Report on the Business Year 1977

Continental

Report on the 106th Business Year 1977

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Agenda

of the Annual Stockholder's Meeting to be held in the Kuppelsaal of the Stadthalle, Theodor-Heuss-Platz 2, Hannover on Wednesday, June 14, 1978 at 10 a.m.

1.

Presentation of the annual financial statements drawn up as of December 31, 1977, of the report of the Supervisory Board and of the annual report of the Executive Board for the business year 1977.

Presentation of the consolidated financial statements and the consolidated annual report for the business year 1977.

Resolution in respect of unappropriated retained income. Executive Board and the Supervisory Board recommend to carry forward the unappropriated retained income of DM 12206 at December 31, 1977.

2.

Voting on ratification of the Supervisory Board's acts for the business year 1977.

3.

Voting on ratification of the Executive Board's acts for the business year 1977.

In conjunction with points 2 and 3, the Supervisory Board and the Executive Board propose a motion ratifying the Supervisory Board's acts and the Executive Board's for the business year 1977.

4.

Election of Supervisory Board.

The period of office of the acting members of the Supervisory Board comes to an end with the conclusion of the Annual Meeting on June 14, 1978. A new election is thus necessary. Reelection is authorized in accordance with § 10 Parag. 4 of the Articles of Association.

The Supervisory Board of the corporation consists of nine members. In accordance with § 96 Parag. 1 of the stock corporation law and § 76 Parag. 1 Betr.VerfG (law relating to the social constitution of corporations) two thirds of the members shall be representatives of the stockholders and one third shall be representatives of the employees. In view of the proceedings brought by the Deutsche Schutzvereinigung für Wertpapierbesitz e.V., Düsseldorf (german Security owners' association) for a court ruling on the composition of the Supervisory Board of Continental Gummi-Werke Aktiengesellschaft in accordance with § 98 of the stock corporation law, the codetermination law dated May 4, 1976 is not applicable for the composition of the Supervisory Board in this new election.

The Annual Stockholders' Meeting is not bound to the election nominations in the election of the stockholders' representatives.

Mr. Otto Merkle has requested not to be re-elected due to his age.

The Supervisory Board proposes a motion to elect the following gentlemen to represent the stockholders as members of the Supervisory Board, in accordance with § 10 Parag. 1 of the Articles of Association, until conclusion of the Annual Meeting in which the vote on the ratification for the business year 1982 is taken:

Manfred Emcke, Merchant, Hamburg; Rudolf Groth, Banker, retired, Tutzing; Alfred Herrhausen, Member of the Executive Board of Deutsche Bank AG, Düsseldorf; Hans L. Merkle, Chairman of the Managing Board of Robert Bosch GmbH, Stuttgart; Wilhelm Meyerheim, Merchant, Leverkusen-Schlebusch; Bernhard Timm, Chairman of the Supervisory Board of BASF AG., Ludwigshafen.

5.

Election of auditor for the business year 1978.

The Supervisory Board proposes a motion to elect the Deutsche Treuhand-Gesellschaft, Wirtschaftsprüfungsgesellschaft, Berlin/-Hannover, as auditor for the business year 1978.

Members of the Supervisory Board

Alfred Herrhausen, Chairman
Member of the Executive Board of Deutsche Bank AG

Benno Adams*), Deputy Chairman
District Manager of the Industrial Union Chemicals-Paper-Ceramics

Hans L. Merkle, Deputy Chairman
Chairman of the Managing Board of Robert Bosch GmbH

Günther Bartilla*)
Chairman of the Joint Works Council of Continental Gummi-Werke AG

Rudolf Groth
Banker, retired

Otto Merkle
Insurance director, retired

Wilhelm Meyerheim
Merchant

Bernhard Timm
Chairman of the Supervisory Board of BASF AG

Wilhelm Wessel*)
Member of the Works Council of Continental Gummi-Werke AG

*) elected by the employees

Report of the Supervisory Board

The Supervisory Board has been kept regularly informed of the development of the Company by means of written and verbal reports by the Executive Board and has supervised the management of the Company.
In the meetings of the Supervisory Board and in numerous separate meetings we have discussed the business and financial position as well as the planned capital investments of the Company. The budget for the business year 1978 and the long-term planning of the two divisions, tires and technical products, was given particular attention in connection with the overall development of the Company.

The annual financial statements, the accounting and the annual report have been audited by Deutsche Treuhand-Gesellschaft, Wirtschaftsprüfungsgesellschaft, Berlin/Hannover, and have been given an unqualified certification. We agree with the result of this audit.

We ourselves have reviewed the annual financial statements and the annual report. In accordance with the final result of our review, we raise no objections. The consolidated financial statements, the consolidated report contained in the annual report of the Corporation and the report of the auditor of the consolidated financial statements have also been presented to us.

We have given our approval to the annual financial statements prepared by the Executive Board. They have thus been adopted.

In the year under report the Company has continued to make progress. Our thanks are due to the Executive Board, the works council and the employees.

Hannover, April 10, 1978
The Supervisory Board
Alfred Herrhausen, Chairman

Members of the Executive Board

Carl H. Hahn
Chairman

H. Norbert Dahlström
Marketing, Technical Products

Werner Klein
Purchasing and Logistics

Gerhard Lohauß
Personnel and Legal Depts.

Julius Peter
Technology, Tires

Wilhelm Schäfer
Marketing, Tires

Horst W. Urban
Finance

Hans Georg Wenderoth
Technology, Technical Products

Report of the Executive Board

General survey

The revival in the German economy continued in 1977 with an increase of only 2,5% in the adjusted gross national product. This was lower than expected as neither private consumption nor investments in the home market gave the impetus that would have been essential for a stronger upswing. Demand from abroad, also increased to a lesser extent than in the previous year owing to the instability of the international economic situation.

The automobile industry which accounted for approx. one third of our turnover was, as in the previous year, among the few branches of the economy to register a promising development, attaining its best production record to date with a total of 4,1 million vehicles. The increased production as compared with 1976 is due, however, solely to a marked increase in the passenger car sector which was greater than the decline in the commercial vehicle production. In other customer industries such as mechanical engineering, the shoe industry and mining, there was a stagnation in development.

Conditions for our industry remained difficult in 1977. The unusually keen cut-price competition continued in the tire market. Hard-fought price wars were experienced in the replacement tire markets of the Federal Republic and in Europe; these cancelled out a large part of the success achieved by us through rationalization. Tire sales showed an increase only in the original equipment sector and in the export trade.

The picture in the market for technical rubber and plastic products is far more differentiated in contrast. Here, the conveyor belting sector registered a sharp decline in demand, giving rise to price wars similar to those in the tire replacement sector. In almost all other sectors of this important branch of our Company we continued to make progress in sales and in profitability.

Through improved product structure, increases in sales and cost reductions we more than offset the negative external influences, though not as yet to a sufficient extent to provide us with satisfactory business results. An improvement in operating earnings from DM 6,0 million to DM 14,9 milion was, however, achieved.

Loss-Carryover eliminated

In order to make use of the tax los-carryover from 1972 expiring in 1977, we undertook revaluations by switching from the accelerated method of depreciation to the straight-line method. Including the resulting extraordinary income, we show for 1977 a net income that has increased from DM 8,0 million to DM 20,2 million and which is not subject to corporation income tax.

Together with the reserve under the Equalization of Burden Act of DM 5,5 million released after the early discharge of our residual commitment, DM 25,7 million were available to reduce the remaining accumulated deficit of DM 81,2 million carried forward from the years 1972 to 1974.

The loss previously carried forward and shown as a "reminder" in the balance sheet has induced foreign observers especially to draw the wrong conclusions in evaluating the Company.

In view of the stabilized profitability we have resolved to cancel the loss carried forward by transferring DM 55,5 million from the free reserves.

Because of the risks to the international economy, which were intensified by the recent decline in the dollar and other major currencies, no rash expectations may be raised, however, with regard to future developments from the cancellation of the loss carried forward. As long as price instability continues to apply to part of our products for reasons of competition and currency, it is more difficult than ever to forecast results despite the further rationalization measures which are scheduled for this year. This does not change our prime objective of paying a dividend as soon as possible, which will be as much in the interest of our stockholders as of our employees.

The balance sheet structure of Continental shows a picture of continued promise. The improved result of the Company led to an increase in the proportion of stockholders' equity from 35,1% to 35,7%, covering almost 73% (70% in 1976) of fixed assets. Whereas receivables hardly changed compared with the previous year, inventories increased owing to the growth in sales. Total liabilities, however, increased only slightly.

Continued sales expansion

Continental's world-wide sales, including the consolidated sales of foreign subsidiaries in which we have a controlling interest, increased by 4,8% to DM 1 954 million (DM 1 865 million in 1976). Consolidated sales increased by 4,4% to DM 1 858 million (DM 1 779 million in 1976).

The table below shows the development of the Corporation sales:

Corporation sales	1977 DM mio	1976 DM mio	Fluctuation in %
Domestic	1135,5	1078,1	+5,3
Foreign	383,4	360,9	+6,2
Total	1518,9	1439,0	+5,6

Approx. DM 900 million of sales was accounted for by tires (+7,8%) and DM 600 million by technical products (+2,7%). This is a ratio of 60 to 40, a shift of 2 percent being realized in favor of the tire sector as compared with the previous year. Sales per employee increased by 8,7% from DM 77 100 to DM 83 800. 25,2% or a solid quarter of our production went directly into foreign markets. The export share for tires was 30% and for technical products 18%.

The progress made in 1977 is further expressed in the stabilization of our personnel figures. In production, for the first time, we have replaced the bulk of the fluctuation by new employees. Personnel expenditure represented 41,7% (42,3% in 1976) of gross revenues which increased by 5,5% to DM 1567 million. Material expenditure accounted for 43,8% as compared with 43,6% in the previous year.

Through a systematic continuation of our structural reorganization we once again made a profit in the technical products division in 1977, the improvement exceeding the expansion in sales.

The tire division, on the other hand, concluded with a negative result. The deficits were lower than in the previous year and originated mainly from the large-size tire section. They are due to the unfavorable cost structure of the Hannover tire plants, which are still working below capacity, together with the adjustments necessitated there. Passenger car radial tires provided a break even result for the first time.

In the tire division the arduous path via original equipment with its particularly exacting technological demands is proving the right one, also in consideration of its after-effect on business in replacement tires. The once again leading quality of our products led to considerably increased sales of radial tires. In the field of truck tires we belong on an international basis to the few manufacturers with a command of the technology of tubeless all-steel belted 15° tires in design and production quality.

Investments for rationalization and reorganization

In 1977 bottlenecks became evident for the first time in the production of steel belted passenger car tires and truck tires. These were not in the infrastructure but in machine capacities and have led to appropriate investment measures. We take a conservative line in all questions of capacity expansion and take particular account of the differing operating costs in our French and German plants. Our investments in the tire division continue to be focused on improved productivity, on quality assurance and on reorganization of the product range.

In the technical products division we are likewise concentrating on high-yield, technologically high quality products. Although reorganization and modernization have not yet been concluded here either, the improved competitive strength is having a positive effect on business and on earnings.

In order to secure and further expand our export trade, we took over the function of importer in Switzerland, in the United States and in Austria. We have to point out, however, that current international exchange rate, cost and price relationship are confronting us at present with new problems for our exports to foreign markets.

Subsidiaries increasingly consolidated

We made headway with our manufacturing subsidiaries in 1977 but the two subsidiaries in Spain are still a cause for great concern. The measures introduced are running on schedule. The situation in the Alsa Schuhbedarf GmbH, where further reorganization is necessary, is also unsatisfactory. With the acquisition from Kötitzer Ledertuch- und Wachstuch-Werke AG of a one third interest in the Göppinger Kaliko- und Kunstlederwerke GmbH., our financial interest in this corporation increased to 88%.

Conti-Phoenix plan not implementable

Our intention to acquire from the Corona Beteiligungsgesellschaft mbH their 61,9% share in the Phoenix-Gummiwerke AG, Hamburg-Harburg, met with insuperable problems.
A compromise solution considered by those concerned, to amalgamate the two corporations with Corona as the parent company likewise proved to be unworkable.

The development of Continental in the past years shows that our Company with a group turnover of almost two billion DM is quite capable of solving the tasks set on its own initiative, although international experience shows that a larger enterprise is, as a rule, better equipped to fight the growing risks in the international economy.

Election of Supervisory Board

The law on employee co-determination came into force on July 1, 1976. In accordance with our obligation thereunder, we published the "Notice on the future composition of the Supervisory Board of Continental Gummi-Werke AG" in the Federal Register on August 17, 1976 and displayed it on the same day in all plants, departments and branch offices of the Company and of its German affiliates.

The scheduled new election of the Supervisory Board of the Company was adjourned, however, as the Deutsche Schutzvereinigung für Wertpapierbesitz e.V. (German security owners' association) instituted proceedings on August 25, 1976 in the district court in Hannover on the question of whether the co-determination law is compatible with the constitution.

On December 12, 1977 the district court in Hannover ruled that the Supervisory Board of Continental had to be formed in accordance with the co-determination law. At the end of January 1978 the Schutzvereinigung für Wertpapierbesitz filed an appeal against this ruling with the court of appeals in Celle. The Supervisory Board of our Corporation will therefore be formed in accordance with § 96 Aktiengesetz (stock corporation law) and § 76 Betriebsverfassungsgesetz (law on social constitution of corporations) until a final judicial ruling has been rendered.

Continental
1968-77

		1968	1969	1970	1971	1972	1973	1974	1975	1976	1977
Balance Sheet											
Fixed assets	DM Millions	426,2	453,7	514,8	587,3	607,8	568,0	542,0	520,6	504,1	513,2
Current assets	DM Millions	406,2	463,3	566,2	526,0	480,9	527,5	525,0	488,2	511,9	534,8
Balance Sheet Totals	DM Millions	832,4	917,0	1081,0	1113,3	1088,7	1095,5	1067,0	1008,8	1016,0	1048,0
Shareholders Equity	DM Millions	428,7	442,4	453,3	464,2	422,2	381,4	361,5	364,2	356,8	373,9
Long term debt	DM Millions	144,1	162,9	237,0	371,3	370,3	430,7	463,8	460,3	468,2	431,4
Additions to fixed assets	DM Millions	58,5	87,9	134,0	154,8	102,3	60,5	58,9	50,7	60,6	65,5
Shareholder's Equity of total assets	as %	51,6	48,2	41,9	41,7	38,8	34,8	33,9	36,1	35,1	35,7
Shareholder's Equity and Long term debt of: Fixed assets and inventories	as %	94,9	93,5	87,4	96,9	91,0	98,1	101,7	106,4	107,9	102,4
Profit and Loss Statement											
Sales	DM Millions	1103,8	1256,8	1311,7	1301,7	1174,2	1264,0	1453,2	1369,0	1439,0	1518,9
Export Sales	as %	18,3	16,3	15,9	17,4	16,4	19,0	25,6	22,4	25,1	25,2
Cost of Material of gross revenues	as %	43,2	43,3	40,8	38,9	39,5	39,8	42,3	41,9	43,6	43,8
Personnel cost of gross revenues	as %	36,1	36,4	39,7	42,7	47,2	47,4	40,6	42,0	42,3	41,7
Depreciation	DM Millions	58,5	58,1	68,6	77,4	76,7	78,7	81,1	68,7	65,8	53,8
Net income/loss	DM Millions	+ 39,9	+ 39,9	+ 39,9	+ 21,0	− 42,1	− 40,6	− 19,6	+ 3,5	+ 8,0	+ 20,2
Dividends	DM Millions	31,9	31,9	31,9	16,0	-	-	-	-	-	-
Employees Average for the year	in 1000	25,7	27,5	28,1	26,5	24,3	23,4	21,5	19,6	18,7	18,1

Outlook

Sales in the first quarter of 1978 just reached the level of the previous year. The increased currency burdens since the beginning of the year are a source of great concern to us, particularly with regard to our export trade. The labor dispute in the metal working industry has adversely affected the production and sales of our Company.

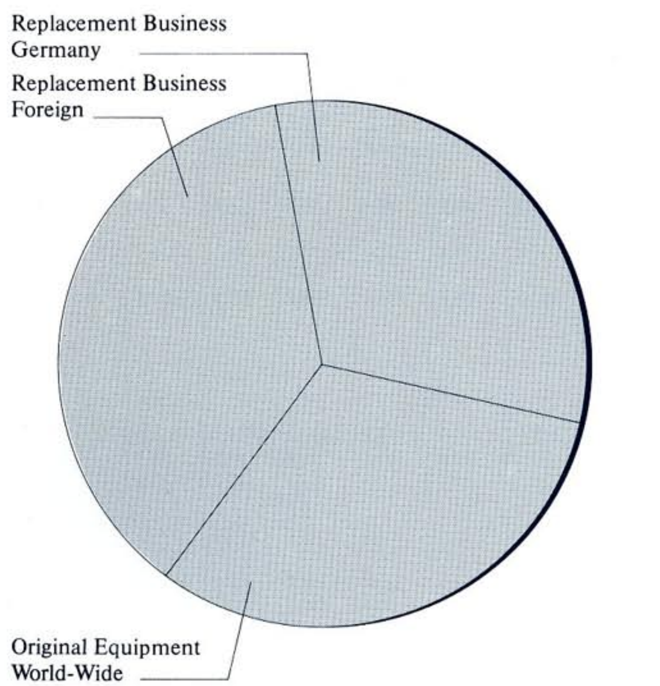
We are planning a further increase in fixed assets in 1978. By 1980 a total investment of DM 300 million is scheduled. These funds are to be used mainly for rationalization measures and for capacity expansion within the framework of the reorganization of our plants.

The unexpectedly weak development in the past year places an additional burden on 1978. The weak economic situation in the industrialized western countries and the basically analogous developments in the Comecon countries plus currency instability will lead to a slower expansion in the German gross national product and international trade this year than in 1977.

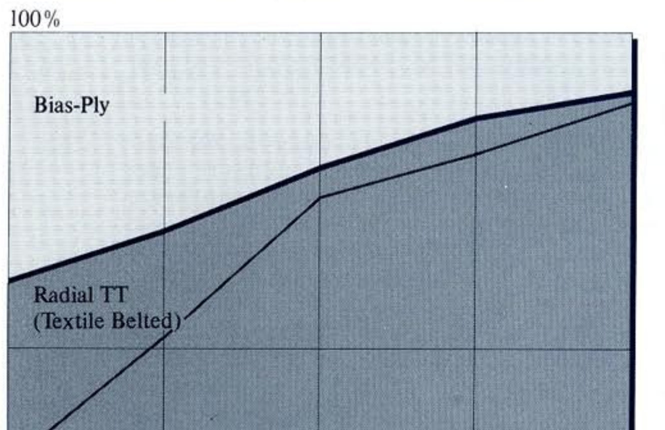
Despite the prevailing negative trends for the German economy and our industry, we hope to make further progress this year. In this connection we are once again confronted with the task of presenting our employees with a challenge in order to master the tasks in hand while adapting to the deteriorating economic situation. We thank all our employees for the work performed by them under difficult conditions in 1977.

Tires

Tire Sales



Radial Tires
Share of Production (Passenger Car Tires)



Marked progress in quality and productivity have enabled us to gain market share in 1977 both in the original equipment market and in the declining replacement market. Tire sales rose by 7,8%, the original equipment business and exports making an above-average contribution whereas sales in the replacement tire market were maintained only with difficulty, due partly to falling prices on the domestic market. Tire sales accounted for 60% of total sales.

A market increase has been achieved above all in sales of our steel belted tires for passenger cars (by 16%) and for trucks (by 18%). The market-based decline in the cross-ply tire sector, which plays only a minor role in our production, was more than covered by these figures.

Although we attained a balanced result with our radial-ply passenger car tires for the year under report, this division of the Company concluded with an overall operating loss, though a smaller one than in the previous year. The losses arose from large-size tires as the tire manufacturing plant in Hannover, which is being re-equipped for the production of high-grade radial-ply truck tires, inevitably still has an unfavorable cost structure. The plants in Korbach and Sarreguemines (France) specializing in the production of labor intensive passenger car tires were operating at full capacity.

Original equipment

We were able to improve our position in the market among German and foreign car manufacturers by systematic orientation towards quality of the finished product and in the manufacturing process. In this vital market, however, competition is not only dictated by quality but also by price so that the margin for pricing remained narrow.

Replacement business

Our strong position in the original equipment market led to an increasingly stable demand for Continental products in the replacement market. The long service life of steel belted tires, however, led to a reduction in consumer demand for passenger car tires, with a consequent aggravation of the price war, particularly in the German market.

Export

In 1977 we increased our sales abroad of total sales by 9,3%, the export share increasing slightly to 30%. In important markets we took over the distribution, as we had done earlier in France, Great Britain, Italy and Sweden. In 1977 Switzerland was added to this list, and in early 1978 the United States and Austria.

Passenger Car Tires

Apart from safety, performance and comfort, our tire development program is taking ever-increasing account of the energy saving potential to be attained by a reduction in rolling resistance.

A change-over to the new 236 tread pattern has enabled us to improve the aquaplaning and non-skid properties of our SR tires on wet roads to top grades.

We introduced the studdable ContiContact TS 730 onto foreign markets where the use of studded tires is permitted. The properties of this winter tire combine to offer an optimum level of safety and performance under all road conditions. We regret that even road-protecting studs are prohibited in Germany so that drivers are forced to suffer restrictions in winter driving properties.

Two-wheeler tires

Further sizes of the matched "twin tires" have been added to the tire range for motorcycles. New in this range are V-tires for speed ratings exceeding 210 km/h (130 mph) and tubeless motorcycle tires that have been very well received, particularly in the United States. We hold a leading position in important markets with our tires for heavy motorcycles.

Commercial Vehicle Tires

Our tires for commercial vehicles and small trucks and our 15° all-steel belted radial truck tire have proved highly successful with original equipment manufactures and in the replacement markets.

With the RS 415 N we have developed a new all-steel belted tire in 5° and 15° versions for long-distance truck transportation. Production has already started. We followed the market trend towards lower tire sections with 70% tires for semi-trailer trucks, buses in scheduled city service and vehicles with high bodies. For fast touring coaches we shall be introducing a newly designed tire with a maximum rated speed of 130 km/h (80 mph) onto the market in 1978. We are also including in our production range the low section tire 15 R with a 22,5 inch rim diameter in a tubeless version for trailers and semi-trailers. A special-purpose truck tire is scheduled for hot climates.

Favorable Reception from Press and Public

The quality of our tires has met with an extremely favorable reception in the technical press. The ADAC (German Automobile Association) and the Stiftung Warentest (an independent consumer research foundation) designated our TS 771 steel belted passenger car tire as the "best tire year-round". The journal "sport auto" stated that the Conti high-speed tire TS 772 "had made absolutely the greatest leap forward". The trade journal "lastauto omnibus", reporting on the RS 321 commercial tire, considers that "it is only Continental that has produced a feasible compromise for an all-year tire". The automobile journal "mot" describes the ContiContact TS 730 winter tire as a "top tire for all-round service"; the "Auto-Zeitung" recommends it for "fast and comfort-oriented vehicles". Our two-wheeler tires were also highly commended. "The Conti twins" says the Frankfurter Allgemeine Zeitung "are well known to motor-cyclists".

Our participation in the International Automobile Exhibition in Frankfurt, at which we presented our entire range of tires and technical products for the first time since 1969, also made a strong impression on consumers, dealers and original equipment manufacturers.

Our aim for the future, too, is uncompromising quality. Despite only a relatively low rate of growth expected in certain European tire markets, the sale of high-grade steel belted tires for today's class of cars, of tires for small trucks, of 15° all-steel belted truck tires and of motorcycle tires gives an overall promise of growth.

Technical Products

The year 1977 ran as scheduled for the technical products division which accounts for approx. 40% of sales. After a distinct decline in growth rates in the second half of the year, sales were 2,7% above those of the previous year, the individual product groups varying in their development. Air springs and hoses, for instance, attained two-digit rates of growth whereas the conveyor belting sector underwent a decline of 10% in a market with an overall contraction of almost 20%.

The picture also changed from 1976 with regard to distribution channels. While the original equipment business with the motor vehicle industry increased with the production development of that industry and export registered a 4% growth despite a slackening trend, the remaining domestic business stagnated.

The policy of the Company, however, was not to attain growth at any price. Our aim was rather to continue the systematic reorganization of our production program and to concentrate on profitable products. In this way we succeeded in stabilizing the lines of foam products and footwear materials and in improving the low returns of those product groups.

All in all, the progress reflected in the result for 1977 exceeds the growth in sales. The positive operating results of previous years continued to improve in the year under report.

The structural reorganization in the plants and the increased level of mechanization in numerous production processes have led to better productivity figures and have contributed at the same time to an improvement in working conditions for our personnel.

The business development was stimulated mainly by the continued high level of business in the domestic motor vehicle industry, which took delivery of more than one quarter of the technical products manufactured by us, and by a positive development in the export trade, particularly in the first half of the year.

Demand in foreign markets underwent an increasing decline in the second half of the year, but the export share showed a slight improvement to 18%.

In the year under report we undertook a comprehensive location assignment for all sections of our production program. This serves as a basic guideline for our development, investment and marketing policies.

Effective January 1, 1978, the functions of development, production and marketing are concentrated on a product-related basis in the eight product groups of this division. This will permit our markets to be served more purposefully and with a higher degree of specialization.

In 1978 we plan to continue optimizing our product range, to improve our production processes and to cut costs. This plan is based on overall modest rates of growth in the major markets. Our Company policy is directed above all towards strengthening our internal organization.

The individual product groups have undergone the following development:

Drive elements

Throughout the year we were able to work to a satisfactory capacity level and thus to stabilize sales at the level of the previous year. We were confronted with considerable pressure from competitors at home and abroad. We were once again able to obtain interesting orders in our business with the Comecon countries.

The development of domestic business was furthered by the good level of business in the motor vehicle industry. It is in this vital customer area that we have helped the technology of our raw-edge V-belts, manufactured by a new process and offering considerably improved technical efficiency, to make a breakthrough. Production was running to full capacity and is being rapidly expanded. The same development is being applied by us on the raw-edge broad section V-belt sector; these belts are in use mainly in sophisticated gear units and have met with a good reception on the market.

The production of rubber toothed belts has been adapted to a new design and a new manufacturing process. Thus, the preconditions for a long-term participation in this growing market have been fulfilled.

Molded goods

The sales trend in this product group was likewise furthered by the good level of business in the motor vehicle industry and by increased application of the parts supplied by us in new models. The stimulation expected from the capital goods industry did not materialize, on the other hand, in the general technical trade. The targets set were nevertheless attained.

Continued development in design and in material technology, particularly in couplings, bushings, bearing elements, rubber diaphragms and rubber seals has opened up new applications. Reprocessed rubber waste has served in the production of new insulating plate systems for railway and highway construction.

Rubberized fabrics, printing blankets, rollers, fabricated products

The major customers of our printing blankets and typewriter platens were hit in the first half of the year by a marked recession. Even the international exhibition DRUPA did not bring our Company the anticipated impetus. In the second six months, however, the typewriter platens business underwent a more promising development.

The high level of business in the motor vehicle industry had a positive effect on rubberized diaphragm fabrics, an extremely exacting product. Sales of dunnage bags and pillow tanks and of other fabricated products exceeded our expectations. The overall result of this product group corresponds to that of the previous year.

Air springs and tube joints

The expansion in sales of our air suspension system has been furthered by a number of new designs for trucks and railway vehicles. Air spring technology is meeting increased customer demands for comfort and for road and cargo protection.

Foam products

The problematic situation in the polyurethane flexible foam business continued in 1977. The furniture industry continued its trend towards less voluminous but more expensive foam upholstery.

The seasonal recession in summer was more marked than in former years. The overall low level of business led to keen price competition for all suppliers, particularly in the foam block sector. Cut-rate prices originating in France and the Benelux countries influenced the domestic market situation. We counteracted this development with systematic cost reductions and selectivity within our product range towards higher values. Consequently a distinct improvement on the still negative operating results was achieved in spite of the unfavorable market situation.

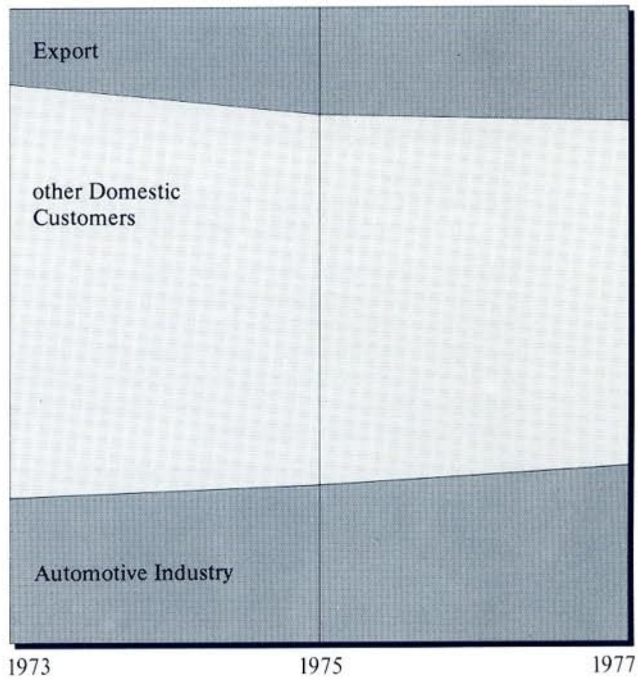
Footwear materials

Against the background of an increasingly consolidated and specialized German shoe industry and of the contraction process now concluded in the shoe repair trade, we were able to realize our sales and profit objectives. Negative trends in the manufacturing sector were compensated by the sales of repair materials and parts. We have developed into the leading supplier on the European repair market. Contributory factors have been a long-term brand promotion and an active product line policy. The hitherto inadequate profitability has been improved by intensified measures to cut cost.

Industrial hose

With the plants working to capacity, sales showed a considerable rise in comparison with the previous year. The positive business situation benefitted equally from motor vehicle hoses, hydraulic hoses and refuelling hoses. Export sales also reached a

Development by Groups of Customers



good level despite currency problems. The pressure of imported goods was felt more strongly, however, in the refuelling hose business.

Conveyor belting

The conveyor belting business was extremely difficult and had a negative effect on the overall result. This sector was marked, as in the previous year, by a sharp decline in demand on domestic and foreign markets. Insufficient employment of capacities led to unusually keen price competition among domestic competitors; this was intensified by low-price imports. A large number of significant foreign projects were deferred for economic reasons and for lack of convertible currency. There is increasing evidence, however, that demand and business volume are beginning to return to normal.

Employees

It is with some satisfaction that we can look back on the employment situation of the year 1977. With our plants generally working more to capacity we were able to stop the downward trend of the labor force to a large extent. It was only in the fixed cost area that the number of employees declined once more. In the production sector we have been replacing the standard fluctuation by new hirings since the middle of the year under report. In some production areas the labor force was even increased.

The number of employees fell by 2,9% from 18 674 to 18 127 on average for the year. On December 31 our personnel comprised 18 173 employees.

Varying developments in the individual product groups and the reorganization of our plants necessitated over 600 personnel transfers. This relatively high figure indicates the extent to which the mobility of our employees formed a precondition for internal staffing adjustment in 1977, too. Almost 200 employees chose early retirement.

The number of foreign workers employed by us increased by 157 to 2 621, representing a proportion of 14,4% of the work force. The largest foreign contingents are provided by Greece, Yugoslavia and Turkey.

Despite the repeated slight decline in the number of employees, personnel expenses (see table below) increased by 3,9% to DM 653 million, representing an average of DM 36 013 per employee. This is 7% higher, and 6,4% higher per hour worked, than in the previous year. The proportion of personnel expenses to gross revenues fell from 42,3 % in the previous year to 41,7%.

	1977	1976	1975
Personnel expenses (in million DM)	652,8	628,6	570,0
Change (in %)	+3,9	+10,3	−4,9
Personnel expenses per employee (in DM)	36 013	33 662	29 102
Change (in %)	+7,0	+15,7	+4,5

The increase in personnel expenses is due essentially to the 6% labor contract increase that came into force in mid-1977 and to vacation rights being increased by one day.

With north/south differentials, the labor costs incurred by the rubber-processing industry in the Federal Republic of Germany in 1977 were once again the highest among the international competition.

Of the so-called nominal manhours, 7,6% – slightly less than in the previous year (7,7%) – were lost through illness, whereas the vacation proportion increased from 9,3% to 9,6%.

Special attention was given to vocational education and to the further training of our personnel.

We have explored new channels to expand our range of vocational education. In conjunction with the Hannover-Hildesheim Chamber of Industry and Commerce and the Academy of Administration and Economics in Hannover, we have been taking part in a model experiment to enable high school graduates to qualify in industrial mangement by combining theory with practice. We feel that this is an appropriate way of training the next generation of managerial staff.

After the increase in 1977, further training facilities are scheduled for 1978, the training of women in professions regarded as typically male having a model experiment character.

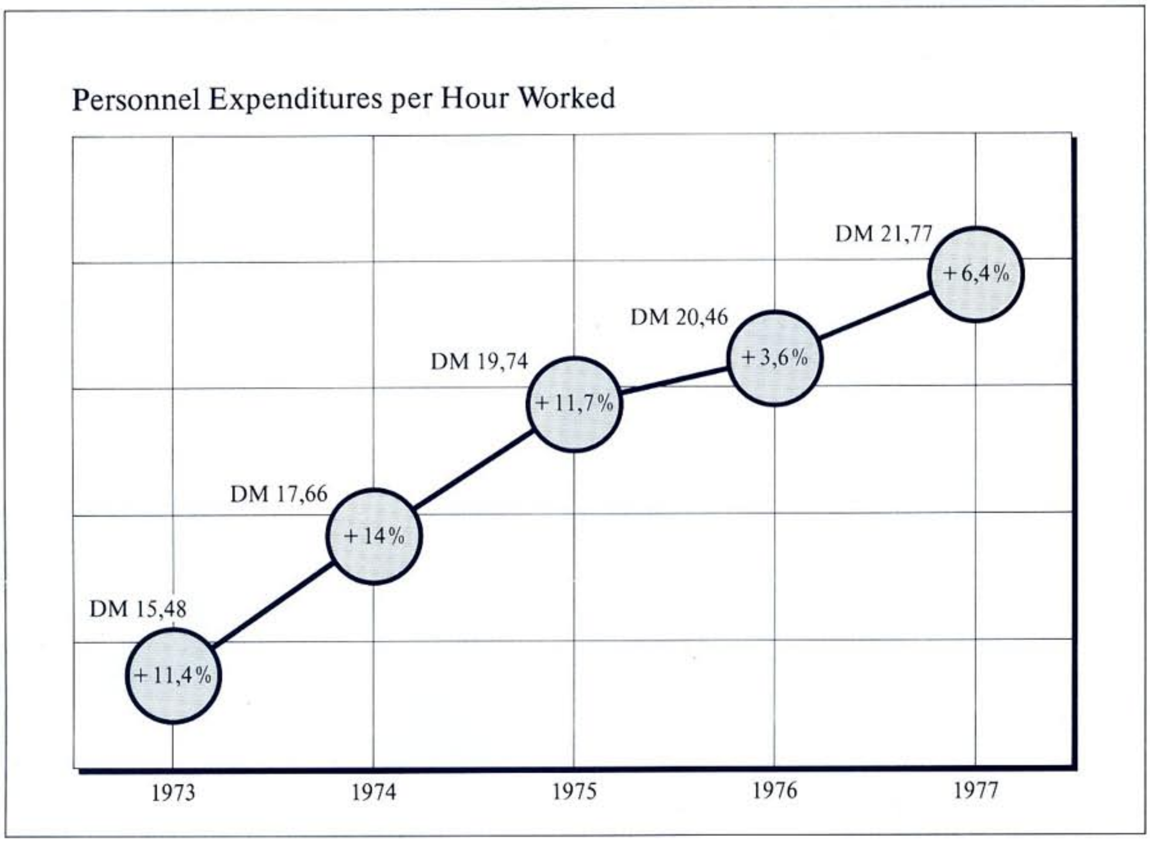
This project is being supported by the Federal Ministry of Education and Science and by the Ministry of Education for Lower Saxony and has a scientific aspect as a research project. It provides for the employment of 28 women in areas including measuring and regulating mechanics, steel casting, turning and universal milling.

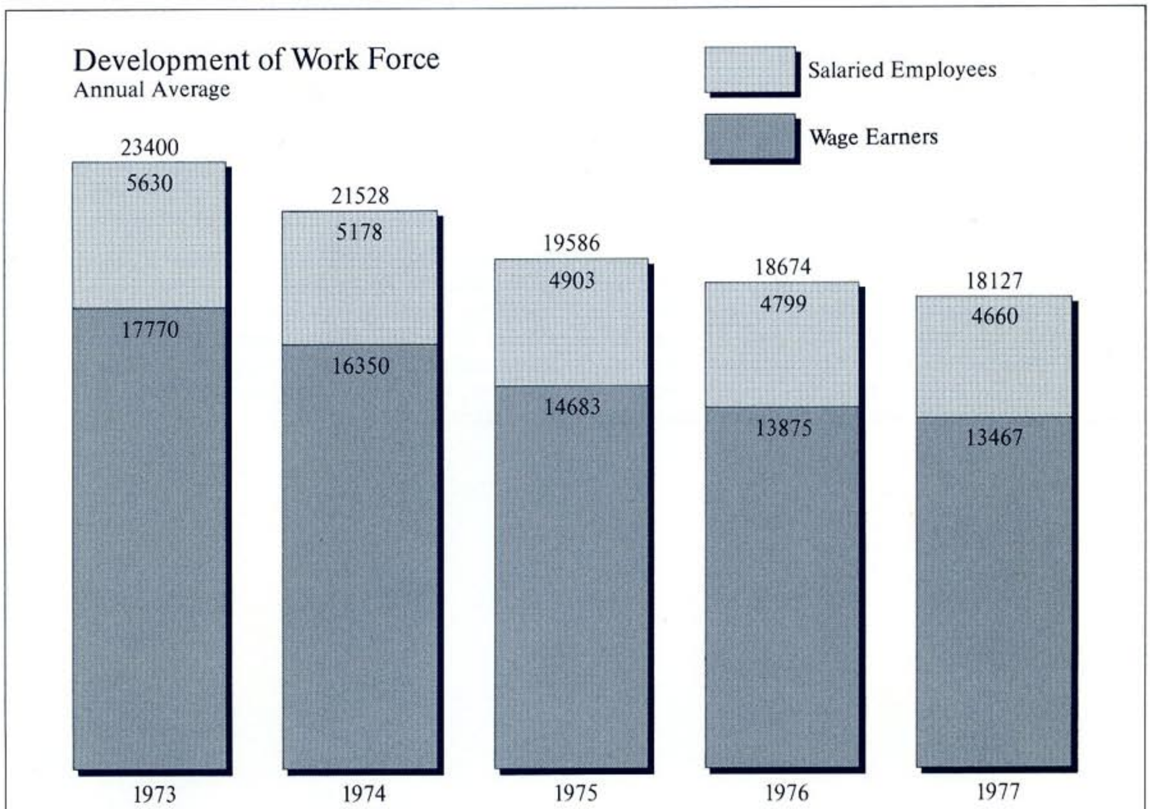
Courses in foreign languages and in-service training of master employees have been intensified. Training programs in tire marketing have been given special promotion in the training of the coming generation of managerial staff. With the employment administration we undertook a series of retraining programs. A large number of employees attended courses in industrial safety.

In 1977, our employees also played an active part in improving production processes and techniques.

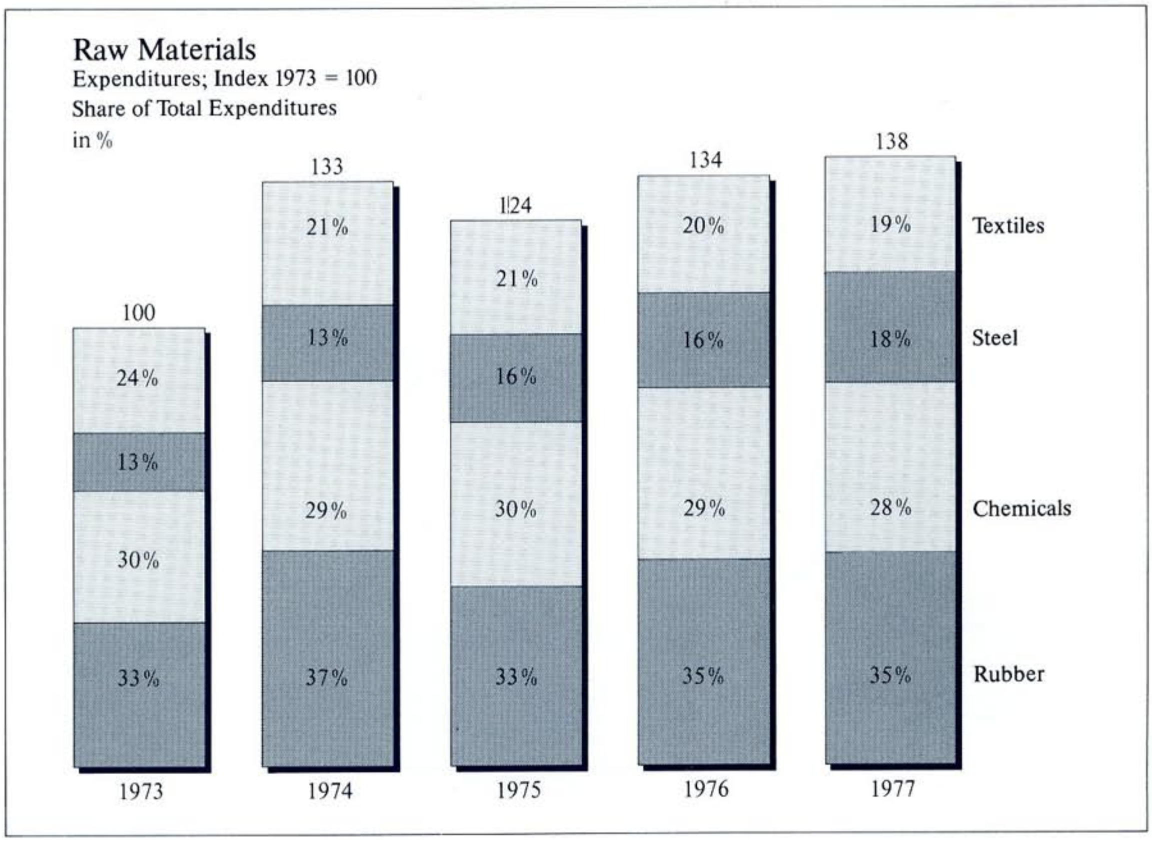
It is gratifying to record that the number of reportable industrial accidents continued to decline, although the number of minor accidents is still relatively high. This has led to supplementary charges on the contributions paid to the employers' liability insurance association. In the Dannenberg, Northeim and Korbach plants, a competition was held to reduce the number of industrial accidents. An improvement in working conditions was achieved on a broad basis.

In the year under report, more than 400 employees celebrated their 25th or 40th anniversary with the Company so that we now have a total of 2 500 employees that have been working for the Company for over 25 years, 83 of them for over 40 years.


Personnel Expenditures per Hour Worked
DM 15,48
+11,4%
DM 17,66
+14%
DM 19,74
+11,7%
DM 20,46
+3,6%
DM 21,77
+6,4%
1973
1974
1975
1976
1977


Development of Work Force
Annual Average
Salaried Employees
Wage Earners
23400
5630
17770
21528
5178
16350
19586
4903
14683
18674
4799
13875
18127
4660
13467
1973
1974
1975
1976
1977

Purchasing



Costs of materials increased in 1977 by 5,9% to DM 686 million. This accounted for 43,8% of gross revenues as compared with 43,6% in the previous year.

Two thirds of the purchasing volume represent raw materials and one third finished goods, services and supplies.

Modifications in requirement composition were only slight, although more steel cord was used as a result of the rapidly expanding production of steel belted tires for passenger cars and commercial vehicles. All-steel truck tires in which both the belt and the carcass consist of steel cord require approximately twice as much steel as passenger car tires.

The increased expenditure on the elastomers, chemicals and textile and steel tension members used by us is due to variations in the product mix and to price increases. We had to accept an average price increase of 8,5% for natural rubber over 1976.

Supplies of raw materials from affiliates, especially from the Drahtcord Saar GmbH & Co. KG, Merzig, and the Deutsche Gasrußwerke GmbH & Co. KG, Dortmund, had a stabilizing effect on prices.

The recessional trend in the economy from spring 1977 onwards, the increased supplies from abroad resulting from the currency revaluations and the efforts of the Comecon countries to barter even more had an effect on prices, as well. These factors, however, were insufficient to offset price increases altogether.

Subsidiaries and Affiliates

Further consolidation of our subsidiaries and affiliates was achieved in 1977. Here, too, as with the parent company, we are confronted with problems of restructuring. We are confident, however, that the measures taken will lead to stabilization and adaption to future requirements. We took over the marketing organization in our vital markets of the United States, Switzerland and Austria.

ALSA SCHUHBEDARF GMBH,
ÜRZELL/SCHLÜCHTERN

Share capital:	DM 0,5 million
Interest:	100%
Personnel:	250

Business activity: Production and marketing of footwear materials: molded plastic shoe sections, instep raisers, shoes for recreation and gardening.

The results of the ALSA GmbH for 1977 were marked by the situation in the German shoe industry. The decline in sales could not be fully offset by rationalization, so that the company closed with a loss.

Further cost-cutting measures have been introduced to improve the results.

AUTOREIFEN VERGÖLST
NEUGUMMIERUNGSWERKE GMBH,
BAD NAUHEIM

Share capital:	DM 20,0 million
Interest:	99,1%
Personnel:	1653

Business activity: Tire retreading and sales of new tires of all brands.

Excess capacities still present in parts of the tire sector led to further intensification in competition within the German tire trade in 1977. As a result, there was considerable pressure on prices both of new tires and of retreads.

Vergölst, one of Europe's leading retreaders, made a profit in the year under report despite these problems. This is due in no small measure to the quality of the product and to the delivery service offered by the company.

DEUTSCHE SCHLAUCHBOOTFABRIK
HANS SCHEIBERT,
ESCHERSHAUSEN

Share capital:	DM 3,0 million
Interest:	60%
Personnel:	200

Business activity: Production and marketing of inflatable boats, boats for work and sport, military craft, pontoons and inflatable life rafts.

The decline of the previous year was offset by increased sales in 1977. The enterprise again concluded the year with a positive result.

GÖPPINGER KALIKO- UND
KUNSTLEDER-WERKE GMBH,
EISLINGEN

Share capital:	DM 8,1 million
Interest:	88,2%
Personnel:	922

VEREINIGTE GÖPPINGER-
BAMBERGER KALIKO GMBH,
BAMBERG

Share capital:	DM 3,0 million
Interest:	82,1%
Personnel:	196

Business activity: Production and marketing of artificial leather for the motor vehicle, bag-making, footwear and clothing industries, sheeting for the motor vehicle and upholstery industries and for application as welding foils and for the manufacture of casings and small cases, book-binding materials, window shade materials, industrial fabrics.

In the meantime, we acquired from the Kötitzer Ledertuch- und Wachstuch-Werke AG their financial interest of one third in the Göppinger Kaliko- und Kunstleder-Werke and have thus increased our interest in this company to 88,2%. We disposed of our majority interest in Kötitz at the beginning of 1978.

The development of the Kaliko-group in 1977 was satisfactory. One particularly pleasing aspect was the success of Bamberger Kaliko in the window shade and industrial fabrice sector.

CLOUTH GUMMIWERKE AG,
COLOGNE

Share capital:	DM 12,0 million
Interest:	50%
Personnel:	1602

Business activity: Production and marketing of conveyor belting and of rubber and plastic molded goods, rubberized fabrics, tank linings, hoses.

Sales of Clouth AG in 1977 equalled that of the previous year, but profits declined considerably. In the conveyor belting section, which is of great significance for the company, there was extremely fierce price competition.

USINE FRANÇAISE DES
PNEUMATIQUES CONTINENTAL SARL,
SARREGUEMINES/FRANCE

Capital:	FF 57,5 million
Interest:	100%
Personnel:	1129

Business activity: Production and marketing of tires and technical products.

Sales and profits of the Usine Française underwent a further improvement in 1977. Our French plant was working to full capacity. Wage-intensive radial ply passenger car tires in particular are manufactured there.

LABORTEX SA,
SANTO ANDRÉ/SÃO PAULO/BRAZIL

Capital:	Cr. 40,0 million
Interest:	100%
Personnel:	708

Business activity: Production and marketing of molded rubber goods for the automobile, electrical and household appliance industries, rubber extrusions, V-belts, inflatable boats, accessories for textile machinery.

Overview

1. Affiliates included in Consolidated Statements

	Stated Capital	Interest in %
ALSA Schuhbedarf GmbH, Ürzell/Schlüchtern*)	DM 500000,–	100
Autoreifen Vergölst, Neugummierungswerke GmbH, Bad Nauheim*)	DM 20000000,–	99,125
Continental Caoutchouc-Compagnie GmbH, Hannover*)	DM 250 000,–	100
Continental Caoutchouc-Export-Aktiengesellschaft, Hannover*)	DM 800000,–	100
Conti Versicherungsdienst GmbH, Hannover*)	DM 20000,–	100
Deutsche Schlauchbootfabrik Hans Scheibert, Eschershausen	DM 3 000 000,–	60
Formpolster GmbH, Hannover*)	DM 20000,–	100
Göppinger Kaliko- und Kunstleder-Werke GmbH, Eislingen	DM 8100000,–	82,114
Iroplastics Kunststoff- und Kautschukvertriebsgesellschaft mbH, Hannover*)	DM 3500000,–	100
Kötitzer Ledertuch- und Wachstuch-Werke AG, i. L., Düsseldorf	DM 1600000,–	81,844
Wilh. Leo's Nachf. GmbH, Stuttgart	DM 420000,–	41,878
Union-Mittelland-Gummi-GmbH, Hannover*)	DM 25000,–	100
Vereinigte Göppinger-Bamberger Kaliko GmbH, Bamberg	DM 3000000,–	82,114

*) Profit/Loss takeover agreements are in force with these affiliates

2. Affiliates not included in Consolidated Statements

2.1 Domestic

	Stated Capital		Interest in %
Clouth Gummiwerke AG, Köln-Nippes	DM	12 000 000,–	50
Deutsche Gasrußwerke GmbH, Dortmund	DM	250 000,–	28,76
Drahtcord Saar Geschäftsführungs-GmbH, Merzig/Saar	DM	60 000,–	33,333
Drahtcord Saar GmbH & Co., KG, Merzig/Saar	DM	30 000 000,–	33,333
KA-RI-FIX Transportband-Technik GmbH, Horrem**)	DM	20 000,–	100
KG Deutsche Gasrußwerke GmbH & Co., Dortmund	DM	8 000 000,–	22,5
Unterstützungskasse mbH der Göppinger Kaliko- und Kunstleder-Werke GmbH, Eislingen**)	DM	20 000,–	82,114
Reifen-Friedenburg KG, Troisdorf**)	DM	90 000,–	66,08
Reifen-Stötzel KG, Hüttental-Weidenau**)	DM	60 000,–	66,08
Rhein-Conti Kunststoff-Technik GmbH, Heidelberg	DM	1 000 000,–	50
Wohnbau Kaliko GmbH, Eislingen**)	DM	40 000,–	82,114
Wohnungsbau Salach GmbH, Salach**)	DM	20 000,–	49,27

2.2 Foreign

	Currency		Interest in %
Conti-Calan Ltd., Johannesburg/Südafrika	Rand	860 000	50
Continental SpA, Pneumatici Prodotti di Gomma e Plastici, Milano/Italien	Lire	300 000 000	100
Continental Gummi AB, Solna/Schweden	skr	100 000	100
Continental Caoutchouc (Suisse) SA, Zürich/Schweiz	sfrs	1 000 000	100
Continental Industrias del Caucho SA, Coslada/Madrid/Spanien	Ptas	253 837 000	97,58
Continental Products Corporation, Tenafly N.J./USA	$	250000	100
Continental Tyre and Rubber Company, Ltd., London/Großbritannien	£	50 000	100
Corrosive Resistant Coatings (CRC), Ltd., Johannesburg/Südafrika	Rand	40 000	50
Especialidades del Caucho SA, Gavá/Barcelona/Spanien	Ptas	437 000 000	100
Ferroplastic & Rubber Industries Ltd., Johannesburg/Südafrika	Rand	330 000	50
D. I. Fram & Comp. Ltd., Johannesburg/Südafrika	Rand	800 000	50
Labortex SA, Santo André/São Paulo/Brasilien	Cr	40 000 000	100
Tensile Rubber Ltd., Johannesburg/Südafrika	Rand	9 000	50
Triple »A« Rubber Co., Ltd., Durban/Südafrika	Rand	8 300	50
Usine Française des Pneumatiques Continental SARL, Sarreguemines/Frankreich	F	57 500 000	100

The Company further holds an interest in two corporations having negligible business activities

**) not consolidated in accordance with § 329, 2 Stock Corporation Act

The capital of Labortex was increased from Cr. 30,0 million to Cr. 40,0 million by using the conversion privileges provided by the Brazilian accounting and taxation laws.

The company increased its sales - due partly to inflation - but concluded the year under report with a loss. The reasons for this were on the one hand the restrictive economic policy of the Brazilian government and on the other company-specific problems that we have begun to solve by the reorganization measures introduced some time ago.

ESPECIALIDADES DEL CAUCHO SA,
GAVÁ/BARCELONA/SPAIN

Capital:	Ptas 437 million
Interest:	100%
Personnel:	412

Business activity: Production and marketing of rubber molded goods for the motor vehicle and household appliance industries, rubber extrusions and rubber matting

We have taken steps involving both personnel and investments in order to help the company back into the profit zone. Despite the continued difficult economic situation in Spain, the results obtained to date have confirmed that the measures taken by us were the right ones.

CONTINENTAL INDUSTRIAS
DEL CAUCHO SA,
COSLADA/MADRID/SPAIN

Capital:	Ptas 253,8 million
Interest:	97,6%
Personnel:	295

Business activity: Tire retreading, production of solid rubber and cushion-type tires (CSE tires).

We increased our interest from 95,6% to 97,6% by acquiring further shares. Despite the improvement attained in sales and operating results, this enterprise, one of the leading Spanish retreaders, is not yet again showing profit.

CONTINENTAL GUMMI AG,
SOLNA/SWEDEN

Capital:	Skr 0,1 million
Interest:	100%
Personnel:	37

CONTINENTAL TYRE AND RUBBER COMPANY, LTD.,
LONDON, GREAT BRITAIN

Capital:	£ 0,05 million
Interest:	100%
Personnel:	74

CONTINENTAL SPA, PNEUMATICI PRODOTTI DI GOMMA E PLASTICI,
MILAN/ITALY

Capital:	Lire 300,0 million
Interest:	100%
Personnel:	88

CONTINENTAL CAOUTCHOUC (SUISSE) SA,
ZURICH/SWITZERLAND

Capital:	Sfr 1,0 million
Interest:	100%
Personnel:	101

Business activities: Marketing of tires and technical products.

The marketing corporations in Sweden, Great Britain and Italy have increased their sales as compared with the previous year and have made a profit despite currency-related problems.

The operating result of our marketing coporation in Switzerland which we took over as of 1st January 1977 was also pleasing.

CONTI-CALAN LTD.,
JOHANNESBURG/SOUTH AFRICA

Capital:	R 0,86 million
Interest:	50%
Personnel:	1283

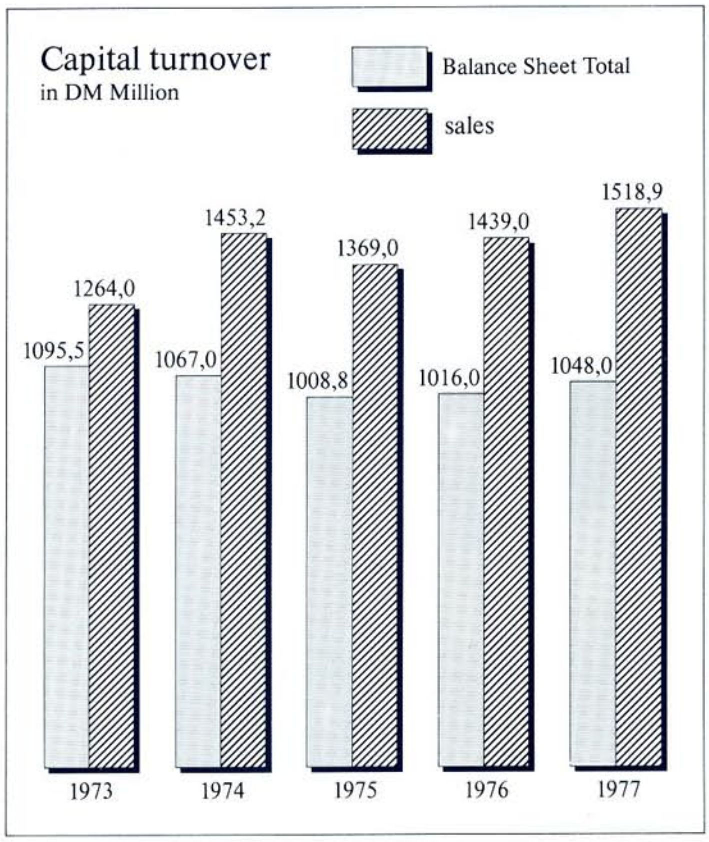
Business activity: Production and marketing of molded rubber goods, extrusions, solid rubber and CSE tires, protective footwear and safety boots, tank linings.

The Johannesburg and Durban subsidiaries combined in the Conti-Calan holding corporation closed with a satisfactory operating result.

Comments on the Annual and Consolidated Financial Statements

Financial and profit situation

The balance sheet totals of DM 1048,0 million show an increase of 3,1% over the previous year's totals adjusted for the loss carried forward, a weaker growth rate than that of sales. Due to the relatively low level of investment in prior years and a strict control of inventories, the balance sheet totals as compared with 1973 have decreased by DM 47,5 million, i.e. by 4,3%. In the same period gross revenues of the Company increased by 23%. The capital turnover rate (sales to total assets) has consequently improved from 1,15 to 1,45 in the past 5 years.



Fixed assets increased by DM 9,1 million over the previous year but their proportion is now only 49% (49,6% in 1976) of the balance sheet totals. Similarly, the trend that was perceptible in former year has continued, whereby the proportion of current assets is increasing through the expanding volume of business and increases in costs affecting inventories (51% in 1977 as compared with 50,4% in 1976). A similar trend can be established in the balance sheets of our competitors at home and abroad.

Equity capital increased as of the balance sheet date by DM 17,1 million to DM 373,9 million and represents 35,7% of the balance sheet totals. 72,9% of the fixed assets (70,8% in 1976) are thus covered. The fixed assets and inventories are financed to 102,4% (107,9% in 1976) by equity capital and long-term borrowed funds. The equity capital ratio is still to be regarded as good by German standards despite the low profits of previous years, although some of our foreign competitors are much better provided with capital.

Judging by the formula "short-term receivables and liquid assets in relation to short-term liabilities", the liquidity of the Company fell at the end of 1977 from 135,8% to 107,1%. The fact should be taken into account, however, that we have deliberately reduced hitherto relatively high long-term borrowings and have converted them to short-term borrowings in line with contractual agreements, in order to benefit from more favorable interest rates. The self-financing quota, i.e. the financing of investments by the net cash flow amounted to 120,6% (110,0% in 1976).

A five-year comparison of balance sheet trends together with the sources and application of funds in 1977 are shown in the charts on page 21 and 23.

The accumulated deficit still remaining after offsetting the annual net profit of DM 20,2 million was covered by releasing the residual reserve of DM 5,5 million for property levy under the Equalization of Burden Act and by a transfer from the free reserve of DM 55,5 million.

In the consolidated balance sheet, however, there is still an accumulated deficit of DM 2,0 million to be carried forward after offsetting a total of DM 62,2 million against the free reserve, the reserve for property levy and the consolidation adjustment, as the accumulated deficit was hitherto higher than in the balance sheet of the parent corporation. This difference is due mainly to the fact that the inventories from intercompany suppliers stored with the consolidated subsidiaries are to be adjusted to the intercompany costs of manufacture. The gross cash flow (per DVFA formula) amounted to DM 107,9 million in 1977 which is 7,1% (6,3% in 1976) of sales. The net profit per share (per DVFA formula) has increased to DM 2,80.

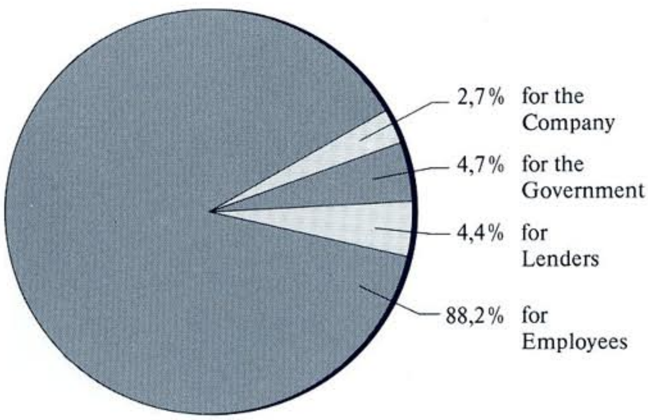
Consolidated Group of Companies

The consolidated balance sheet includes the 13 domestic companies listed on page 16 in which we have a direct or indirect financial interest of more than 50%.

Six other domestic corporations in which the Company also has a majority share were not included in the consolidation owing to their low business volume. These corporations are of minor significance in assessing the financial and profit situation of the Company.

Application of Funds

DM 740000000 = 100%



Total funds equal gross revenues net of cost of material, depreciation, losses from disposal of fixed assets, losses from profit and loss pooling agreements and other expenses.
The amount represents funds originated by the Company.
Most of the funds were used for compensating our employees.

The corporations
KE-MA-Reifen GmbH, Trier
Reifen-Reif, Autoreifen- und Autozubehör-Vertriebsgesellschaft mbH, Cologne
Vulkanisierbetrieb Fr. Reitemeier GmbH, KG, Hameln
were merged into Autoreifen-Vergölst, Neugummierungswerke GmbH in 1977 and are therefore eliminated. The group of consolidated companies has thus remained practically unchanged.

All affiliated corporations have their fiscal year end on December, 31.

As the consolidated financial statements are influenced essentially by the accounts of the parent corporation, we are commenting as before on the two annual financial statements jointly. The following explanations refer generally to the statements of the Corporation. When data refer to the consolidated statements, this is expressly stated.

Balance Sheet

Apart from the change in depreciation methods already mentioned, the balance sheet for 1977 is based on the same accounting principles as in the previous year. These were explained in detail in the annual report for 1976.

The change over from the accelerated method to the straight-line method of depreciation for movable fixed assets was undertaken solely to utilize the corporation income tax loss carryover from the year 1972, that would otherwise have lapsed when the 5-year period expired. However, the depreciation percentages for buildings, structures and related equipment are unchanged. Low value assets are fully depreciated in the first year in accordance with § 6, parag. 2 EStG (income tax law). It is only with respect to machinery and mechanical equipment that the transition to the straight-line method has resulted in lower depreciation. Taking the tax impact into account, the difference in accordance with § 160 AktG (stock corporation law) amounts to DM 9,2 million.

The depreciation to be provided in the coming years on the fixed assets recorded on December 31, 1977 will therefore be higher than previously and will affect the financial results of those years, but we have thus preserved the tax deductibility. As soon as the tax loss carryovers have been used up we naturally intend to revert to the accelerated method of depreciation.

Property, Plant and Equipment

Investments in property, plant and equipment have increased by 17% to DM 62,2 million as compared with the previous year. They are divided almost equally between tires and technical products, the individual plants accounting for

	DM million
Hannover	42,8
Korbach	9,3
Northeim	7,9
Dannenberg	0,7
Sales branches and administration	1,5
	62,2

Apart from rationalization and replacement, it was in particular structural improvement and quality assurance that benefited from the investments, together with, in certain areas, capacity expansion, e.g. for truck tires and selected technical products.

Additions to capital assets of the consolidated subsidiaries (DM 11,0 million) are on the same scale as the total of depreciation and dispositions of fixed assets.

The dispositions of fixed assets relate to obsolete machinery and equipment and to two unused, undeveloped plots of land outside the plants.

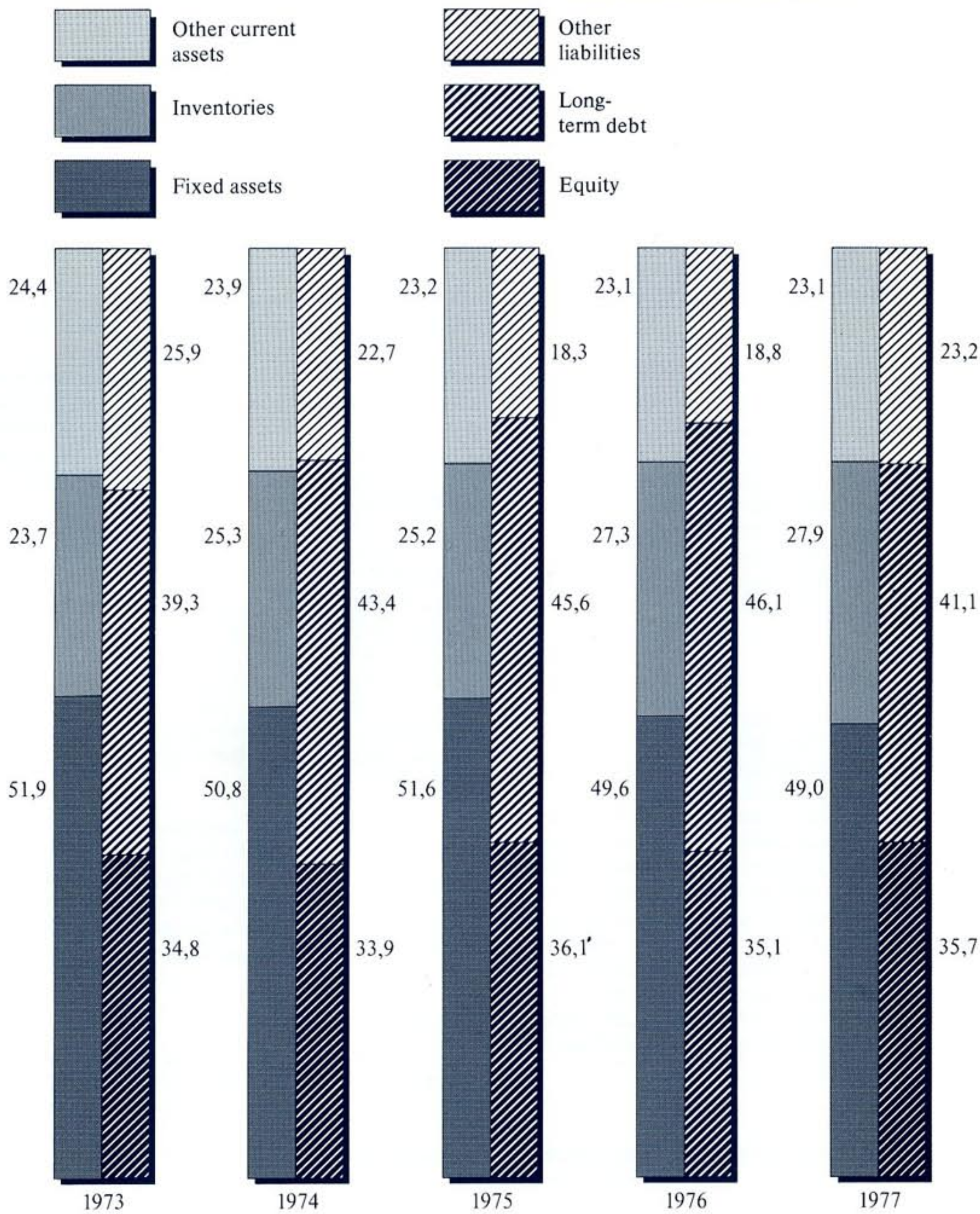
We have provided the following depreciation on the capital additions and transfers of the current year.

	Additions and transfers DM mio	Depreciations DM mio
Land and buildings	0,8	0,03
Machinery and equipment	35,6	2,42
Plant and office equipment	21,4	5,46
	57,8	7,91

Development of Balance Sheets

Assets

Liabilities and Shareholders' Equity



Balance Sheet Totals in DM 1000000

1973	1974	1975	1976	1977
1095,5*)	1067,0*)	1008,8*)	1016,0*)	1048,0
Change of %				
+0,6	−2,6	−5,5	+0,7	+3,1

* net of accumulated losses

Investments

Additions to investments in affiliates comprise the purchase of further shares in the Kötitzer Ledertuch- und Wachstuch-Werke AG, Düsseldorf, plus an increase of capital stock in our Spanish subsidiary, Continental Industrias del Caucho SA, Madrid, by converting long-term loans to equity capital.

The higher figure for additions to investments in affiliates in the consolidated balance sheet is due to the takeover of the business of our former importer in Switzerland and to an increase in capital stock in our US marketing corporation. We have a financial interest of 100% in both corporations via an interim holding.

The long-term loans refer mainly to housing loans to our employees. In the case of interest-free receivables, they are adjusted to their present value or fully reserved.

Difference arising from consolidation

The difference contained in the consolidated balance sheet represents the balance between the parent company's book value of investments (DM 55,2 million) and the pro rata equity capital of the companies included in the consolidated balance sheet (DM 46,7 million). The amounts concerned are latent reserves in the balance sheets of the affiliates. The equity capital of 6 consolidated companies is below the book value and that of 4 corporations above it.

Inventories

As it was possible once again to reduce the quantity of raw materials and supplies, the book value has decreased despite increased cost of purchase. These inventories are valued at the lower of cost or market prices on the balance sheet date, with discounts and rebates deducted. The value of inventories with a limited commercial usefulness or overlong storage period is adjusted correspondingly. The increases in production and sales last year led to an increase in finished and unfinished products. Valuation was made as before at production costs including proportional factory overhead. Any inventory risks are also covered by adequate adjustments in value. Inventories have increased overall by DM 15,3 million (5,5%).

Receivables

Although accounts receivable arising from sales and services to foreign customers have increased considerably due to higher volumes of export sales than in the previous year, the book value has scarcely changed as receivables from domestic customers have decreased despite increased sales. In addition, the accounts receivable with the two new marketing corporations in Switzerland and the United States now to be accounted for as intercompany receivables. In the valuation we have taken account of foreseeable risks arising from merchandise receivables and bills receivable by individual adjustments in value and by reserves.

Accounts receivable with affiliates concern mainly the delivery of goods. There are also, however, claims from profit/loss transfer contracts, loans and other offsets. Long-term receivables amount to DM 14,9 million.

Capital and reserves

The Corona Beteiligungsgesellschaft mbH, Frankfurt/Main has informed us that it no longer has a financial holding of more than 25% in our capital stock.

The free reserve has been reduced to DM 37,5 million by the transfer of DM 55,5 million to offset the accumulated deficit shown in the balance sheet.

The untaxed reserve was to be reduced by an unbudgeted release of DM 2,1 million in addition to the budgeted release in accordance with the revenue act applying to developing countries, as the related loans for which the reserve was originally created were devalued in 1977. The reserve for property levy under the Equalization of Burden Act was used for a premature cancellation of the residual debt thereunder.

Accruals

The pension accrual has been calculated on the basis similar to the entry age normal method in accordance with actuarial principles. The addition to the accrual corresponds to the permissible allowance according to the provisions of the income tax law, the value in the consolidated balance sheet contains an adjustment arising from the revaluation in one subsidiary.

The other accruals have increased by DM 3,5 million to DM 83,0 million. This item covers warranty, tax and bonus liabilities, contributions to the employers' liability insurance association, risks arising from bills discounted and pending contracts together with other obligations arising from sales and services.

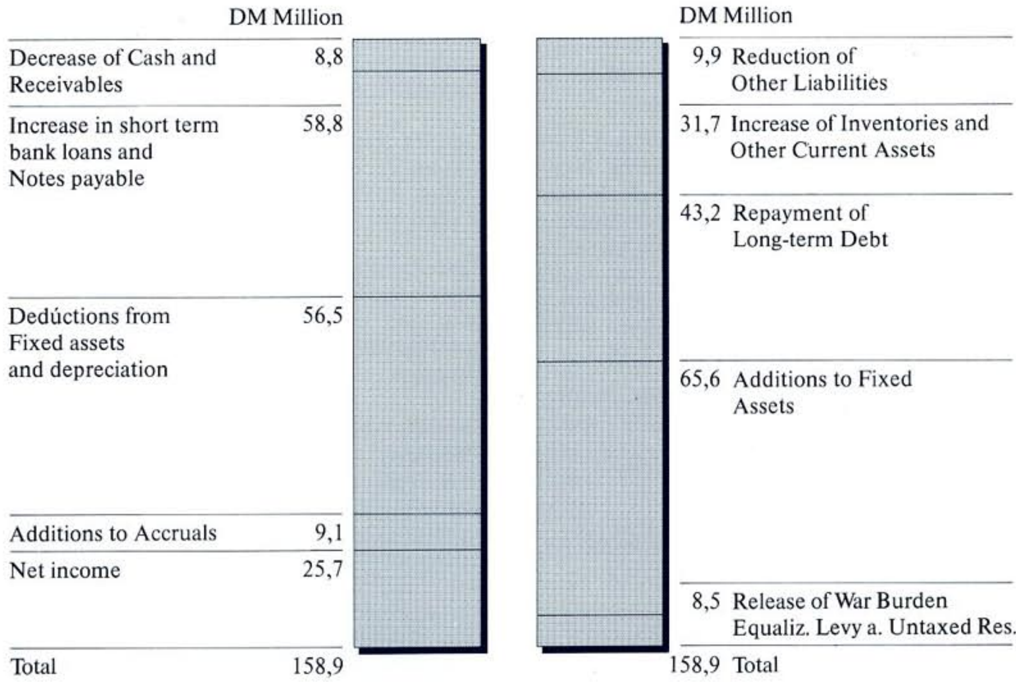
Liabilities

Liabilities with a term of at least 4 years have decreased by DM 43,2 million; short-term bank borrowings and bills payable on the other hand have risen by DM 58,8 million. As already stated, these changes are due to deliberate refinancing measures.

Contingencies

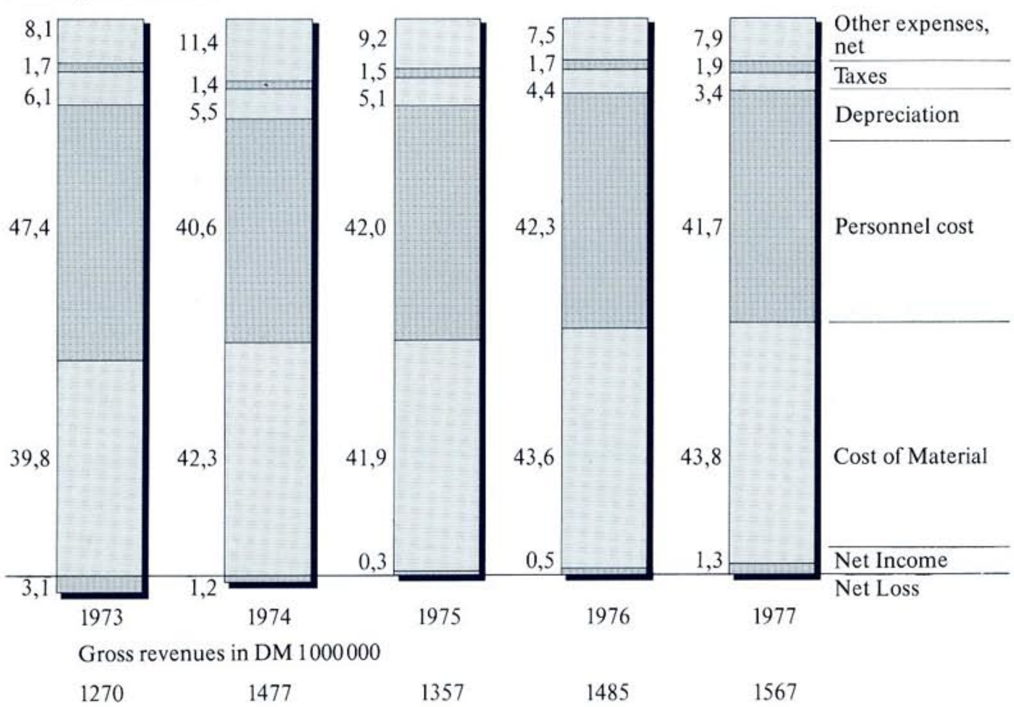
On the balance-sheet date, contingent liabilities from bills of exchange discounted amounted to DM 89,0 million (DM 87,2 million in 1976). Guarantees and warranties totalling DM 63,5 million concern mainly our subsidiaries and affiliates and have increased by approx. DM 6,8 million over the previous year. The outstanding payments due on contributions to capital and liabilities with cooperative associations amount to DM 3,1 million.

Source of Funds



Expense Structure

in % of gross revenues



Profit and Loss Statement

Sales (without VAT) have increased by 5,6 % as compared with 1976 to DM 1518,9 million, 25,2 % (25,1 % in 1976) being accounted for by exports.

The growth in consolidated sales was somewhat lower at 4,4 %, mainly caused by the somewhat weaker sales trend in the Vergölst group.

With the level of changes in inventories and work on capitalized company-produced assets being approximately the same as in the previous year, the gross revenues have increased correspondingly to the sales by 5,5 % to DM 1566,6 million. While costs of materials and supplies accounted for 43,8 % (43,6 % in 1976) of gross revenues the proportion of personnel costs and fringe benefits fell from 42,3 % to 41,7 % (see explanations on page 12).

The earnings from profit transfers have declined in comparison with 1976 as the Vergölst group showed a lower profit. The expenses from loss transfers relate to the Alsa Schuhbedarf GmbH, Ürzell.

Earnings from dispositions of assets have normalized. Extraordinary profits from the sale of real estate did not accrue in 1977.

The term Other Income covers not only proceeds from services, rents and leases but also cost reimbursements, commissions, released value adjustments and proceeds from written-off accounts receivable as well as investment grants.

The modification in the method of depreciation is explained on page 20.

Depreciation on current assets (inventories excluded) contains a value adjustment for loans to our subsidiary in Madrid. This expenditure is, however, partly offset by an extraordinary release of the untaxed reserve.

Despite the increase in the volume of business, interest expense has once again been cut by DM 2,7 million to DM 29,4 million and accounted for 1,9 % of gross revenues in 1977.

Corporation income tax was not incurred due to the loss carried forward. The higher profits led, however, to a rise in trade income tax. Expenditure on other operating taxes, on the other hand, has hardly changed.

The term Miscellaneous Expenses covers freight, repairs, advertising and agents' expenses, insurance premiums, rents, fees and other administrative expenditures. In 1977 this item followed the declining trend of the past years and expresses our unrelenting efforts to reduce expenses.

The compensation of the Executive Board totalled DM 3 279 292 for the year 1977; we paid DM 1 929 268 for former members of the Executive Board and their surviving dependents. Supervisory Board remuneration amounted to DM 33 000.

Hannover, March 1978

Continental
Gummi-Werke Aktiengesellschaft

The Executive Board

Carl H. Hahn	H. Norbert Dahlström	Werner Klein	Gerhard Lohauß
Julius Peter	Wilhelm Schäfer	Horst W. Urban	Hans Georg Wenderoth

Continental Gummi-Werke Aktiengesellschaft – Balance Sheet, December 31, 1977

Assets	January 1, 1977 DM	Additions DM	Reclassifications DM	Deductions DM	Depreciation DM	December 31, 1977 DM	December 31, 1976 DM 1000
Fixed Assets							
Property, Plant and Equipment							
Land							
with commercial plant and other buildings	182 962 536	557 202	210 474	96 878	8 992 383	174 640 951	182 963
with residential buildings	2 409 499	–	–	–	100 945	2 308 554	2 409
without buildings	70 800	–	–	–	–	70 800	71
Machinery	153 910 453	25 170 086	10 457 024	1 507 902	26 911 319	161 118 342	153 910
Furniture and equipment	25 694 018	18 438 495	3 003 451	497 921	17 508 497	29 129 546	25 694
Assets under construction and prepayments	20 880 560	17 998 198	– 13 670 949	–	294 672	24 913 137	20 881
	385 927 866	62 163 981	–	2 102 701	53 807 816	392 181 330	385 928
Investments							
Investments	116 304 001	2 415 427	–	139 575	–	118 579 853	116 304
Loans with a term of at least 4 years, thereof secured by mortgages DM 1 947 003	1 864 337	955 259	–	411 530	–	2 408 066	1 864
	504 096 204	65 534 667	–	2 653 806	53 807 816	513 169 249	504 096
Current Assets							
Inventories: Raw materials and supplies			DM	77 194 291			83 266
Work in process			DM	41 936 224			39 266
Finished products, goods for resale			DM	172 564 990			153 462
Services rendered, not yet billed			DM	624 603			992
					292 320 108		276 986
Other Current Assets							
Prepayments					857 401		227
Accounts receivable					166 333 069		167 732
due after one year			DM	355 370			
Notes receivable					3 175 750		1 887
rediscountable with the Federal Bank			DM	1 796 368			
Checks					5 311 353		5 855
Cash on hand, at Federal Bank and on postal checking accounts					2 699 692		2 730
Cash at banks					8 198 814		16 360
Due from affiliated companies					46 449 903		30 829
Other receivables (§ 89 AktG)					358 208		359
Other assets					7 002 680		6 516
						532 706 978	509 481
Prepaid Expenses							
Loan discounts					1 575 627		1 813
Other					553 634		610
						2 129 261	2 423
Accumulated Deficit						–	81 157
						1 048 005 488	1 097 157

Liabilities And Shareholders' Equity

		December 31, 1977 DM	DM	December 31, 1976 DM 1000
Share Capital (Common Stock)			270 000 000	270 000
Open Reserves				
Statutory reserve			65 451 393	65 451
Reserve for war burden equalization levy		5 503 347		7 777
Release		5 503 347		2 274
			–	5 503
Free reserves		93 000 000		
Release		55 500 000		
			37 500 000	93 000
Untaxed Reserves				
§ I sect. 1.2 Entwicklungsländer-Steuergesetz			970 417	3 958
Accruals				
Accrued pensions		98 719 354		92 382
Accruals for deferred maintenance		–		769
Other accruals		83 006 123		79 505
			181 725 477	172 656
Liabilities with Terms of at least 4 Years				
Bonds		90 000 000		100 000
thereof secured by mortgages	DM 90 000 000			
Loans and debentures		102 893 418		117 716
thereof secured by mortgages	DM 76 626 188			
Due to banks		139 741 414		158 101
thereof secured by mortgages	DM 241 127		332 634 832	375 817
Due within four years	DM 141 679 147			
Other Liabilities				
Trade payables		49 305 062		50 036
Notes payable		19 551 687		–
Due to banks		39 210 059		–
Advances		3 919 542		3 403
Due to affiliated companies		961 395		9 325
Other liabilities		46 763 418		48 008
			159 711 163	110 772
Unapppropriated Retained Income			12 206	–
Bills discounted with recourse	DM 89 030 468			
Guarantees	DM 32 114 358			
Warranties	DM 31 425 764			
			1 048 005 488	1 097 157

Continental Gummi-Werke Aktiengesellschaft – Profit and Loss Statement for the year 1977

	1977 DM	1977 DM	1976 DM 1 000
Sales	1 518 883 377		1 438 951
Change in inventories of products	+ 22 011 856		+ 22 939
		1 540 895 233	1 461 890
Overheads capitalized on construction of fixed assets		25 700 775	23 117
Gross Revenues		1 566 596 008	1 485 007
Raw materials and supplies used		685 822 111	647 733
Gross Margin		880 773 897	837 274
Income from profit and loss pooling agreements	7 514 418		9 824
Investment income	2 811 866		3 934
Income from long-term loans	297 865		318
Interest and similiar income	2 961 226		3 078
Income from disposal of fixed assets	1 547 443		9 074
Income from release of accruals.	2 154 777		438
Income from release of untaxed reserves	2 987 417		5 472
Other income	21 955 145		21 178
there of extraordinary . . . DM 4 899 406			
		42 230 157	53 316
		923 004 054	890 590
Wages and salaries	547 813 823		528 816
Social security contributions	87 107 768		83 333
Pensions and employees' welfare	17 884 568		16 418
Depreciation of fixed assets	53 807 815		65 788
Depreciation on current assets (excluding Inventories)	4 359 844		573
Losses from disposal of fixed assets	461 098		564
Interest and similiar expenses	32 313 120		35 157
Taxes			
a) on income profit and net worth . . . DM 29 611 772			
charged to subsidiaries . . . DM 777 560			
DM 28 834 212			
b) Other . . . DM 637 772			
	29 471 984		24 009
War burden equalization levy	5 606 188		2 585
Expenses from profit and loss pooling agreements	1 525 625		1 614
Other expenses	122 486 607		123 690
		902 838 440	882 547
Net income		20 165 614	8 043
carry forward:		20 165 614	8 043

	1977 DM	1977 DM	1976 DM 1 000
carried forward		20 165 614	8 043
Losses brought forward		81 156 754	91 474
Release of free reserves		55 500 000	
Release of reserve for war burden equalization levy		5 503 346	2 274
Unappropriated Retained Income (loss in 1976)		12 206	81 157

Continental Gummi-Werke Aktiengesellschaft
The Executive Board

According to our audit made in conformity with our professional duties the accounting and the financial statements comply with German law and the Company's statutes.

Berlin/Hannover, March 2, 1978

Deutsche Treuhand-Gesellschaft
Wirtschaftsprüfungsgesellschaft

Wolff
Wirtschaftsprüfer

Kirste
Wirtschaftsprüfer

Continental Gummi-Werke Aktiengesellschaft – Consolidated Balance Sheet, December 31, 1977

Assets			December 31, 1977 DM	December 31, 1977 DM	December 31, 1976 DM 1 000
Fixed Assets					
Property, Plant, Equipment and Intangible Assets					
Land					
with commercial plant			203 737 667		212 466
residential buildings			3 481 053		3 583
without buildings			233 510		455
Building on third parties' land			4 511 894		4 590
Machinery			173 533 068		166 553
Furniture and equipment			37 404 621		34 366
Assets under construction and prepayments			25 918 146		21 944
Intangible assets			483 186		87
				449 303 145	444 044
Investments					
Investments			113 399 318		103 933
Loans with a term of at least 4 years,			3 236 861		2 734
thereof secured by mortgages	DM	2 105 547		116 636 179	106 667
				565 939 324	550 711
Difference arising from Consolidation				8 494 880	7 609
Current Assets					
Inventories			356 003 553		340 113
Other Current Assets					
Prepayments			1 025 105		286
Accounts receivable			223 694 795		229 701
due after one year	DM	483 011			
Notes receivable			3 543 434		2 249
rediscountable with the Federal Bank	DM	1 943 845			
Checks			5 335 441		6 390
Cash on hand, at Federal Bank and on postal checking accounts			3 339 878		3 285
Cash at banks			8 517 157		16 836
Due from affiliated companies			19 408 303		12 571
Other receivables (§ 89 AktG)			516 271		550
Other assets			9 167 889		9 210
				630 551 826	621 191
Prepaid Expenses					
Loan discounts			1 786 050		2 103
Other			1 272 236		1 105
				3 058 286	3 208
Losses attributable to Minority Shareholders				-	27
Accumulated Deficit				2 043 204	84 353
				1 210 087 520	1 267 099

Liabilities And Shareholders' Equity		December 31, 1977 DM	December 31, 1977 DM	December 31, 1976 DM 1000
Share Capital			270 000 000	270 000
Open Reserves				
Statutory reserve		65 451 393		65 451
Reserve for war burden equalization levy		–		5 611
Free reserves		37 500 000		93 000
			102 951 393	164 062
Untaxed Reserves according to § 1 section 1, 2 Entwicklungsländer-Steuergesetz, § 74 EStDV and § 6 b EStG			2 456 517	5 479
General provision for bad debts			876 842	1 099
Minority Interests			3 930 067	5 193
Accruals				
Accrued pensions		124 550 166		119 267
Accruals for deferred maintenance		88 000		862
Other accruals		97 764 486		96 720
			222 402 652	216 849
Liabilities with Terms of at least 4 years				
Bonds		90 000 000		100 000
there of secured by mortgages	DM 90 000 000			
Loans and debentures		102 893 418		117 716
there of secured by mortgages	DM 76 626 188			
Due to banks		162 636 746		182 375
there of secured by mortgages	DM 5 564 696			
Other liabilities		284 931		373
there of secured by mortgages	DM 265 431			
			355 815 095	400 464
Due within four years	DM 153 293 898			
Other Liabilities				
Trade payables		63 612 312		66 060
Notes payable		56 628 677		34 673
Due to banks		70 314 405		34 207
Advances		4 087 039		6 454
Due to affiliated companies		15 552		3 613
Other liabilities		56 522 925		58 199
			251 180 910	203 206
Retained Earnings attributable to Minority Interests			474 044	747
War Burden Equalization Levy				
Present Value	DM 173 912			
Quarterly Instalments	DM 35 748			
Bills discounted with recourse	DM 70 126 969			
Guarantees	DM 32 125 017			
Warranties	DM 30 920 765			
			1 210 087 520	1 267 099

Continental Gummi-Werke Aktiengesellschaft – Consolidated Profit and Loss Statement for the year 1977

		1977		1976
		DM	DM	DM 1 000
Sales		1 858 124 712		1 778 838
Expenses not to be disclosed separately and net of change in Inventories of Products		1 736 931 858		1 670 824
			121 192 854	108 014
Investment income		2 172 586		3 441
Income from long-term loans		325 662		357
Interest and similar income		1 044 317		1 567
Reversal of prior years depreciation		114 424		–
Income from release of accruals		5 542 023		1 375
Income from release of untaxed reserves		3 028 405		5 494
Other income		25 751 940		34 126
			37 979 357	46 360
			159 172 211	154 374
Depreciation of property, plant, equipment and intangible assets		65 318 013		77 195
Depreciation of investments		36 090		247
Interest and similar expenses		33 452 307		36 451
Taxes				
a) on income, profit and net worth	DM 32 675 976			
charged to subsidiaries	DM 19 608			
	DM 32 656 368			
b) Other	DM 1 234 767			
		33 891 135		28 325
War burden equalization levy		6 020 314		2 859
Expenses from profit and loss pooling agreements		5 010		3
			138 722 869	145 080
Net income			20 449 342	9 294
Accumulated deficit at beginning of year			84 220 113	95 916
			63 770 771	86 622
Release of free reserves			55 500 000	–
Release of reserve for war burden equalization levy			5 610 676	2 318
Decrease in difference arising from consolidation			1 497 504	1 029
Addition to difference arising from consolidation			406 569	358
			1 569 160	83 633
Income attributable to Minority Interest			474 044	747
Loss attributable to Minority Interest			–	27
Accumulated deficit			2 043 204	84 353

Continental Gummi-Werke Aktiengesellschaft
The Executive Board

According to our audit made in conformity with our professional duties the annual consolidated financial statements comply with German law.

Berlin/Hannover, March 22, 1978

Deutsche Treuhand-Gesellschaft
Wirtschaftsprüfungsgesellschaft

Dr. Richter, Wirtschaftsprüfer
Wolff, Wirtschaftsprüfer