for the investment by assuming the obligation to transfer 2.8 million Deutsche Postbank AG shares with a nominal value of DM 50 per share to Deutsche Post AG on January 1, 1999. The number of shares constitutes a 17.5 percent stake in Postbank. The difference between the amount of increase in share capital and the valuation of the shares the Government is to transfer to Deutsche Post was allocated to capital reserves.

Selected balance sheet items in DM millions	1996	1997	+/-	
Balance sheet total	19,370	21,346	10.2	1,976
Shareholders' equity	5,195	5,687	9.5	492
of which subscribed capital	2,000	2,140	7.0	140
Accruals	8,864	10,836	22.2	1,972
of which for pensions and similar obligations	1,072	3,434	220.3	2,362
Payables	5,311	4,823	-9.2	-488
of which to banks	772	506	-34.4	-266
of which to Telekom AG	1,430	1,038	-27.5	-392
Equity ratio	26.8%	26.6%		

At 26.6 percent, our equity ratio remained virtually unchanged from the previous year's level.

We slashed the amounts owed to banks by a substantial 34.4 percent to DM 506 million during 1997. We were also able to reduce debt owed to Deutsche Telekom AG listed under other liabilities by DM 392 million to DM 1,038 million. This item involves the allocation of debt of the former Deutsche Bundespost per Postreform II.



Large capital expenditures accelerate structural change

We also continued our planned multi-year investment program during fiscal 1997. Additions to property, plant and equipment amounting to DM 1,929 million (1996: DM 1,879 million) were financed entirely from internally generated cash flow.

As in 1996, investment activity continued to focus on establishing new production facilities for the Letter Mail business. The number of state-of-the-art letter processing centers grew from 20 to 58 in 1997. This project envisages a total of 83 centers and will be completed ahead of schedule in late 1998.

As part of our efforts to increase the international orientation of our corporation, we have successfully concluded several acquisitions during the financial year.

Deutsche Post Express und Transport GmbH (Bonn) has acquired a 24.8 percent stake in trans-o-flex Schnell-Lieferdienst AG (Weinheim) through a holding company. Along with our participation in the pan-European Eurodis Network, the trans-o-flex acquisition, with its subsidiaries in six countries, helps form a top-quality network that will ensure better service for Deutsche Post customers, particularly in the European region.

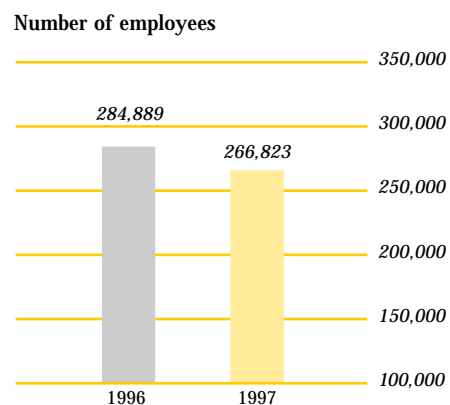
We acquired a majority share of Belgian Parcel Distribution N.V. (Boom). In addition, Deutsche Post AG is also the majority shareholder in Servisco Sp. z o.o. (Warsaw), the leading parcel delivery service in Poland. We also succeeded in acquiring full ownership of Switzerland's G.P. Paketlogistik AG (Basel).

In the European freight market, we will continue systematically to pursue our goal of offering top-quality service that invites international comparison. As in the past, we will also be examining potential options in the form of participations, cooperation agreements and the establishment of our own facilities.

In Germany, we acquired TNT Netzwerk Logistik GmbH in Troisdorf, which was renamed Deutsche Post Transport GmbH, and we increased to 100 percent our holding in DTZ Zadelhoff Holding GmbH in Frankfurt am Main.

Reduced staff levels

As of December 31, 1997, Deutsche Post had a total of 266,823 employees (including trainees). This figure is 6.3 percent lower than that at the end of 1996 – a reduction of 18,066 employees. This necessary staffing reduction occurred primarily through attrition and thus did not violate Germany's unwritten social contract. We also negotiated collective agreements with labor that enable us to adjust our personnel costs to stay competitive. In the coming years, we will have to continue to reduce our staff in order to raise productivity.



Customer focus and a policy of “consistent quality”

Our systematic quality campaign continued across all areas during 1997. The recent records set for letter, freight and international mail delivery times were exceeded again in 1997. According to studies conducted by an external institute, our letter mail service was able to deliver 92.9 percent of all letters the day after dispatch; 99.1 percent of all letters reached their destination within two days of dispatch.

Quality management throughout the Deutsche Post is based on an integrated concept of quality and the methodological evaluation procedures used by the European Foundation for Quality Management (EFQM). The paramount guideline for all our divisions and business segments is a rigorous customer orientation; this has consistently led to quality gains along the entire interface between Deutsche Post and its customers.

Continued optimization and innovation

In 1997, we were able to further extend the range of our services and to improve our production structures in all corporate areas. Productivity was greatly increased once again. Our focus on innovation generated a number of successful new products and new business segments.

New letter processing centers continue to go operational (all 83 will be in operation by the end of 1998), enabling us to deliver letter mail even faster, more reliably and at lower cost than ever before. In addition, our mail delivery network was optimized even further in 1997 with the opening of Direct Marketing Centers; 29 of the 30 centers planned were already doing business by the end of the year. Thanks to these facilities, we won many new customers for our “Werbung per Post” (advertising by mail) service. One example of new services offered is our chocolate gift service, Praliné Post, which has been well received since its launching nationwide in late 1997.

The traditional personal letter continues to be popular and is expected to remain so even in the age of electronic media. People still like to write letters, and our LetterNet club seeks to reinforce this by arranging pen pals. The response to date has been positive.

Early 1997 saw the creation of the new Courier Express Parcel and International Post (KEP/I) division. Its mission is to coordinate Freight Mail, Express Mail and International Post. So far KEP/I has already made enormous progress. Service quality has risen throughout the Freight Mail division. In 1997, the average delivery time of a parcel within Germany was 1.2 days. Thanks to our new Internet service, business customers can now “track and trace” their parcels and retrieve information for their inventory control systems. Costs were reduced even further as a result of our redrawing the areas serviced by our respective post offices. Facing changing market needs, our entire production process was reorganized to take advantage of the latest state-of-the-art information technology. The reorganization of sales activities in the Freight Mail division – and the consequent enhancement of those activities – have also produced positive results. The numerous product innovations that were introduced successfully in the market last year include our “Free Way” (a kind of postage stamp for parcels) and “Post Box” products (reusable mailing boxes).

In the express mail sector (the former EMS Kurierpost company was renamed Post Express GmbH) we developed a completely new product and production concept. When the plan was launched on January 1, 1998, Post Express replaced Deutsche Post’s postal express delivery service with a modern express parcel product. Its goal: to achieve market leadership in the express and courier services field.

With the opening in the autumn of 1997 of the International Postal Center (IPZ) in Frankfurt am Main, Deutsche Post has reorganized the entire international letter and freight mail process (with the exception of surface freight mail and mail by sea). As a result, costs have since been substantially reduced and international delivery times shortened. Furthermore, important decisions regarding cooperation agreements, alliances and participations were taken in 1997 with the aim of expanding activities on the European parcel and express mail markets. Our acquisitions in Belgium, Poland and Switzerland and the establishment of our own parcel mail operations in Austria have already produced positive results in the marketplace.

Our Postal Branches division is making good progress in implementing its new network and sales concept. Successful new retail outlet concepts ("Center" branches, Shop-in-Shop branches, "PostPlus" stores and further expansion of the postal agency network) in conjunction with an employee training program, provide the foundation for attractive new products and greater customer service. As a result, our postal branch network is positioned superbly for sustained excellence in performance and ability to compete.

Close collaboration with Postbank and its partners, in particular Wüstenrot, a savings and loan association, and HDI, an insurance company, has led to the introduction of an entirely new range of products in our financing service offering. A nationwide sales campaign was kicked off by Postbank in the autumn of 1997.

Looking to the future

While sales and revenue goals are being met according to plan in 1997, Deutsche Post continues to streamline and modernize its operations and organization. Future optimization measures to be implemented in all areas will lead to further productivity gains and enhanced service for our customers.

The acquisition of a 22.5 percent stake in DHL International Ltd., the global market leader for international express courier services, planned for March 1998 marks a significant increase in the international activities of Deutsche Post.

New retail branch concepts were tested in cooperation with McPaper AG, a stationery chain. Due to the success of these tests, Deutsche Post acquired McPaper from Herlitz AG; the acquisition is retroactive as of January 1, 1998.

As an integral part of the fast-growing communications, transport and logistics sectors the postal services market will become increasingly attractive in the coming years. Deutsche Post will make even greater efforts to meet current and future customer needs with integrated solutions. In pursuit of this objective Deutsche Post can rely on the various subsidiaries such as Deutsche Post Direkt GmbH (direct marketing services) or Deutsche Post Kontraktlogistik GmbH (development and implementation of logistic strategies) to work closely together with and pool resources and expertise with the divisions of the holding company.

The new Postal Act that went into effect on January 1, 1998, lays down the regulatory framework within which Deutsche Post can operate in the future. A product of the political process, the Postal Act is a compromise solution offering a rational and sensible base for ensuring Deutsche Post's competitive strength and corporate value in the future. With the passing of the act, Deutsche Post is now in the situation to embark on a forward-looking corporate strategy without the regulatory uncertainties of the past.

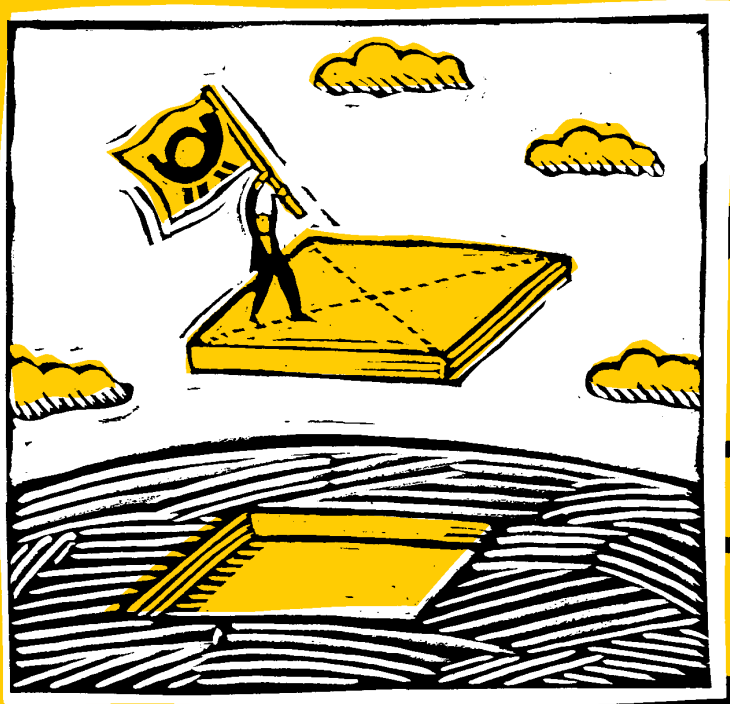
The continued liberalization of the postal services market as stipulated by the Postal Act clearly presents a challenge which Deutsche Post is prepared to meet head-on. In this market Deutsche Post will bring to bear its distinct strength in current services offering, its ability to develop innovative services, its strong position and its ability to compete. We are determined to seize the new business opportunities and, in particular, to put special emphasis on securing and expanding our strong position with large corporate and institutional companies.

The foundations for a long-term and sustainable growth strategy have been laid in all divisions and business segments. In addition, further activities in several directions have been initiated to strengthen corporate growth: internationalization, express services and value-added services, currently the key areas of the corporate growth strategy, have already shown encouraging success. In addition to expanding these key areas in-house, management continues to pursue an expansion strategy through acquisition of qualified and highly competitive logistics companies.

The Board of Management's Report on Relations with Affiliated Companies ("Dependency Report"), closing statement

The Board of Management closed the above report with the following statement:

None of the transactions entered into in 1997 and described in this report were prejudicial to the Company's interests. In each transaction the Company received fair and reasonable consideration. No transactions were entered into with third parties at the request of the Federal Government or in the interests of the Federal Government or its affiliated companies. Deutsche Post AG neither took, nor omitted to take, any measures in 1997 at the request or in the interests of the Federal Government or its affiliated companies.



Milestones 1997

KEP/I restructured

Reorganization of the Courier Express Parcel and International Post (KEP/I) division is complete. Its product focus: integrated logistics solutions Europe-wide. Deutsche Post aims to increase its market leadership by expanding its presence throughout Europe.

Investment in Postbank

The ruling government coalition stipulates the conditions for cooperation between Deutsche Post and Deutsche Postbank which allows Deutsche Post to purchase a 17.5 percent interest in Postbank.

Acquisition in Poland and Belgium

Deutsche Post acquires controlling interests in market leader Servisco in Poland and in Belgian Parcel Distribution. This is the first step toward establishing its own European logistics network in the business-to-business market segment.

DP Kontraktlogistik launched

Deutsche Post Kontraktlogistik GmbH is founded. Its product offering to the industrial and services sectors covers the entire value-added chain of logistics products.

January

February

March

April

22

1997

Milestones

Postbank agreement signed

Deutsche Post takes a major step toward ensuring higher utilization for its retail branch network by signing a cooperation agreement with Postbank.

New letter processing centers

Thirteen new letter processing centers are opened which brings the total number of these state-of-the-art centers to 45 and contributes to further quality and cost improvement.

Opening of new Direct Marketing Centers

Another 15 Direct Marketing Centers open their doors to the public. Deutsche Post's direct marketing services are particularly popular among small and medium-sized businesses.

Reorganization of the international business

To strengthen its position in the global market International Post, Deutsche Post's international operations, establishes three subsidiaries – International Parcel Post GmbH (IPP), International Mail Service GmbH (IMS) and International Postal Service GmbH (IPS).

Acquisition of TNT NetLog

Deutsche Post acquires TNT NetLog (TNT Netzwerk Logistik GmbH) and transfers it to Deutsche Post Transport GmbH. Its mission is to operate the long-distance traffic between Deutsche Post's freight processing centers.

Deutsche Post Express und Transport GmbH founded

Deutsche Post Express und Transport GmbH is established as a holding company on July 1. Its operations revolve around future-oriented courier, express-mail and postal services.

Equity stake taken in trans-o-flex

Deutsche Post acquires a 24.8 percent stake in trans-o-flex Schnell-Lieferdienst AG which becomes part of the Deutsche Post Express und Transport GmbH holding company.

Market launch in Austria

International Parcel Post (IPP) completes its parcel mail network in Austria. Operations begin with partners on a franchise basis.

"PostPlus" stores

The concept of offering convenience articles and postal products under one roof proves to be a success. Another 19 "PostPlus" stores are opened on July 1.

Fewer branches – more agencies

In the first eight months of the year, Deutsche Post closes 1,190 of its branches and opens 287 agencies – milestones for a better utilization of its retail branch network and for substantial cost savings.

May

June

July

August

Wüstenrot, a new partner of Postbank

The Wüstenrot savings and loan association becomes a Postbank product partner. Deutsche Post's cooperation with Postbank is another step to ensure full utilization of its retail branch network.

IPZ into operation

After 24 months of construction and trial operation, the International Postal Center (IPZ) at Frankfurt airport goes into operation. IPZ, the main hub of Deutsche Post's international operations, is the platform for quick and reliable cross-border delivery.

Deutsche Post and Postbank meet the press

Dr. Dieter Boening, Chairman of the Board at Deutsche Postbank AG, and Dr. Klaus Zumwinkel, Chairman of the Board of Management of Deutsche Post, meet with journalists to discuss the two companies' common future. One highly visible sign of this shared future is the launch of a joint advertising campaign aimed at stimulating new business for Postbank products throughout Deutsche Post's branch network.

Cooperation with McPaper

Market research confirms that customers prefer more opportunities for one-stop shopping. In response to the demand, Deutsche Post offers postal services in selected shops of the McPaper stationery store chain.

Still more letter processing centers

The opening of another 13 letter processing centers increases their total number to 58. Today, nearly all of Germany's metropolitan areas are serviced by new state-of-the-art production facilities.

Launch of Deutsche Post Express

Deutsche Post Express begins operations with a new product range geared to customer needs. The new company has set its sight on gaining market leadership in the growing market for courier and express-mail services.

HDI becomes a Postbank partner

Postbank gains another product partner in the universal financial services field – the HDI insurance company. This partnership marks yet another important step in ensuring full utilization of Deutsche Post's branch network.

The Postal Act

The new Postal Act is passed on December 22, 1997. It introduces competition in two stages and moves Germany into a front-runner position in the liberalization of Europe's postal markets.

Acquisition in Switzerland

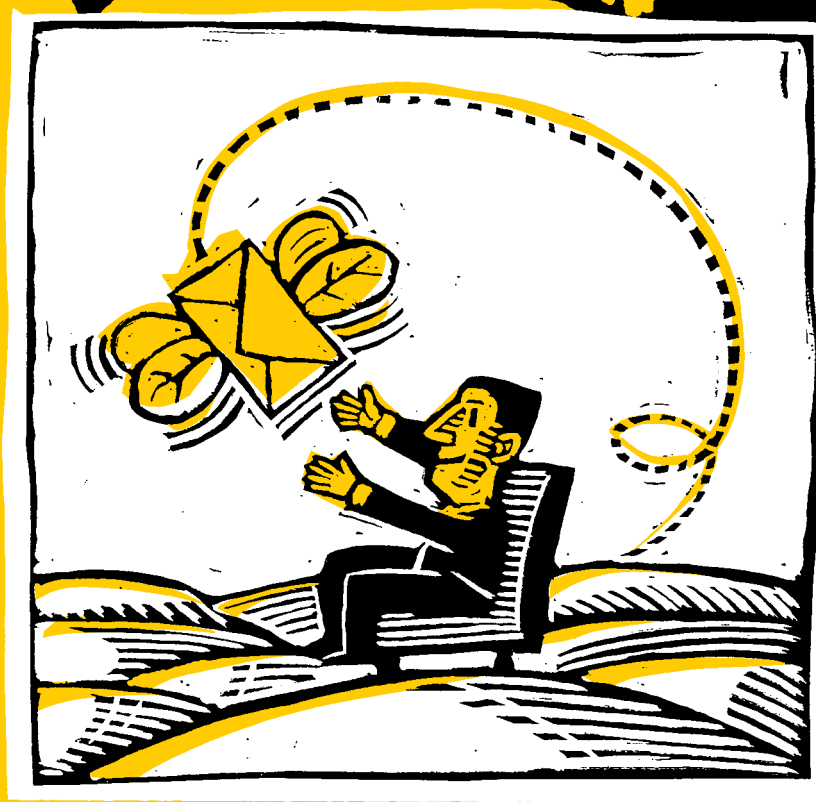
Taking another step toward establishing its own logistics network in Europe, International Parcel Post acquires the Swiss GP Paketlogistik.

September

October

November

December



Review of Operations

The Letter Mail division continues to generate the highest revenue for Deutsche Post.

Virtually everyone can be reached by letter, which no other means of communication can boast. Our high level of competence is evidenced by the development and refinement of successful products and by the shortening of delivery times.

LETTER MAIL

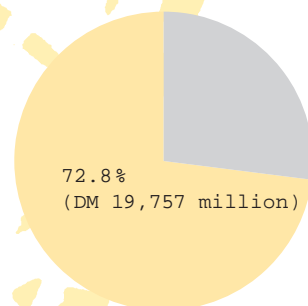
Standing firm in the face of new-media competition

Despite the growing competition from electronic media, the number of letters we processed in Germany has risen by some 25 percent since 1991 to 20 billion letters delivered in 1997 – an increase of 467 million items or 2.4 percent over 1996. This positive performance was due in large part to “Infopost”, which reported a 5.4 percent rise in sales. The number of standard letters also increased by 0.5 percent. As for the handling of “Pressepost”, a slight volume decrease of 1.4 percent occurred, primarily as a result of the downward trend in the magazine market segment.

Revenue in the Letter Mail division rose by DM 547 million – 2.9 percent – during 1997. Generating DM 19,757 million in revenue, the division accounted for some 73 percent of total corporate revenue. As in past years, the “Infopost” business was once again the top performer, with revenue growing by 5.5 percent to DM 4,635 million. The letter business gained 2.2 percent, generating DM 13,630 million in revenue. Despite a slight decline in sales volume, “Pressepost” was able to book a 0.7 percent increase in revenue over 1996.

To ensure a strong future for letter mail business, the two-pronged strategy put in place some years ago was continued in 1997. First, the strategy aims to maintain and to increase a high standard of service

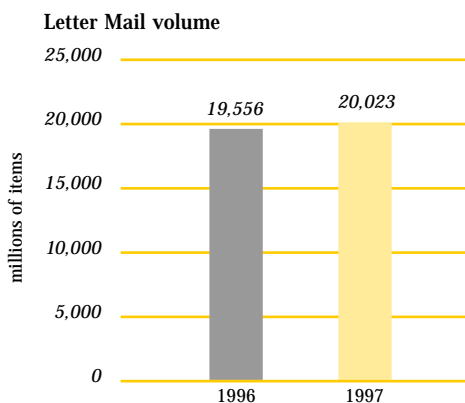
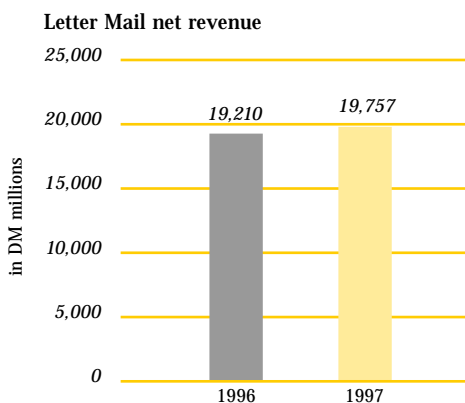
Share of total revenue generated by Letter Mail



quality, to operate efficiently and economically and to maintain the competitive edge in production. The latter was achieved with the new logistics network equipped with 83 state-of-the-art letter processing centers. Second, the strategy focuses on opening new market segments employing innovative, value-added products and services.

On the way to becoming a high-tech business

The Letter Mail division in 1997 systematically expanded the use of the latest technology. These initiatives ranged from automating letter processing activities to using new technologies for the electronic mail service ePost. The number of letter processing centers rose from 26 to 58 during 1997. As a result, Deutsche Post is nearly fully equipped with state-of-the-art production systems, especially in Germany's metropolitan areas. Another 19 processing centers are targeted to begin operation in 1998. The project "Brief 2000", in which about DM 4 billion was invested, will be completed a year ahead of schedule.



The employment of innovative technology in production ensures continual gains in service quality and operational efficiency. Letter delivery time was further reduced in 1997, setting a new record with a 1.6 percent improvement; 92.9 percent of all letters were delivered the day after mailing. The use of enhanced OCR technology was also a factor in this performance.

The increasing use of technology throughout Deutsche Post has gone hand in hand with rising skill levels among employees. Satisfied customers, dedicated and highly skilled staff and cost-optimized processes are the three objectives targeted by the QuiB-quality program. As part of this program, 770 "quality teams" were formed all over Germany during 1997 to optimize operations on-site, raise efficiency and enhance the quality of customer-oriented services.

Streamlining production

In 1997, the design for an automated letter processing system was completed. The introduction of a significantly more detailed barcode for standard letters will enable the fully automated sorting of letters right down to house numbers. The full potential for rationalizing letter processing will be known once the pilot project has been completed in the first half of 1998.

Also successfully completed in 1997 was a pilot project for establishing an information-technology-based information and planning system. This IT-based system, developed to optimize maintenance and materials management, will be implemented at all production sites in 1998.

Four IT-based Mail Redirection Centers and one COA processing center for redirection applications were commissioned in 1997 in order to further improve service quality. In 1997, trial tests were conducted on a data processing system designed to maintain more than four million items of sorting-related information – names of towns, streets and post office box holders, among other data. The system will be implemented nationwide beginning in July 1998. It reduces data maintenance work and allows data bases to be updated much more frequently than in the past.

Increased service for key accounts

With individualized offers, tailor-made products and intelligent services, Deutsche Post, in anticipation of growing competition, has made customer orientation the key of their marketing and sales strategy. As part of these efforts, we reoriented our Letter Mail sales organization and introduced the Key Account Management concept. A new department at headquarters and regional key account managers at our directorates are assigned to customers with large letter volume, customers in the mail-order business, public organizations, insurance companies and manufactures of brand-name products. We have also



Letter processing center

bundled our activities in the private customer market segment. Our foremost goal is to establish additional sales channels and develop new sales promotion measures.

Barcoding: a new service

The latest in tracking-and-tracing technology provides information regarding the delivery of registered and COD letters. For tracking and tracing, letters must have a barcode label that can then be scanned into a data processing system upon posting. The barcode is scanned once again upon delivery and the letter's status reported to a central computer. Customers can find out at call centers when the letter they posted was delivered.

Services bring positive response from business customers

Our "PostIdentservice" is the latest example of how serious we are about providing good service. Deutsche Post offers a special service to banks and other financial service providers that do not operate a



Letter-sorting system

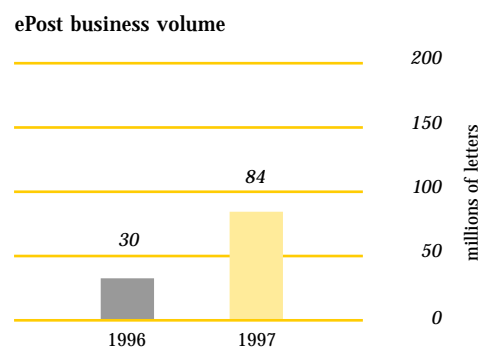
branch network: confirmation of the identity of new customers – as requirement of Germany's Money Laundering Act. This special service is performed by a mail carrier or by a postal branch obtaining and confirming the necessary information on behalf of the customer. Of all the institutions making up the potential market for this service, more than half have already signed up.

We are working to increase loyalty among our business customers. To that end we started to provide mobile postal services in 1997. In 1998, we will be offering nationwide delivery and collection services to and from business customers; taking advantage of this service they can save both money and trips to the post office.

With facilities at more than 6,000 locations throughout the country, Deutsche Post already has an extensive post office box network. In Germany today, some 1.5 million customers rent P.O. boxes. We are expanding our P.O. box facilities at easily accessible locations and expect even more customers to opt for picking up their mail prior to delivery time.

Electronic mail service reports dramatic growth

ePost, Deutsche Post's electronic mail service, has grown rapidly during 1997. About 84 million letters were sent via ePost, an increase of nearly 300 percent over the previous year. Customers deliver letter files to an ePost-Center electronically or via a floppy or CD; Deutsche Post then prints, seals, postmarks and delivers the letters through its conventional letter delivery network. ePost combines the advantages of electronic data transmission – speed and easy handling – with legal acceptability and the traditional nationwide letter delivery. Particularly suited for frequent communication and promotional letters, ePost combines 150 individual services. The opening of our Electronic Data Interchange (EDI) Clearing Center in September marked the launch of a new service. The clearing center receives streams of information, sorts according to recipient profiles on file and



delivers the information to the recipients in the desired form – per in-house file, ePost, fax, e-mail or as an attachment that has been loaded onto a web-server.



ePost center

Pre-mailing services

The development of an entire range of Deutsche Post services related to the physical transport of letters yields substantial benefits for customers. Accurate and up-to-date mailing lists, for example, are important to all companies, government offices and organizations that rely heavily on postal service for their communication needs. Misspelled, outdated or incomplete addresses generate unnecessary costs and have reverberations on the sender's image. We cross-check data files provided to us, correct them where necessary and ensure that our customers' letters reach each and every addressee.

Other useful services have been developed by our "Post Direkt" business segment which, due to its strong growth, was spun off as a subsidiary on January 1, 1998. It now operates under the name Deutsche Post Direkt GmbH with headquarters in Bonn. It will introduce an address collation service via Internet in 1998, a service which will also become economical for companies with small and medium-sized data bases. Besides data maintenance, Deutsche Post Direkt also offers a service for businesses that must process documents

such as lottery tickets, catalogue requests, orders and other forms. Our document reading center in Mannheim can process more than a million documents a day. The use of context-oriented OCR technology ensures that these documents can be read and recorded without error in a highly automated process.

Advertising by mail

Another new product, “Postwurf Spezial”, was tested during 1997. It filters the data base through a range of characteristics to deliver highly selective information. Deutsche Post can thus identify to whom – down to the individual household – and on what date brochures and advertisements should be delivered. This greatly increases the likelihood that a company’s advertising will land in the mailbox of someone who is genuinely interested in it. We will be introducing Postwurf Spezial to the marketplace in 1998 as a product that offers optimized scheduled delivery, a streamlined accounting system and substantially enhanced data quality in the selection of target groups.

Expert consulting services for small and medium-sized businesses

Deutsche Post’s Direct Marketing Centers have proven to be a good platform for direct marketing efforts especially by small and medium-sized companies. Another 19 Direct Marketing Centers began operation in 1997. More than 40,000 customers have taken advantage of our “Werben per Post” (advertising by mail) consulting service, making it a major factor in the rise in “Infopost” revenue.

Expertise and highly developed know-how are our trump cards in the ever-growing direct advertising market. We were one of the first to pursue systematic research in this field. Together with leading market research institutes, we have been conducting direct marketing studies since 1995. The findings are published in our annual Direct Marketing Monitor.



Consulting service at a Direct Marketing Center

“Pressepost” successfully defends its market share

In the highly competitive press products market, Deutsche Post has set quality standards as the market leader and, in 1997, has demonstrated that it can respond to new challenges with flexibility. Despite considerable effort, the competitors were unable to gain any significant market share in the press products market. We did not lose customers but rather won key accounts due to our staggered rate schedule tied to household density.

Prices in conformity with the market and above-average quality will continue to be the hallmark of this business segment in the coming years. Pressepost will also expand its range of features and services so that publishing houses can give their undivided attention to their core business.

Philately – postage stamps and more

Stamp collecting has always been and is likely to continue to be a very popular hobby. We support the stamp-collecting passion with a range of attractive products and an exemplary delivery service. Our latest product in the philately field is the “PortoCard”, a custom-designed advertisement that features postage stamps. Some 1.5 million PortoCards were sold in 1997, primarily to businesses in the service sector. Deutsche Post’s Direct Marketing Centers distribute the credit-card-sized PortoCard booklet. PortoCards are generally issued in relatively small numbers and thus are a hot item for collectors.

The year also saw the launch of the collector’s journal “postfrisch”, aimed at raising customer loyalty levels. The journal is delivered free of charge to all 750,000 customers who order stamps regularly from our collector service.



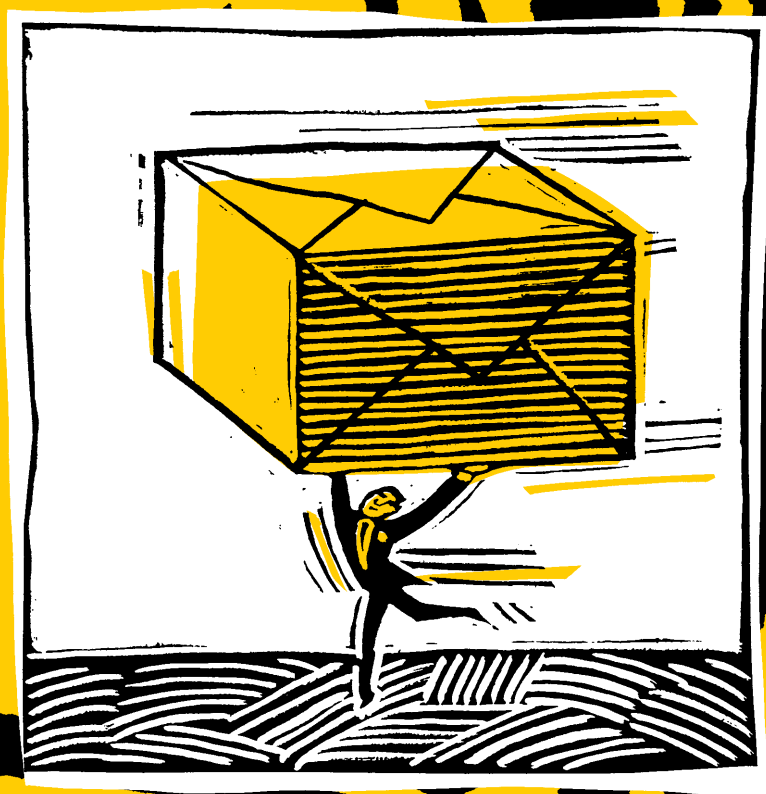
Stamp collecting

Looking to the future

The Letter Mail division is well positioned to meet future challenges. Letter mail and “Infopost” will continue to offer business customers attractive solutions integrated with an expanded range of value-added services. For private correspondents, letters can be an emotional medium possessing intrinsic worth. This represents revenue potential for Deutsche Post that will be tapped through a number of segment-specific marketing measures.

Until complete market liberalization in the year 2003, we will rigorously expand Deutsche Post’s strengths to ensure the long-term competitive strength of our letter mail business. We will take advantage of all options offered by modern information technology to improve our products and services even further and to continually modernize our core postal business. In addition, we will systematically develop our hybrid ePost product into a comprehensive range of electronic products.

With our quality program we will direct our efforts even more selectively toward developing customer interfaces and expanding customer benefits. Long-term customer loyalty is built upon a rigorous customer and market orientation, outstanding quality and cost-optimized production processes. Letter Mail is an integral part of a continually growing market for messaging services and transactions while Infopost is an essential element of the direct marketing service market that will continue to flourish in the future. Both letter mail and Infopost will retain their status as vital products in our postal business.



The largest service provider in the German small-goods-logistics market today is Deutsche Post with a 25 percent market share.

With the introduction of a number of product innovations we have further improved our service quality. The employment of sophisticated logistics systems in our 33 freight processing centers has cut down delivery time within Germany to just 1.2 days on average in 1997.

FREIGHT MAIL

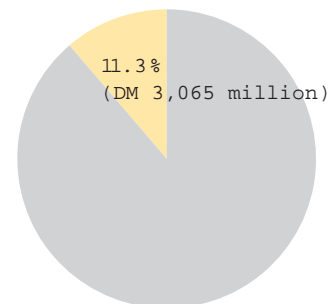
On the right track

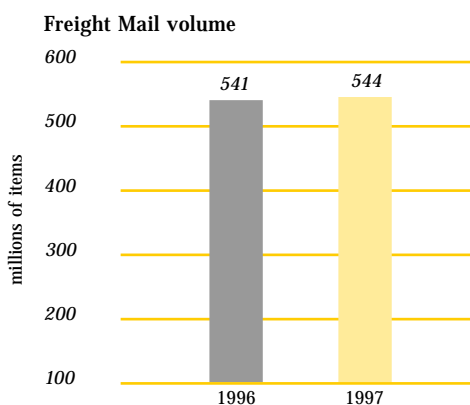
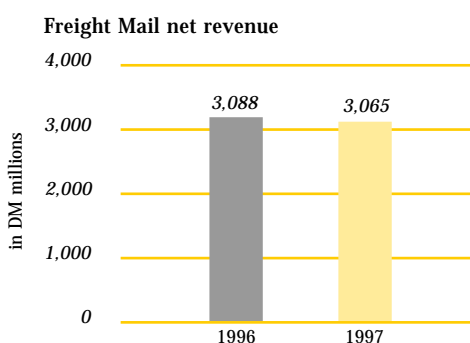
By implementing stringent economy measures and taking rigorous rationalization measures we reduced the negative performance from a loss of DM 1.4 billion in 1996 to a loss of less than DM 900 million in 1997.

Sales turnaround

Stepped-up marketing and sales activities in 1997 stopped sales decline for the first time in years. And even though the mail-order business, the most important freight mail market segment, was flat at best due to unfavorable economic circumstances, sales volume of the division nevertheless rose slightly to 544 million items, a 0.7 percent increase over 1996. This increase was generated primarily by such value-added services as COD and registered parcels, as well as by permit-mailer parcels. By contrast, the number of standard parcels mailed at postal counters declined. At DM 3,065 million, Freight Mail revenue remained largely stable compared to the 1996 revenue of DM 3,088 million. The decline in revenue for standard parcel service was compensated by increased revenues generated by the permit-mailer parcels.

Share of total revenue generated by Freight Mail





Innovations in parcel mail service

Initially introduced on only a regional basis, our reusable Post Box package registered a positive response with customers. The shock-proof Post Box with its economical use of packing material is extremely well suited to the mailing of valuable goods. With our new “Scheckpaket” (cheque-on-delivery parcel service), it is possible to mail goods worth up to DM 20,000. We also offer private customers and small businesses a very convenient method of dispatching parcels – the “FreeWay”, a prepaid-postage label that can be purchased in advance and that includes parcel collection service.

Effective marketing

With the objective to expand our market share in various industry sectors in 1997, we set up Key Account Management, in addition to the regional sales offices. Specific logistics concepts have been developed for five industries and successfully implemented to date. By offering tailor-made products, we were able to win over important customers in industries such as multimedia, textile/clothing, transport, publishing/printing and commerce.

Optimized production processes

The 1997 re-drawing of the areas serviced by postal offices helped ensure a better capacity utilization of all facilities. In addition, package handling systems, the barcoding process and loading of vehicles were fitted to local shipment volume in all freight processing centers. These changes freed up sufficient resources for the development of new product solutions and for meeting specific customer production requirements.

The introduction of more than 10,000 hand-held scanners for freight mail carriers significantly improved the quality of information provided by our tracking-and-tracing system. Deutsche Post’s data processing system, tracking all freight mail items at the various processing stages, offers a high degree of data reliability. With broad deployment of infor-

mation technology for operational control wherever possible, we lower costs, pinpoint and analyze weak points, secure revenues and facilitate the planning process in respect to customers, product management and resource allocation and control.

Freight mail takes to the rail

Deutsche Post remains committed to transport as much of its freight mail as possible by rail. Therefore, we use Deutsche Bahn freight trains for shipment per standardized containers with two-day delivery guarantee.

Building on the experience gained in 1996, we systematically continued to optimize our long-distance transport infrastructure. Reduced shipments and higher process-control efficiency helped to cut



State-of-the-art information technology is the heart of our logistics systems.



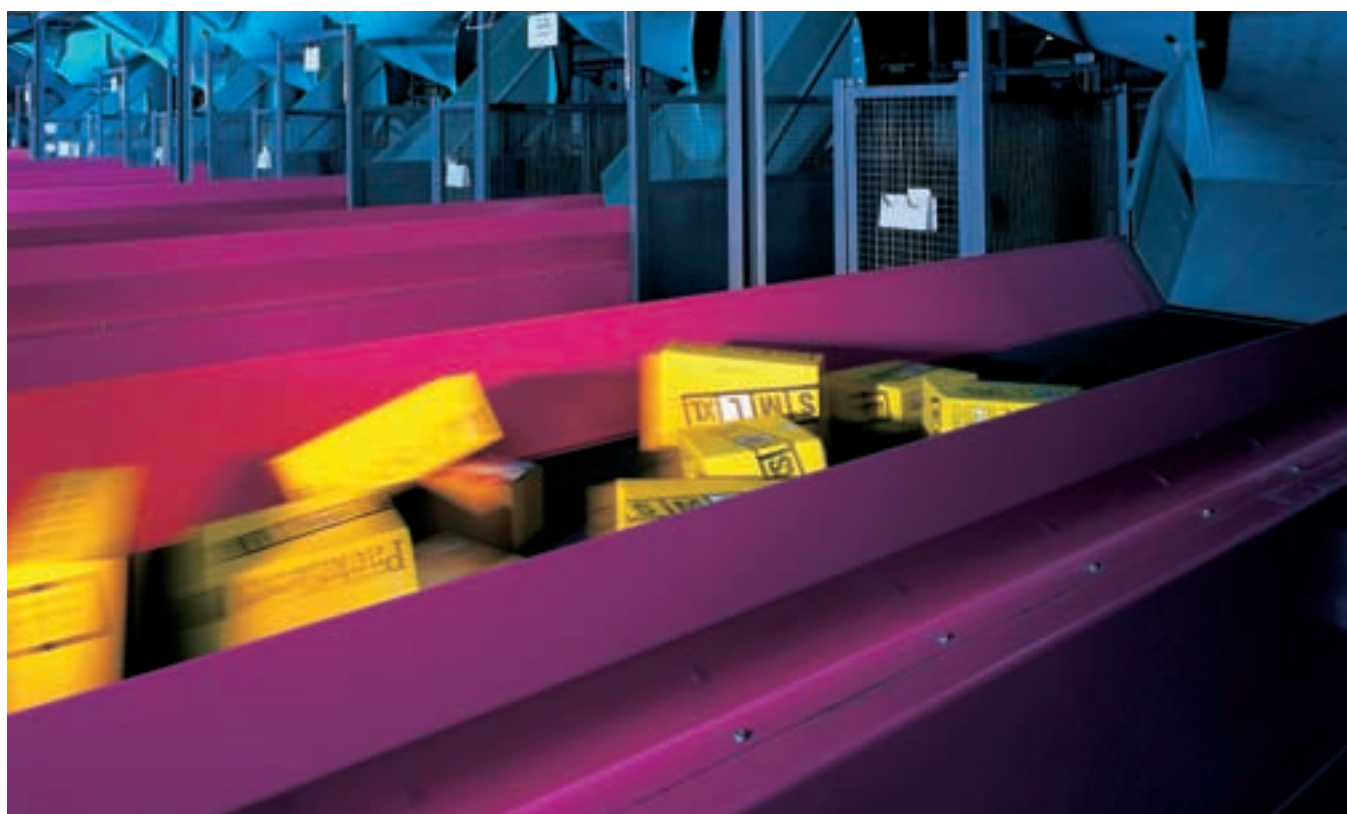
Barcode scanner station

costs significantly over 1996. Efficiency, for example, was enhanced by reducing the number of vehicle types in the delivery fleet. In addition, Deutsche Post increased efficiency further by merging fleet management of the Letter Mail and Freight Mail divisions effective as of March 1, 1997. This opened the way to synergies and made it possible to optimize vehicle deployment.

Looking to the future

As we expect freight mail volume in Germany to grow only slightly in the coming years, mainly due to economic circumstances, we give priority to high-quality standard services. As in 1997, corporate policy continues to focus on product innovations and on intelligent, sector-specific solutions that increasingly integrate value-added services. For example, we will treat several parcels mailed by one sender to a single addressee as one shipment.

Our product "FreeWay" will undergo further development and will be the subject of more intense marketing efforts. In response to strong demand, our reusable Post Box system will be offered nationwide. In our sales organization, Key Account Management is to increase market share in the business-to-business market segment. Using modern information technology such as item scanning, data traffic via the Internet, and Track & Trace with the relevant information accessible to customers, we will equip our entire freight mail production process at all levels to meet today's market requirements.



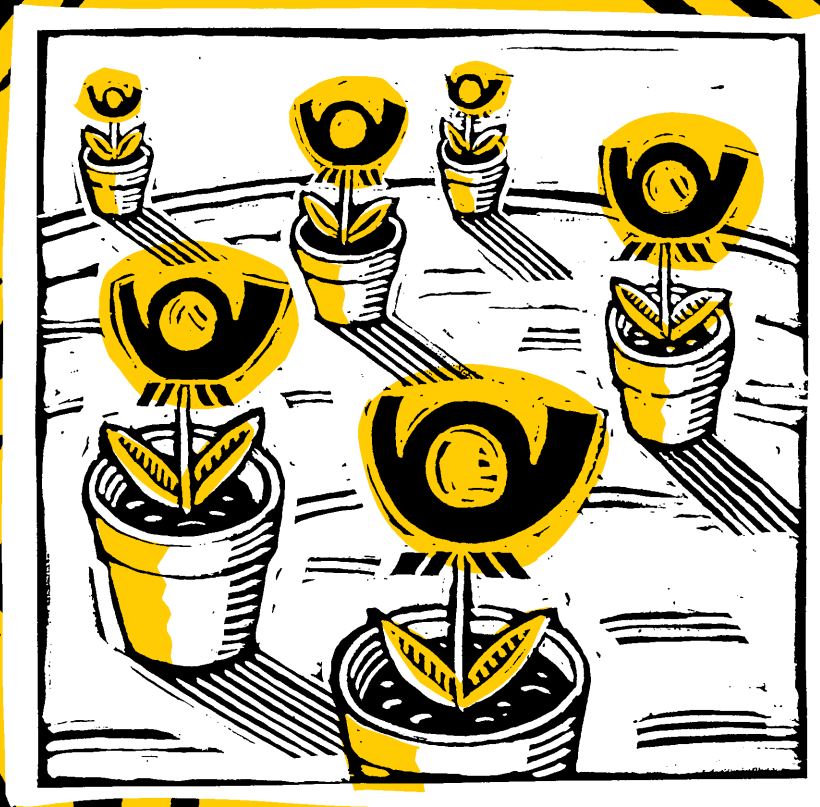
Sorting at freight processing center



Barcoding station at freight processing center

The Freight Mail division will continue to develop and market innovative services to stay competitive and to boost sales, particularly in the fast-growing European courier express parcel market. And we will continue to push ahead with the consolidation of the division on two fronts: increasing and strengthening our marketing efforts and at the same time pursuing a strict cost-control program.





*Our new
postal branch
concept brings
our sales network
even more in
sync with the
market.*

Deutsche Post will reduce the number of its branches to 12,000 by the year 2000 and to 10,000 by the end of 2002. The strategy in respect to physical presence is demand-driven without jeopardizing fulfillment of Deutsche Post's "Infrastrukturauftrag" (infrastructural mandate).

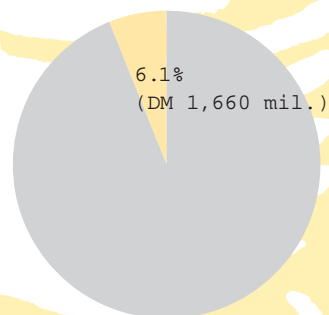
POSTAL BRANCHES

Just around the corner

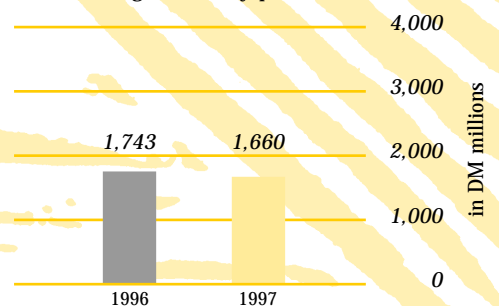
With some 15,300 stationary points of sale and 17,000 employees in our Mobile Postal Service (mail carriers offering an expanded range of services), Deutsche Post in 1997 had one of the largest sales networks in Germany at its disposal. Thanks to new sales vehicles such as postal agencies, more than 90 percent of the country will continue to have access to stationary postal services in the future. In areas with weak infrastructure our Mobile Postal Service will guarantee the availability of a comprehensive range of postal services.

At 296 million, the number of transactions reported by our postal branches for 1997 remained generally stable (1996: 298 million). Revenue generated by external users of our branch network fell to DM 1,660 million, a decline of 4.8 percent over 1996. This drop was due primarily to a decline in telephone card sales as a result of increased competition from other providers and the increasing use of mobile telephony. Low-priced products also contributed to this decline: selling well, their share of total revenue increased.

Share of total revenue



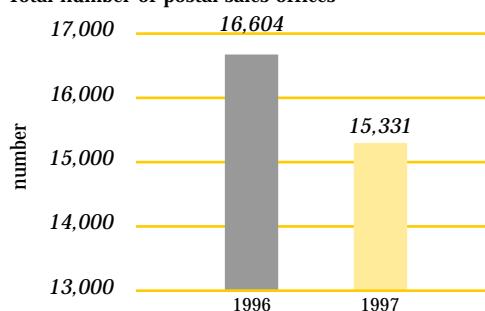
Net revenue generated by postal branches



Reorientation of our branch network

We have substantially improved the customer orientation of our postal sales network by substituting new sales concepts for traditional ones: for instance, providing one-stop shopping service with extended opening hours as well as offering non-postal products, enabling us to cut costs significantly and to make use of synergies gained through collaboration with sales partners.

Total number of postal sales offices



Following field tests in 1996, we added the “PostPlus store” to our sales network. Under one roof, in addition to postal products, it offers a broad range of convenience articles such as stationery, beverages and snacks. The success of these PostPlus stores prompted us to increase their number to 80 during 1997 and to 100 during the first quarter of 1998. The operator of the PostPlus stores – Deutsche Post’s own Service- und Vertriebsgesellschaft (DPSV) – also offers modern, self-service areas that are open to the public 24 hours a day.

The number of postal agencies in operation has increased more than tenfold in the four years since this new sales vehicle underwent trial



Branch with open-service design

operation. During 1997, more than 5,200 agencies offered postal services, particularly in those areas where we had closed small postal branches that were no longer economical.

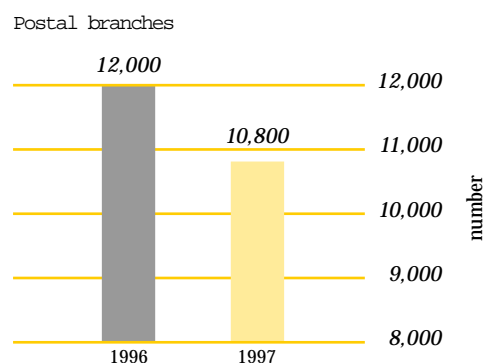
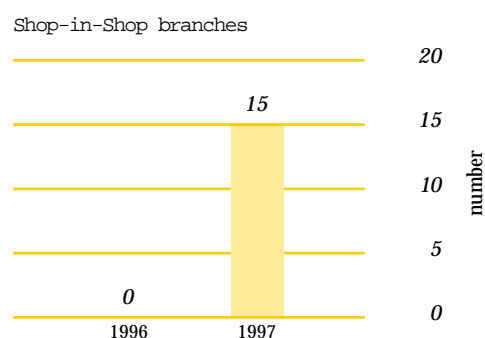
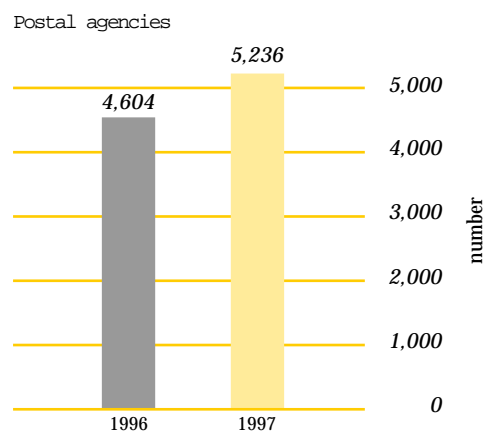
In light of the high level of customer satisfaction and cost advantages that this sales concept offers, we will establish postal agencies in locations with stronger demand as well. Our plan is also to integrate entire postal branches into major department stores. Three Deutsche Post-operated “Shop-in-Shop” branches opened their doors in late 1997, more are in the planning.

Encouraged by the positive response to these Deutsche Post-operated Shop-in-Shop branches in large department stores, we decided to move ahead with another variation: postal branches which are operated by a third party in collaboration with a retail partner. By the fall of 1997, we had collaborated with McPaper AG to set up 13 Shop-in-Shop branches. This trial was such a success that Deutsche Post acquired the McPaper stationery products chain from Herlitz AG retroactive to January 1, 1998. We plan to open some 550 Deutsche Post/McPaper branches throughout the country in the next five years so that our customers can benefit from convenient one-stop shopping facilities at attractive locations.

Top technology, functional design

We continued modernizing our branch network in 1997, investing some DM 100 million over the course of the year. Nearly 100 branches were renovated according to our “open service” design; another 500 to 600 branches will follow.

With more than 22,000 EPOS (electronic point of sale) systems in place, Deutsche Post has terminals in nearly all its sales outlets, both in those it operates itself and in those operated by other companies. Today, 98.5 percent of all transactions are conducted via these IT-based systems.



Collaboration with Postbank

Deutsche Post expanded its business relations with Postbank through a cooperation agreement signed in May 1997 and through the acquisition of a 17.5 percent interest in Postbank.

The agreement defines sale and invoicing of Postbank products at postal branches and the remuneration for these services. It stipulates further that Deutsche Post is the exclusive stationary sales channel for financial services offered by Postbank and its product partners for a period of at least ten years. This collaboration with Postbank – Deutsche Post's most important external user – ensures, for the long-term, a high and predictable utilization of the branch network.

A number of new financial products – loans, investment funds and credit cards – are scheduled to expand our product range in the future. With Wüstenrot, a savings and loan association, and HDI, an insurance company, Deutsche Post in 1997 gained two powerful partners in the financial service segment. Our primary goal, however, is to strengthen Postbank's core business – i.e., its savings and checking accounts operations. Deutsche Post will employ specially trained sales people and advanced EDP-sales systems to support sales activities.

An ongoing process of improvement

In 1997, our Postal Branch division began to employ the EFQM for quality control. Initial results indicate that we are making progress toward developing total quality awareness. Measures implemented to date and aimed at increasing the quality of our services include flexible opening hours, shorter waits for customers, better advice to our customers and modern appearance of our branches.

Looking to the future

In 1998, we will mobilize our staff through intensive training programs to be even more focused on customers and their needs. In

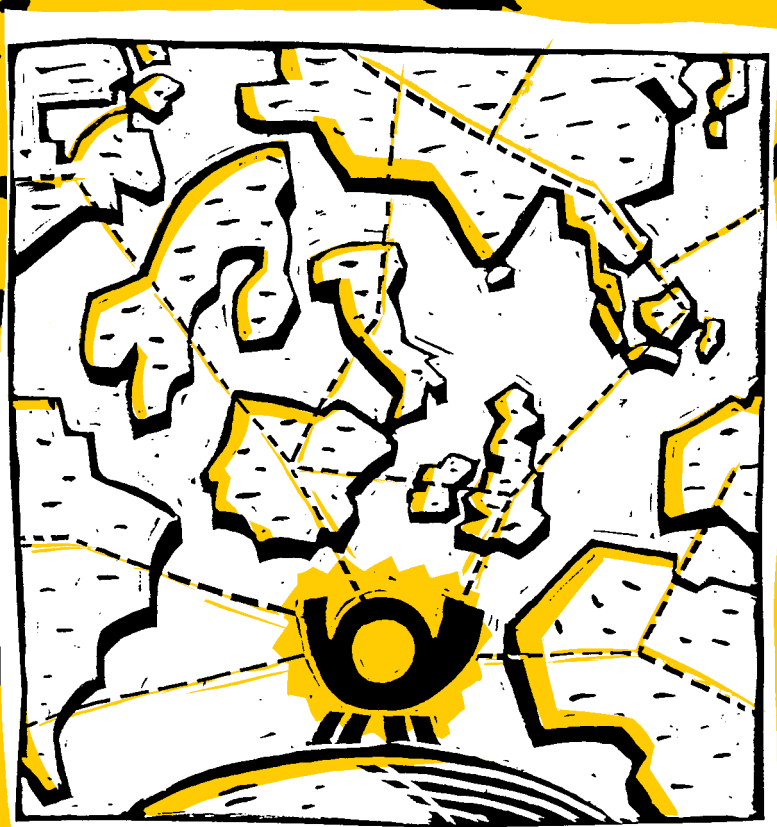
larger branches additional sales and advisory service areas will be set up so that customers can obtain professional answers quickly. Our branch strategy is clearly directed toward the development of the “Center” branch.

In the future these Centers will be the heart of our sales network. In convenient downtown locations, the Centers will focus on providing customers with comprehensive advice on postal products as well as on financial services. The first 17 pilot Centers are to open in April 1998. Our plan is to develop high-powered Regional Centers out of the Center concept.

Continuing the trend of recent years in 1998, we will direct the clientele for postal services to a smaller number of branches. Customer demand will be the primary factor in determining locations.



Customer information service at an open-service branch



The globalization of postal markets accelerates.

Deutsche Post is serving the global letter and freight mail market with customer-oriented products and services. During 1997, we expanded our international operations even further.

INTERNATIONAL POST

Expansion – through innovation and acquisition

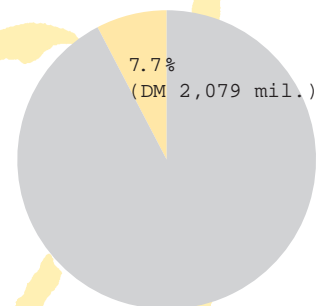
Deutsche Post in 1997 initiated new trends in the international exchange of goods and documents. Among these, the “Local Reply” service was introduced to expand the value-added chain in our cross-border direct marketing service offering. With “Postwurf International” (a direct-mailing product) we provide the advertising industry with a cross-border marketing tool to approach customers in foreign countries.

The planned acquisition of a 22.5-percent stake in DHL International Ltd. in March 1998, is a move of strategic importance and signals that Deutsche Post is becoming a serious contender in the global postal and logistics market. This stake in the world’s leading international express courier gives International Post access to a worldwide logistics network for express mail products. As the global economy increasingly interconnects people across borders, this fast-growing international market will become even more attractive in the long run.

Mostly stable volume and revenue

At DM 2,079 million and 1,132 million items, respectively, both revenue and sales volume in the International Post division remained virtually unchanged from 1996 levels (DM 2,081 million and 1,137 million items). Outgoing international letters declined both in sales volume (-4.8%) and revenue (-7.4%) due to a drop in demand from the private customer

Share of total revenue



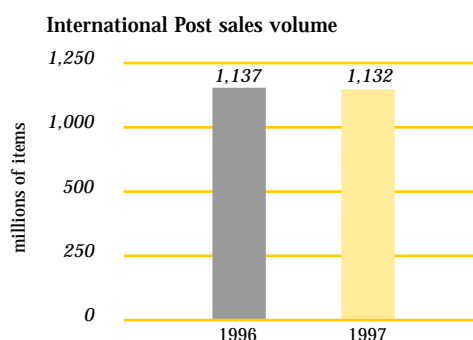
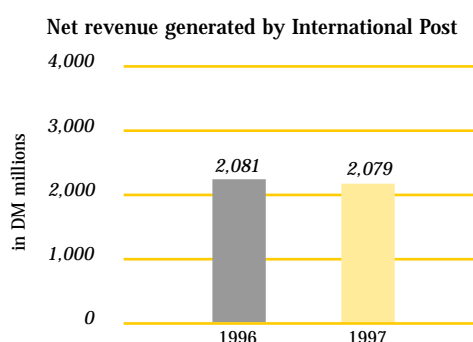
sector. Thanks in particular to a repositioning of the “Premium-Paket” (premium parcel) product, however, revenue generated by business customers in the area of outgoing international freight mail increased by 19 percent over the previous year. The result of increased remailing activities, incoming international letter mail yielded a 2.5 percent growth in volume and an 8.5 percent increase in revenue for the year. A slight decline of 1.6 percent in volume was reported for incoming international freight mail; revenue, however, increased by 3.2 percent over the previous year.

New organizational structure, enhanced flexibility

International Post is already a player in the global arena. In order to strengthen that global reach and competitiveness, we have reorganized our logistics structures, processing centers, channels of distribution and products. In the past, the division focused on the production side, in particular on processing facilities. Today, the focus has shifted toward customers and products: letter mail, freight mail and value-added services for business customers. The reorganization of the international business led to the establishment of three international subsidiaries in mid-1997: International Parcel Post GmbH (IPP), International Mail Service GmbH (IMS) and International Postal Service GmbH (IPS).

IMS is responsible for product management of Letter Mail for business customers and for sales management of International Letter Mail. Its services target business customers both in Germany and abroad who need tailor-made solutions for their cross-border letter mail. Besides focusing on optimizing mail solutions for standard letters, IMS’ consulting service advises customers on how to conduct market- and client-focused direct marketing activities in foreign markets.

IPP is in charge of product management for freight mail for business customers and for sales management of international freight mail. The task at hand is for IPP to organize an efficient logistics network in the



business-to-business segment. By linking four countries in 1997 with Deutsche Post's domestic freight mail network, IPP has established a solid platform for its pan-European parcel mail business. Setting up a franchise system in Austria, obtaining a majority stake in market leader Servisco in Poland, taking a majority interest in Belgian Parcel Distribution and acquiring GP Paketlogistik in Switzerland are the first steps for the Europe-wide network to be expanded further over the coming years.

IPS, in addition to conducting standard mail service, provides international marketing and logistics services. To German firms operating or positioning themselves to operate on an international level and to foreign companies that want to gain a market position in Germany or Europe, IPS offers a variety of services. Among these are shipment handling, consulting services for direct marketing activities and identifying the appropriate service providers who will handle all the details for clients, then mediating on clients' behalf with those service providers. By pooling services, IPS is able to offer clients customized solutions that can give them a virtual presence in markets without



International Postal Center (IPZ) in Frankfurt



Processing air mail bags at the International Postal Center (IPZ) in Frankfurt

having to set up their own infrastructure. In addition, IPS is responsible for product management of consignment.

The establishment and/or acquisition of networks in the business-to-business parcel mail sector in Austria, Belgium, Poland and Switzerland brings Deutsche Post a long way toward achieving the goal of offering Europe-wide cross-border postal and logistics services that meet the highest international quality standards.

Looking to the future

Having taken a position in the European business-to-business market International Post is about to enter the private customer market

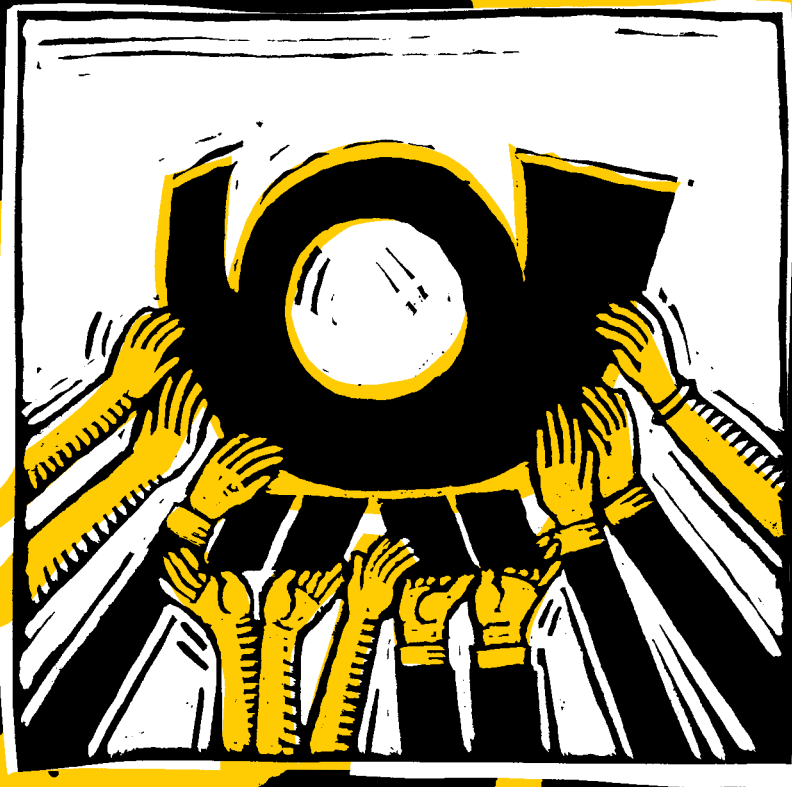
segment as well. We will acquire new customers by systematically gearing our services and products to customer convenience, offering user-friendly products that are tailored to the needs of the market and employ inventive marketing approaches to reach new customers.

Settlement fees arising from cross-border shipments between REIMS II countries (agreeing on a treaty against remailing) are to be raised in 1998. These, after a four-year transition period, will be adjusted to domestic prices. We expect that by then revenues lost due to remailing activities to decrease significantly.

Additional sales offices will be opened abroad to further expand our international letter mail business. Over the next few years, we plan to expand our international freight mail network. In the area of international value-added services we will extend our international consignment activities into other countries and will focus more on integrated logistics solutions for German and foreign business customers.



Loading mail onto a Lufthansa aircraft



The more qualified our employees,
the more competitive we are.

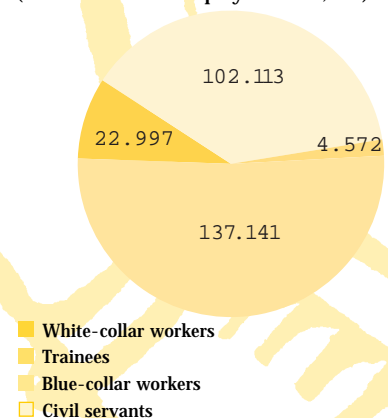
Our competitive strength at home and abroad and the resulting ability to offer job security depends on the skills of our employees. That is why we invest heavily in training programs and why we are fostering a service attitude in our people. We further our staff members by entrusting them with challenging jobs and offering performance-oriented pay. At the same time, however, we must systematically adjust our staffing levels to our actual needs. Job cuts continue to be necessary, but they will be effected through natural turnover and attrition and via early retirement schemes.

Collective wage agreement

In 1997, Deutsche Post committed in a collective bargaining agreement to forego dismissals for operational reasons through December 31, 2000. In return, our employees contribute to a number of measures aimed at cutting personnel costs: shorter breaks, the elimination of hardship pay and the relinquishing of one free day during the year.

As of December 31, 1997, Deutsche Post had a total of 266,823 employees. This represented another substantial drop in staffing level, down 18,066 over the previous year. As a result, expenses for wages and salaries fell by a noticeable 7.0 percent to DM 12,187 million. To be able to manage our largest expense item at a reasonable and sustainable level, however, it will be necessary to take further steps to fully utilize our productivity potential.

Employees as of December 31, 1997
(total number of employees: 266,823)



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Personnel

Expenses for social security contributions, pension expenses and other benefits rose by 8.5 percent to DM 7,435 million. This increase was due to the transfer to pension accruals of DM 621 million previously disclosed in the Notes. Despite this extraordinary item, total personnel expenses declined by 1.7 percent to DM 19,622 million.

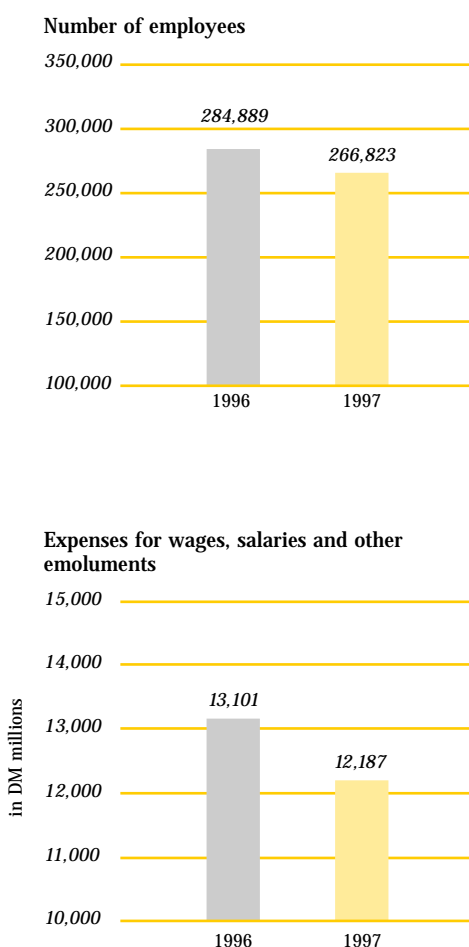
Employees' pension scheme reorganized

The company pension scheme for employees, adopted in 1996, initially applied to our employees in the eastern states of Germany (the former German Democratic Republic). It was subsequently extended to include also all new employees in Germany's western states, effective as of May 1997. At the same time, we introduced the "Betriebsrente Post" (postal pension plan), maintaining the entitlements already earned through "VAP Versorgungsanstalt der Deutschen Bundespost" (Deutsche Bundespost institution for supplementary pensions). We also discontinued statutory insurance coverage through VAP. Vested pensions are now financed by the Deutsche Postbetriebsrenten-Service e.V., Deutsche Post's company pension service established especially for this purpose. A competitive pension scheme for our executive management was introduced on January 1, 1998.

Deutsche Post's pension system now has a calculable and financially sound foundation. It offers employees an attractive supplement to such other pillars of old-age retirement as statutory social insurance and personal retirement provisions. With these changes we also established the prerequisite for substantially reducing in the medium term Deutsche Post's expense burden in this area.

Performance-related pay: new developments

Increasing competition in our business calls for modern compensation systems, i.e., the performance of the individual employee is increasingly important in determining compensation resulting in greater differentiation in individual compensation. It allows us to



categorize all jobs according to their requirements and remunerate correspondingly.

As for our senior managerial staff, a large portion of their total compensation is calculated on the basis of operating results and the achievement of goals individually agreed upon. We plan to extend this proven system to our employees in general. This will entail coupling productivity with quality goals, providing remuneration for individually defined objectives and the utilization of various forms of team work. Collective negotiations on such a performance-oriented pay system have been initiated.

Strong focus on training

In 1997, Deutsche Post again raised the number of traineeships, this time by some 7.0 percent to 2,100. Courses in computer science and systems electronics will be added to the in-house training curriculum in 1998.



Every day, some 25,000 mail carriers make their deliveries by bicycle.

Moreover, in 1997, we offered for the first time a technical and management trainee program. Some 80 technical college and university graduates are to be hired through this program in 1998. Course duration will be geared to the level of the individual's past training and will range from 6 to 18 months.

We are greatly expanding efforts to develop our managerial staff. Candidates who show potential for higher managerial responsibilities are screened in special career advancement seminars. We then prepare them for career-advancing jobs in Germany and abroad, assigning them challenging tasks and integrating them into managerial development groups. Our focus is to train and develop entrepreneurially-minded, motivated managers who thrive on taking responsibility and make a success of it.

Our training methods employ modern learning systems. We have developed a proprietary multimedia system that has often proven more efficient and economical than traditional forms of training.

Equal occupational opportunities for men and women

Women comprise 47.3 percent of Deutsche Post's workforce, making us the largest employer of women in Germany. We promote employee performance without regard to gender, as stipulated by our internal equal opportunity program. Focal points in 1997 were training and occupational re-integration for women who have been absent from the workforce while raising a family, employment during leaves of absence and a non-sexist attitude at every workplace. Local equal opportunity contact persons at our district offices and directorates as well as 15 regional equal opportunity commissioners, who work on a cross-divisional basis, ensure that our equal opportunity plan is more than just a piece of paper.

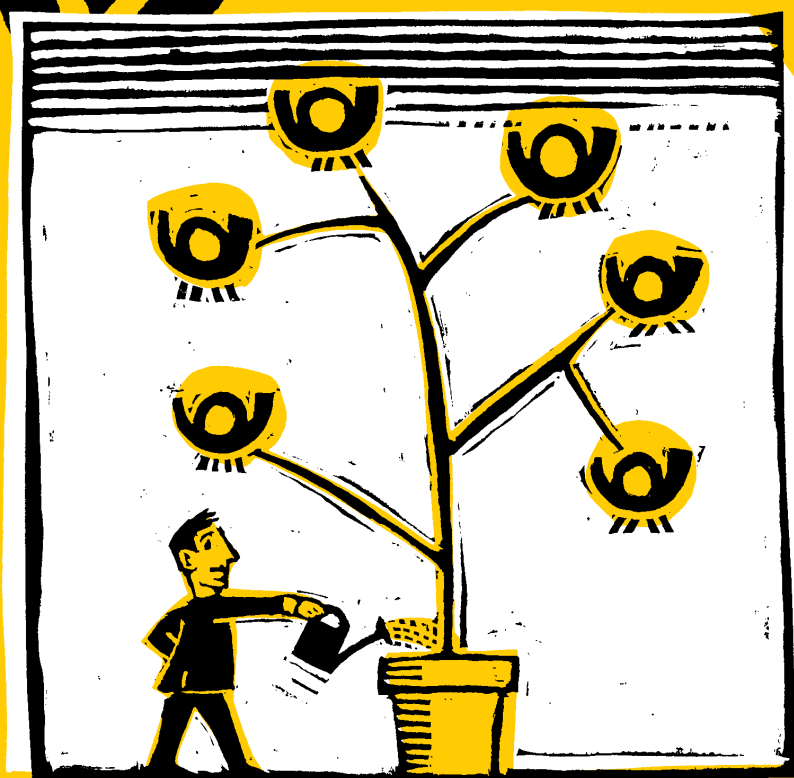


Affixing routing codes at the coding station of a freight processing center

Central works agreement on quality management

In light of how very important service quality is for what is, after all, a service enterprise, we negotiated a central works agreement with employee representatives to ensure high service quality at Deutsche Post. This agreement will serve as the basis for future quality-management activities in all areas of the corporation.

In the personnel field, quality-enhancing activities focus on providing further training and on optimizing core processes. Initial reverberations of these projects are already evident throughout the company.



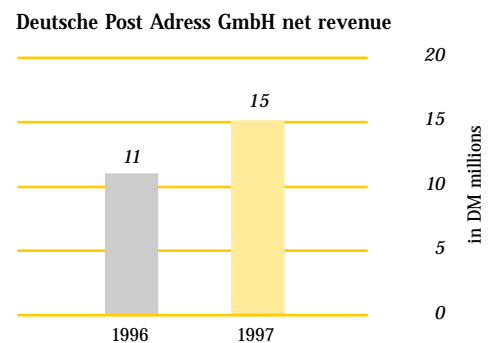
Principal Subsidiaries

A successful service provider improves services continuously.

In order to maintain and expand market leadership, Deutsche Post can rely on the expertise and know-how of its principal holdings – enterprises that have specialized on data processing, software development and logistics.

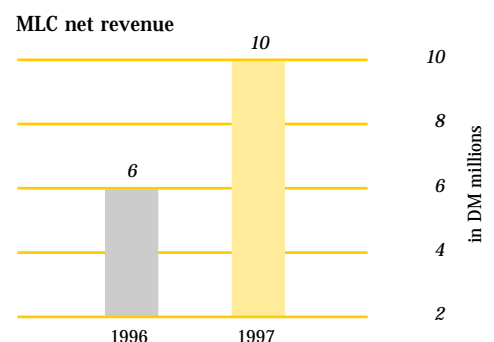
Deutsche Post Adress GmbH

Deutsche Post Adress has a database at its disposal that currently contains some 16 million addresses. Customers have a choice of services, depending upon how frequently they are needed. Revenue from this business grew by a substantial 40 percent to DM 15 million in 1997. We expect further increase in revenue and volume for the current business year as well. The marketing of a reference database managed by Deutsche Post Direkt GmbH and a number of other supplementary databases will also buoy this growth.



MLC Systeme GmbH

MLC is a fast-growing software company with core expertise using optimizing communications processes and logistics operations. During 1997, MLC boosted revenue by 60 percent to DM 10 million. Besides process consulting and adapting software to specific needs, MLC designs, develops and markets high-grade standard software. MLC has been successful in the marketplace for years with its EdiStar core EDI product. Currently, MLC is lining up with new Lotus Notes-based products to develop software solutions for the fast growing e-commerce market.

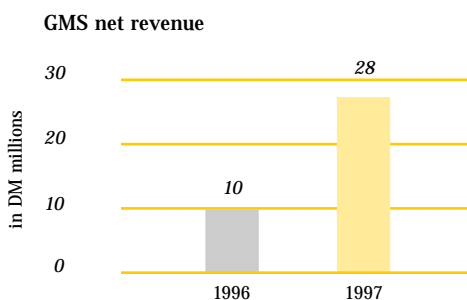


For more than a decade, the market has associated the name MLC with intelligent logistics solutions for the interface between air freight, EDI,

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Principal holdings

inventory management and customs clearance at several major German airports. MLC's partnership with Lotus Notes and Lotus Domino has developed into an area of strong growth in which MLC offers a comprehensive product portfolio, customized solutions, after-sale service, consulting and training. Over the last two years, MLC has advanced into one of the fastest-growing business partners of Lotus.



GMS Deutsche Post Logistik GmbH

GMS registered another successful business year in 1997. With its "InHausPost" service – operating of in-house mailrooms for clients on an outsourcing basis – GMS was able to increase revenue from existing and new contracts to DM 28 million, up from DM 10 million the year before. GMS also expanded into the printing business, offering printing, post-print processing and copying services. It can now plan and manage the entire in-house document flow of large corporations and institutions. GMS aims at extending its consulting and organizational services from paper-based communication to other media such as fax, e-mail and telephone. Further performance gains are to be achieved through the digitization of handling incoming mail by processing systems which will automatically scan, store and distribute documents.

Deutsche Post Express und Transport GmbH

Deutsche Post Express und Transport GmbH (DPET) was founded as a holding company on July 1, 1997. It develops strategies for future-oriented courier, express mail and postal services. Within this holding company have been brought together the operations of Post Express GmbH, Deutsche Post Transport GmbH, Deutsche Post Kontraktlogistik GmbH and the participation in trans-o-flex Schnell-Lieferdienst AG.

EMS Kurierpost GmbH changed its name to Post Express GmbH effective as of July 1, 1997, when preparations got underway for the launch of a completely new, customer-oriented product line aimed at achieving a leading position in the fast-growing courier and express mail services

market. The “Expressbrief” letter – the successor to the letter per express delivery – and the “Expresspaket” parcel are the basis of the new Post Express product range. Next-day delivery is guaranteed. Customers even have the option of choosing a delivery time. Plans for 1998 include the introduction of an express mail product with same-day delivery.

Deutsche Post Transport GmbH (formerly TNT Netzwerk Logistik GmbH) coordinates long-haul traffic between Deutsche Post’s freight mail centers. It also offers its transport network management services to third parties.

Deutsche Post Kontraktlogistik GmbH represents an important step toward tapping the fast-growing value-added logistic services market. The company offers industrial and service companies a broad range of products covering the entire logistics value-added service chain. Besides such traditional services as warehouse management, order processing, dispatch preparation and distribution, Kontraktlogistik also offers services in the purchasing and financial management fields. Already successful in the marketplace with its three logistics centers, Kontraktlogistik will soon be opening additional centers at other locations. In addition to industry-specific logistics solutions, which already exist for the shoe and clothing business, Kontraktlogistik will soon introduce specific logistics solutions for companies in the mail-order and multimedia industries.

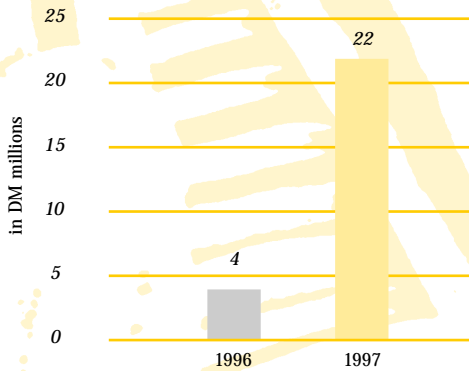
Deutsche Post acquired a 24.8 percent interest in trans-o-flex Schnell-Lieferdienst AG in mid-1997. In Germany, trans-o-flex is the leading express delivery service with specific industry orientation and expertise. It operates in Europe through its subsidiaries in six countries as well as through the pan-European Eurodis Network in which it has an equity interest. As a result, Deutsche Post is able to offer its customers first-class service throughout Europe.



Warehouse of Deutsche Post Kontraktlogistik GmbH

Principal holdings

Net revenue of Deutsche Post Service- und Vertriebsgesellschaft mbH



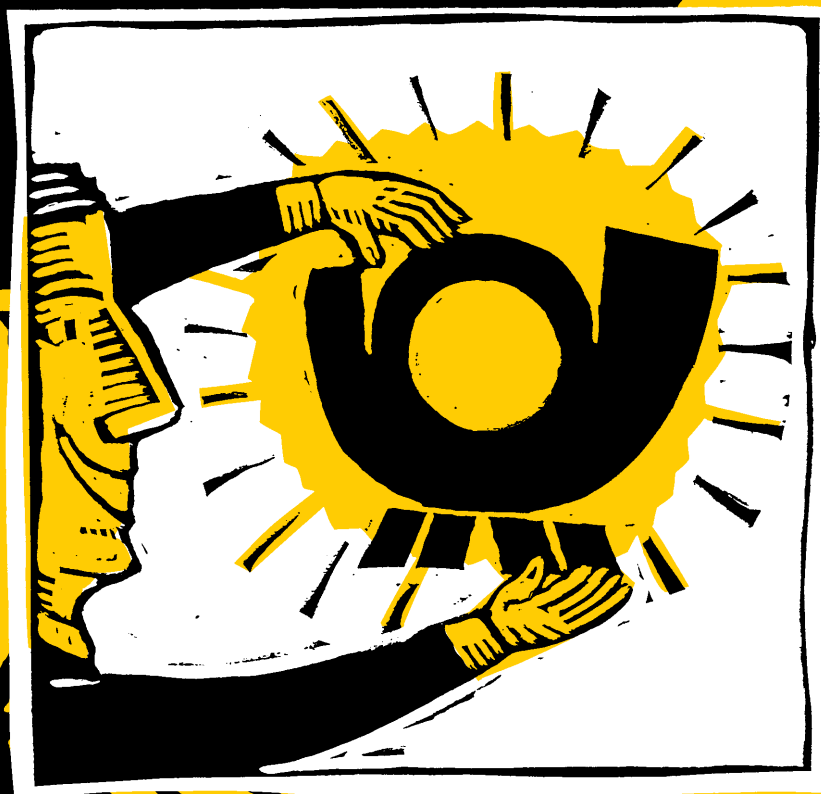
Deutsche Post Service- und Vertriebsgesellschaft mbH

Deutsche Post Service- und Vertriebsgesellschaft (DPSV) operates PostPlus stores. The stores do not only sell postal services but mail-related products and convenience articles as well. In response to the highly favorable customer response to the PostPlus stores, DPSV has expanded at a rapid pace – from 19 stores to 80 during 1997. A total of 811 employees generated DM 22 million in revenue in 1997, which was DM 18 million more than the year before. The plan for 1998 is to increase the number of PostPlus stores by 50 percent to 120 and to triple revenue.



PostPlus store

Financial Statements 1997



Assets

	Dec. 31, 1997 DM '000	Dec. 31, 1996 DM '000
A. Noncurrent assets		
I Intangible assets		
1. Concessions, industrial property rights and similar rights and assets and licenses in such rights and assets	49,593	39,993
2. Advance payments	0	4,745
	49,593	44,738
II Property, plant and equipment		
1. Land, equivalent rights and buildings, including buildings on land owned by third parties	9,642,825	9,328,147
2. Technical equipment and machinery	2,293,873	1,856,008
3. Other equipment, plant and office equipment	1,563,366	1,627,991
4. Advance payments and construction in progress	180,915	680,168
	13,680,979	13,492,314
III Financial assets		
1. Shares in affiliated companies	179,828	224,776
2. Loans to affiliated companies	122,902	118,482
3. Participating interests	875,000	20,838
4. Loans to companies in which participating interests are held		227
0		
5. Housing promotion loans	973,364	973,746
6. Other loans	7,104	8,583
	2,158,425	1,346,425
Noncurrent assets, total	15,888,997	14,883,477
B. Current assets		
I Inventories		
1. Supplies and consumables	72,195	56,983
2. Merchandise	130,206	79,630
	202,401	136,613
II Receivables and other assets		
1. Trade receivables	576,268	592,796
2. Receivables from affiliated companies	252,737	31,005
3. Receivables from companies in which participating interests are held	84,193	142
4. Other assets	1,630,748	894,955
	2,543,946	1,518,898
III Marketable securities		
Other securities	103,252	5,453
IV Liquid assets	2,107,013	1,982,084
Current assets, total	4,956,612	3,643,048
C. Prepaid expenses and deferred charges	500,460	444,853
D. Special loss account from the setting up of certain accruals	0	398,222
	21,346,069	19,369,600

[illegible]

	1997		1996	
	DM '000	DM '000	DM '000	DM '000
1. Net revenue		27,135,948		26,701,740
2. Other capitalized costs		6,000		8,151
3. Other operating income		1,945,758		2,612,852
		29,087,706		29,322,743
4. Cost of materials				
a) Supplies, consumables and merchandise	958,058		990,765	
b) Purchased services	2,679,214	3,637,272	2,271,426	3,262,191
5. Personnel expenses				
a) Wages, salaries and other emoluments	12,186,712		13,101,771	
b) Social security contributions, pension expenses and other benefits	7,435,304	19,622,016	6,851,613	19,953,384
6. Amortization and depreciation				
a) On intangible assets and property, plant and equipment	1,502,292		1,439,756	
b) Amount written off special loss account from the setting up of certain accruals	398,222	1,900,514	202,936	1,642,692
7. Other operating expenses		3,386,858		4,093,529
		28,546,660		28,951,796
8. Financial income/expense (-), net		211,119		205,360
9. Profit on ordinary activities		752,165		576,307
10. Extraordinary income/charges (-), net		-913,272		0
11. Other taxes		222,476		238,998
12. Net income/loss (-)		-383,583		337,309
13. Accumulated loss brought forward		-616,697		-1,156,942
14. Transfer from capital reserve		1,103,684		0
15. Income from release of special reserve under section 17(4) DMBC*		0		202,936
16. Unappropriated retained earnings/accumulated loss (-)		103,404		-616,697

*Law on the Opening Deutschmark Balance Sheet and the Redetermination of Capital

Statement of Cash Flows

	1997		1996	Difference
	DM ' 000	DM ' 000	DM ' 000	DM ' 000
Net income/loss(-)	-383,583		337,309	-720,892
Amortization and depreciation of noncurrent assets and amount written off special loss account	1,900,514		1,642,692	257,822
Changes in long-term accruals	1,783,064		154,260	1,628,804
Other non cash income and expense	-180,553		-213,499	32,946
Material cash income from unusual transactions	-875,728			-875,728
Cash flow according to DVFA/SG formula*	2,243,714		1,920,762	322,952
Gain on disposal of noncurrent assets	-265,318		-348,976	83,658
Changes in current accruals	188,933		32,031	156,902
Changes in current assets and in payables				
Inventories	-65,788		1,221	-67,009
Receivables and marketable securities	-1,122,847		346,505	-1,469,352
Payables (excluding borrowings)	164,000		-105,080	269,080
Changes in prepaid expenses and deferred income	-49,478		-723	-48,755
Net cash provided by operating activities	1,093,216		1,845,740	-752,524
Proceeds from disposal of noncurrent assets	1,715,282		1,502,579	212,703
Capital expenditures	2,026,495		1,995,483	31,012
Net cash used for investing activities	-311,213		-492,904	181,691
Proceeds from short and long-term borrowings	14,995		1,097,225	-1,082,230
Repayments of short and long-term borrowings	672,069		2,414,926	-1,742,857
Net cash used for financing activities	-657,074		-1,317,701	660,627
Change in cash and cash equivalents	124,929		35,135	89,794
Cash and cash equivalents at beginning of year	1,982,084		1,946,949	35,135
Cash and cash equivalents at end of year	2,107,013		1,982,084	124,929

*DVFA = German Association for Financial Analysis and Investment Consulting; SG = Schmalenbach Society

I. General Information

Deutsche Post AG was formed on January 1, 1995; under section 2 of the Post Transformation Act it is the legal successor to Deutsche Bundespost POSTDIENST, which was part of a Federal asset.

The financial statements of Deutsche Post AG have been prepared in accordance with the accounting rules of the Commercial Code (sections 238ff and 264ff). Where captions have been combined in the balance sheet or statement of income, details are given in the notes.

The comparative figures given in () are those of the financial statements for the year ended December 31, 1996.

II. Formats and Accounting Policies

(1) Formats

The formats used for the balance sheet and statement of income are based on those set out in sections 266 and 275 of the Commercial Code. Additional captions result from updating of the opening deutschmark balance sheet. In the noncurrent assets section of the balance sheet a separate caption has been provided for Housing promotion loans.

The statement of income has been prepared in the "type of expense" format.

(2) Accounting policies

Purchased intangible assets are valued at cost, including incidental costs of acquisition, less amortization provided by the straight-line method.

Property, plant and equipment are stated at purchase or construction cost, including incidental costs, less systematic depreciation provided by the straight-line method. Subsidies received are recorded as deferred income and recognized as income over the term of the subsidies. In 1996 they were treated as reductions of purchase or construction cost. Systematic depreciation is provided over useful lives consistent with those specified in the tax rules. Special depreciation is provided where it is necessary for an asset to be stated at a lower value.

In providing depreciation on movable items of plant and equipment advantage is taken of the simplification rule in the Income Tax Regulations permitting provision of a full year's depreciation on additions during the first six months and half of a full year's depreciation on additions during the second half-year. Low value fixed assets costing not more than DM 800 each excluding value added tax are written off completely and treated as disposals in the year of acquisition.

Shares in affiliated companies are valued at cost. Valuation of the right to have Postbank shares transferred to Deutsche Post AG is based on a valuation report; in the balance sheet, this right is included under Participating interests.

Loans receivable bearing no or only a low rate of interest are stated at present value; other loans are stated at nominal amount. The increase in present value from year to year is treated as an addition to the loan. Inventories of postage stamps and heating fuel are stated at fixed values; beginning in 1997, spare parts at freight mail centers are also stated at fixed values. Inventories of other supplies and consumables are stated at the lower of average (moving or weighted) or year-end prices. Merchandise is stated at the lower of (i) cost (determined by the LIFO method) or moving average prices or (ii) market price. To the extent necessary, inventories are stated net of reasonable valuation allowances.

Receivables and other assets are stated at nominal amounts less appropriate individual valuation allowances. Noninterest-bearing receivables with a maturity of more than one year are stated at present value. A general valuation allowance is provided to cover general credit risks. Marketable securities are valued at the lower of cost or market price.

The special loss account from the setting up of certain accruals was set up and included in the opening balance sheet in 1990 under section 17(4) of the Law on the Opening Deutschmark Balance Sheet and the Redetermination of Capital to offset the accruals for uncer-

tain liabilities and expected losses on uncompleted transactions set up in former East Germany as a result of the first application of section 249(1) sentence 1 of the Commercial Code. In 1997 the balance of the account was written off.

The accruals for pensions and similar obligations were determined by the "Teilwert" method described in section 6a of the Income Tax Act (approximately equivalent to the "entry-age normal" method) using actuarial methods and applying the interest rate of 6% required by that statute.

Accruals for taxation and other accruals represent provision for all identifiable risks and uncertain liabilities. They have been set up in the amounts dictated by prudent business judgment.

Accounts payable are stated at repayment amount. Recurring obligations are stated at present value.

Foreign currency receivables and payables are translated at the lower (receivables) or higher (payables) of the historical rate or the year-end rate of exchange.

III. Notes to the Balance Sheet and Statement of Income

A. Notes to the balance sheet

- (1) Details of noncurrent assets are given in the schedule forming Appendix 1 to these notes.
- (2) A list of affiliated companies and companies in which participating interests are held is filed with the Commercial Register maintained by the District Court of Bonn.
- (3) In 1997 the capital of Deutsche Post AG was increased by the issue of shares against non cash contribution. This contribution consisted in the granting by the sole shareholder, the Federal Republic of Germany, of the right to have shares of Deutsche Postbank AG transferred to Deutsche Post AG. This right is disclosed in the balance sheet under Participating interests.
- (4) Housing promotion loans include DM 223 (235) million of loans to

affiliated companies and DM 25 (189) million of loans to companies in which participating interests are held.

- (5) All receivables and other assets, except for items totaling DM 1.6 (–) million, mature in less than one year from the balance sheet date. Receivables from affiliated companies include DM 70.2 (7.9) million of receivables for goods and services. Receivables from companies in which participating interest are held include DM 0 (0) thousand of receivables for goods and services. The remaining receivables consist principally of amounts owed by Deutsche Post Pensions-Service e.V., employees and fiscal authorities.
- (6) Prepaid expenses and deferred charges include DM 7.7 (10.3) million of unamortized debt discount which is being written off over the term of the debt.
- (7) Pursuant to a resolution of the shareholders of Deutsche Post AG passed at the general meeting of July 10, 1997, the subscribed capital was increased by DM 140 million to DM 2,140 million; the consideration received by Deutsche Post AG for the new shares consisted in a claim against the Federal Republic of Germany for the transfer of Postbank shares. After this increase the subscribed capital was represented by 42,800,000 bearer shares of DM 50 each.
- (8) The change in capital reserve is the result of an addition of DM 735 million and a transfer to the statement of income of DM 1,104 million. The capital reserve at the balance sheet date consists of amounts taken to the reserve under section 272(2) no. 1 of the Commercial Code (proceeds from the issuance of shares, including rights, in excess of nominal value).
- (9) The unappropriated retained earnings of DM 103 million include the loss of DM 617 million brought forward from 1996 and the transfer of DM 1,104 million from the capital reserve.
- (10) Pension accruals represent obligations to serving and retired management staff and employees subject to collective bargaining agreements. The accruals for similar obligations were set up for retrospective contributions.

In 1997, Deutsche Post AG set up accruals amounting to DM 2,410 million for part of the indirect obligations to pensioners of the VAP (the Deutsche Bundespost's Supplementary Pensions Institution). These obligations had not previously been accrued, and in 1996 were disclosed only in the notes to the financial statements. Deutsche Post AG also has indirect obligations through Deutsche Post Pensions-Service e.V. relating to pensions and allowances payable to retired civil servants and corresponding expectancies of serving civil servants. These obligations, which are not disclosed in the balance sheet, are partly funded by regular contributions from Deutsche Post AG. The amount of these obligations was determined by actuarial valuation to be approximately DM 16,710 (18,413) million.

The continuing obligations of Deutsche Post AG to pay contributions to Deutsche Post Pensions-Service e.V. are limited by section 16 of the Postpersonalrechtsgesetz to annual amounts of DM 4.0 thousand million up to and including 1999, and thereafter to 33 % of the gross emoluments of serving civil servants and those granted leave of absence.

- (11) Deutsche Post AG has pension obligations amounting to DM 5,010 (8,940) million to non-civil-service employees which are in excess of the pension accruals set up in 1997. These obligations, which are not disclosed in the balance sheet, were computed using actuarial methods and in accordance with the rules for pension accruals set out in section 6a of the Income Tax Act.
- (12) Accruals for taxation were set up principally for real property tax and flat-rate wage tax.
- (13) Other accruals consist principally of amounts accrued for the expected shortfall between the sources of regular income of the Post Office Civil Servants' Health Insurance Fund and the benefits paid, unperformed services relating to the sale of postage stamps, the letter mail and other reorganization concepts and miscellaneous personnel expenses.
- (14) The portions of accounts payable falling due in less than one year or more than five years from the balance sheet date are shown in the schedule forming Appendix 2 to these notes.

- (15) Other payables include the loan from Deutsche Telekom AG under section 2(2) of the Post Transformation Act and employee wages.
- (16) Under section 119 of the Sixth Book of the Code of Social Law, Deutsche Post AG acts as paying agency for social insurance authorities. Under the Ordinance Regulating the Postal Pension Payments Service, Deutsche Post AG's status relative to the funds entrusted to it for this purpose is that of trustee. This trusteeship is not disclosed in the balance sheet. At December 31, 1997, the assets held in trust by Deutsche Post AG in this activity amounted to DM 210 (161) million.
- The assets held in trust by Deutsche Post AG in its function as administrator of housing promotion loans amounted at December 31, 1997, to DM 593 (617) million.
- (17) Contingent liability guarantees amounted at the balance sheet date to DM 1,131 (1,099) million.
- (18) Deutsche Post AG has issued letters of support for amounts totaling DM 1 (2) million.
- (19) Other financial commitments amounted at December 31, 1997, to DM 2,422 (2,619) million, and consisted principally of future payments under long-term transportation contracts and lease agreements and purchase contracts for noncurrent assets.

B. Notes to the statement of income

- (1) Net revenue in 1997 consisted of

(Millions of DM)	1997	1996
Letter Mail		
Letters and Infopost items	18,265	17,729
Pressepost items	1,492	1,481
Letter Mail, total	19,757	19,210
Freight Mail	3,065	3,088
International Post	2,079	2,081
Postal Branches	1,660	1,743
Other net revenue	575	580
Net revenue, total	27,136	26,702

- (2) Other operating income consisted principally of income from the

reversal and application of accruals, gains on disposal of noncurrent assets and rent received.

- (3) Cost of materials: cost of merchandise consisted almost entirely of the cost of phonecards sold. This caption also includes the cost of office supplies, printed matter and consumables. Cost of purchased services consisted principally of transportation, maintenance and energy costs.
- (4) Personnel expenses: pension expenses amounted to DM 5,476 (4,738) million. This item includes DM 4,000 million of contributions to Deutsche Post Pensions-Service e.V., which is the pension fund responsible under section 15(1) of the Postpersonalrechtsgesetz for the payment of pensions and medical allowances to retired civil servants. In 1997, this item also includes transfers to the first accruals for indirect obligations to pensioners of the VAP (the Deutsche Bundespost's Supplementary Pensions Institution) who retired on or after January 1, 1991; these obligations had not previously been disclosed in the balance sheet.
- (5) Amortization and depreciation expense includes DM 173 (205) million of nonsystematic charges.
- (6) Other operating expenses consisted principally of transfers to various accruals, rent, the cost of services provided by the Federal Post and Telecommunications Institute and outside services.
- (7) Financial income/expense consisted of:

<i>(Thousands of DM)</i>	<i>1997</i>	<i>1996</i>
<i>Income from participating interests</i>	<i>154,744</i>	<i>104,221</i>
<i>(of which from affiliated companies)</i>	<i>(154,744)</i>	<i>(103,387)</i>
<i>Income from loans carried as noncurrent assets</i>	<i>233,504</i>	<i>280,112</i>
<i>(of which from affiliated companies)</i>	<i>(79,846)</i>	<i>(112,957)</i>
<i>Other interest and similar income</i>	<i>65,204</i>	<i>39,954</i>
<i>(of which from affiliated companies)</i>	<i>(4,083)</i>	<i>(663)</i>
<i>Interest and similar expense</i>	<i>242,333</i>	<i>218,927</i>
<i>(of which paid to affiliated companies)</i>	<i>(58,216)</i>	<i>(36,841)</i>
<i>Financial income/expense, net</i>	<i>211,119</i>	<i>205,360</i>

- (8) Extraordinary income/charges consisted of extraordinary income from the sale of a participating interests (DM 876 million) and extra-

ordinary charges of DM 1,789 million from the nonrecurring transfer to accruals for indirect pension obligations to employees who retired prior to January 1, 1991. Previously, these obligations had been disclosed in the notes to the financial statements in accordance with Article 28(2) of the Implementation Act to the Commercial Code.

IV. Other particulars

(1) Numbers of employees

The average numbers of employees during the year were as follows:

	1997	1996
<i>Civil servants</i>	106,821	119,422
<i>Wage earners</i>	139,036	146,310
<i>Salaried staff</i>	23,673	26,295
	269,530	292,027

In addition to the above, Deutsche Post AG also had 4,523 (4,373) apprenticed trainees.

(2) Board of Management and Supervisory Board

The names of Board members are given in Appendix 3 to these notes.

(3) Emoluments of members of the Board of Management and Supervisory Board

The emoluments of members of the Board of Management in 1997 amounted to DM 6.5 (6.8) million; the emoluments of former members amounted to DM 0.6 (0.4) million. Accruals for pension obligations to former members of the Board of Management and surviving dependents amounted at December 31, 1997, to DM 8.1 (3.8) million. The emoluments of members of the Supervisory Board amounted to DM 0.6 (0.6) million.

(4) Share ownership

The Federal Post and Telecommunications Institute administers the shares of Deutsche Post AG on behalf of the Federal Republic of Germany, for which it holds a majority interest in Deutsche Post AG as defined in section 16(1) of the Stock Corporation Act.

Noncurrent Assets

Appendix 1 to the notes to the financial statements

Purchase or construction cost					
	Jan. 1, 1997	Additions	Reclassifications	Disposals	Dec. 31, 1997
Thousands of DM					
I Intangible assets					
1.	Concessions, industrial property rights and similar rights and assets and licenses in such rights and assets				
	66,938	37,962	4,745	1,197	108,448
2.	Advance payments				
		4,745	0	-4,745	0
	71,683	37,962	0	1,197	108,448
II Property, plant and equipment					
1.	Land, equivalent rights and buildings, including buildings on land owned by third parties				
	10,104,132	527,491	464,839	226,367	10,870,095
2.	Technical equipment and machinery				
		2,400,655	565,799	146,343	73,889
1,856,008					
3.	Other equipment, plant and office equipment				
	2,780,435	695,221	2,384	324,233	3,153,807
4.	Advance payments and construction in progress				
	680,168	140,526	-613,566	26,213	180,915
	15,965,390	1,929,037	0	650,702	17,243,725
III Financial assets					
1.	Shares in affiliated companies				
		224,776	52	0	45,000
2.	Loans to affiliated companies				
		118,482	7,000	0	2,580
3.	Participating interests				
		20,838	875,000	0	20,838
4.	Loans to companies in which participating interests are held				
	0	340	0	113	227
5.	Housing promotion loans				
		977,513	232,162	0	236,311
6.	Other loans				
		8,583	495	0	1,974
	1,350,192	1,115,049	0	306,816	2,158,425
	17,387,265	3,082,048	0	958,715	19,510,598

Accounts Payable

Appendix 2 to the notes to the financial statements

	Dec. 31, 1997			Dec. 31, 1996		
	Total	of which due within one year	after five years	Total	of which due within one year	after five years
Thousands of DM						
Amounts owed to banks	506,464	44,757	5,602	772,012	45,959	116
Trade payables	990,844	990,844	0	785,014	785,014	0
Amounts owed to affiliated companies of which for goods and services DM 11,802 (prior year 36,594) thousand	1,298,094	201,094	95,480	1,325,209	228,209	323,860
Amounts owed to companies in which participations are held of which for goods and services DM 220 (prior year 1,744) thousand	220	220	0	1,752	1,752	0
Other	2,020,807	978,246	257,955	2,425,516	1,188,067	453,845
of which for taxes DM 151,406 (prior year 164,259) thousand						
of which for social security DM 88,103 (prior year 88,157) thousand						
of which secured by charges on land DM 3,551 (prior year 3,657) thousand						
Total	4,816,429	2,215,161	359,037	5,309,503	2,249,001	777,821

Board of Management and Supervisory Board

Appendix 3 to the notes to the financial statements

1. Members of the Board of Management

Dr. Klaus Zumwinkel

(Chairman)

Dr. Helmut Benno Staab

Dieter Seegers-Krückeberg (until January 31, 1997)

Prof. Dr. Günter W. Tumm

Wolfhard Bender

Dr. Hans-Dieter Petram

Horst Kissel

Dr. Edgar Ernst

2. Members of the Supervisory Board

Shareholder representatives:

Josef Hattig, Chairman

Willem G. van Agtmael

Hero Brahms

Adolf Kracht

Dr. Ing. Manfred Lennings

Dr. Manfred Overhaus

Dr. Klaus Rauscher

Wilhelm Rawe

Dr. Jürgen Richter

Ulrike Staake

Employee representatives:

Kurt van Haaren, Deputy Chairman

Dipl.-Ing. Peter Freis

Petra Heinze (from September 11, 1997)

Henry Hillmann

Heidi Hüther (until April 30, 1997)

Gabi Lips

Günter Nehls

Walter Scheurle

Monika Schleidgen

Siegfried Schulze

Erwin Wohlketter

After completion of our audit we expressed the following unqualified opinion on the financial statements of Deutsche Post AG for the year ended December 31, 1997:

“The accounting and the annual financial statements, which we have audited in accordance with professional standards, comply with the German legal provisions. With due regard to the generally accepted accounting principles the annual financial statements give a true and fair view of the assets, liabilities, financial position and profit or loss of Deutsche Post AG. The management report is consistent with the annual financial statements.”

Essen, April 21, 1998

C & L TREUHAND-VEREINIGUNG DEUTSCHE REVISION

Aktiengesellschaft

Wirtschaftsprüfungsgesellschaft

(B. Klotzbach)

Wirtschaftsprüfer

(Dr. K.-D. Steinfels)

Wirtschaftsprüfer

Report by the Supervisory Board

The Supervisory Board performed the duties assigned by legal mandate and statutes. In fiscal 1997, the Supervisory Board held four meetings.

The Management has regularly informed the Supervisory Board in writing about developments in sales and revenue and about the income situation of the company. The Supervisory Board was informed about all important business transactions. All measures requiring the approval of the Supervisory Board were discussed at length. The Chairman of the Supervisory Board kept in constant touch with the Chairman of the Board of Management and was informed about all important business transactions.

At the meetings held by the Supervisory Board, the Board of Management gave a detailed account of the development of the business and of the income of the company and its business divisions. The Board of Management answered all questions posed by the Supervisory Board. In addition, numerous other reports provided the Supervisory Board with comprehensive information about the company's general situation as well as about issues of particular importance to the development of the company. The topics discussed at length by the Supervisory Board included the Board of Management reports on the new Postal Act, on the status of the negotiations for further cooperation with Deutsche Postbank AG and on the envisaged strategic orientation of the company.

The new Postal Act defines the regulatory framework of the postal markets in the Federal Republic of Germany. The Act, which took effect in early January 1998, provides a solid basis for a future-oriented corporate policy and, on the whole, should ensure conditions for a successful privatization of the company and an environment in which Deutsche Post can successfully compete.

Deutsche Post AG's capital interest in Deutsche Postbank AG and the cooperation agreement between the two companies in respect to utilizing Deutsche Post's branch network pave the way for the two companies working and planning reliably together.



Josef Hattig, Chairman of the Supervisory Board

The Supervisory Board supports the strategy concept, submitted by the Board of Management, for the future growth of Deutsche Post. After the radical reorientation of the business over the last few years, the focus is now on growth in the areas of internationalization, express mail services and value-added services.

The General Committee of the Supervisory Board was expanded to six members from four. Four meetings were held; the agendas included preparing the meetings of the Supervisory Board with an in-depth discussion of the key issues.

At its four meetings, the Personnel Committee discussed a range of human resources issues, including the concept of social security benefits for senior managers.

The Committee for Miscellaneous Affairs held five meetings and discussed and agreed upon the 1996 Annual Financial Statement, the cornerstones of the corporate plan for fiscal 1998, the status of discussions on the new Postal Act, the capital interest in Deutsche Postbank AG, the economic situation of the freight mail segment, the acquisition of holdings as well as real estate projects.

The Mediation Committee did not meet in the year under review. This is in accord with §27(3) of the German Co-determination Law.

The financial statements, the consolidated financial statements, the management report, the Board of Management's report on relations with affiliated companies (the "Dependency Report") and the audit report prepared by C & L Treuhand-Vereinigung Deutsche Revision, Essen, were made available to all members of the Supervisory Board.

The auditors expressed an unqualified opinion on the financial statements, the consolidated financial statements, the management report and the Dependency Report. The Supervisory Board noted and concurred with the results of the audit.

The Supervisory Board has reviewed the financial statements, the management report, the Dependency Report and the consolidated financial statements and discussed them in the presence of the auditors. No objections were raised. The Supervisory Board has therefore approved


the financial statements and Dependency Report prepared by the Board of Management and concurred with the management report. The financial statements have thus been formally adopted.

During 1997, the composition of the Supervisory Board underwent some modification. Ms. Heidi Hüther retired from the Supervisory Board and was succeeded by Ms. Petra Heinze. Further changes were due to the first election of staff representatives who previously had been court-appointed. Ms. Monika Schleidgen and Messrs. Peter Freis and Günter Nehls resigned, and Ms. Pauline Mayer and Messrs. Franz Schierer and Armin Stoffleth were elected to the Supervisory Board.

The Supervisory Board would like to thank its retired member, the management team and all the staff of Deutsche Post AG for their commitment and for the success achieved in 1997.

Bonn, May 11, 1998

The Supervisory Board

A handwritten signature in black ink, appearing to be 'J. Hattig', with a horizontal line extending to the right and a vertical line crossing it.

Josef Hattig

Chairman

Deutsche Post AG: Financial Data at a Glance

Deutsche Post AG	1995 in DM millions	1996 in DM millions	1997 in DM millions
Net revenue	26,680	26,702	27,136
– letter mail	18,872*	19,210	19,757
– freight mail	3,368	3,088	3,065
– international post	2,055*	2,081	2,079
– postal branches	1,847	1,743	1,660
– other	538*	580	575
Profit on ordinary activities	364	576	752
Cash flow according to DVFA/SG formula	1,028	1,921	2,244
Net income/loss (–)	–1,157	337	–384
Noncurrent assets	15,268	14,884	15,889
– intangible assets	24	45	50
– property, plant and equipment	13,375	13,492	13,681
– financial assets	1,869	1,347	2,158
Current assets	3,956	3,643	4,957
– inventories	138	137	202
– receivables and other assets	1,815	1,519	2,544
– Liquid assets and other securities	2,003	1,987	2,211
Prepaid expenses and deferred charges (including special loss account from the setting up of certain accruals)	1,048	843	500
Shareholders' equity	4,858	5,195	5,687
– subscribed capital	2,000	2,000	2,140
– reserves	4,015	3,812	3,444
– unappropriated retained earnings/accumulated loss (–)	–1,157	–617	103

* For a comparison with the 1995 annual financial statement, the figures provide for the following changes:

Letter Mail Division: without electronic mail, philately and "InHausPost".

International Post Division: including international electronic mail.

Other revenue: including national electronic mail, philately and InHausPost.

Deutsche Post AG	1995 in DM millions	1996 in DM millions	1997 in DM millions
Liabilities	15,414	14,175	15,659
– accruals	8,678	8,864	10,836
– payables (incl. deferred income)	6,736	5,311	4,823
Balance sheet total	20,272	19,370	21,346
Capital expenditures in property, plant and equipment	2,558	1,879	1,929
Depreciation of property, plant and equipment	1,193	1,426	1,469
Debts ¹⁾	4,383	3,465	2,823
Financial income net	25	205	211
Personnel expenses	20,455	19,953	19,622
– wages, salaries and other emoluments	13,858	13,102	12,187
– social security contributions, pension expenses and other benefits ²⁾	6,597	6,851	7,435
Personnel expenses as % of total	71.9	68.4	68.2
Annual average workforce ³⁾ (in numbers)	314,905	296,400	274,053
Workforce as of December 31 ³⁾	307,388	284,889	266,823
Return on Equity after tax ⁴⁾	(in %) 3.2	6.5	9.3
Return on sales before income tax and interest expenses ⁵⁾	(in %) 1.3	2.1	2.9
Equity ratio	(in %) 24.0	26.8	26.6

¹⁾ Total of interest-bearing liabilities

²⁾ incl. social security cost and expenses for welfare

³⁾ incl. junior staff

⁴⁾ Profit on ordinary activities, minus other taxes (excl. levies payable to the Federal Govt. in 1995)

⁵⁾ Profit on ordinary activities, minus other taxes, plus interest paid

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