

2011 Extraordinary Shareholders' Meeting of Pfleiderer AG

Thursday, July 21, 2011

Speech by the Executive Board

Hans H. Overdiek, CEO of Pfleiderer AG

- Check against delivery -

Good morning, ladies and gentlemen. I welcome you - also on behalf of my colleagues on the executive board - to today's extraordinary shareholders' meeting.

In the minutes ahead, I want to describe the present situation of Pfleiderer AG in a little more detail and explain the restructuring concept to you. I am confident that it will enable us to restore the basis for a successful future of Pfleiderer.

The circumstances that brought us together here in Munich today are undoubtedly very painful for everyone involved. This certainly holds true for me personally. I wish to take this opportunity to reiterate what I had said at the shareholders' meeting in April:

I take full responsibility for my actions as the chief executive officer of this enterprise. Months ago, I had offered my resignation to the supervisory board. I am not one to cling to office at all costs. However, taking responsibility also means facing challenges in trying times. So I will do everything within my power to pave the way to the company's successful recovery for my successor, and to lead the enterprise until the new ownership structures and a successor have been designated.

In April, I had described to you in detail the causes of our company's crisis. Allow me to briefly recap these to start things off today.

We were clearly on track for further growth well into 2008. The objective of our acquisition strategy was to drive growth and minimize risk by way of regional and product diversification. Our revenues, and particularly our margins, took a positive turn. Of course, while charting a course for growth we also encountered operational and strategic problems that were intensified by the financial crisis.

Until this time, our investment decisions had been made under the assumption that we could finance these out of the cash flow. Then, however, the crisis hit in 2008, affecting not only us at Pfleiderer AG but also the entire global economy with a massive drop in sales volume and, consequently, sharply declining prices and margins.

Let me underscore this point by citing some figures: In the period from 2007 to 2010, revenue dropped from €1.8 billion to around €1.5 billion. This is more than 17%. However, the effect is even more dramatic when seen on the earnings side. From 2007 to 2009 alone, the prices in Western Europe for raw particleboards and fiberboards, for example, plummeted by about a third each, and some cases even by half. The cost of sales, that is the sum total of the costs of purchasing raw materials and fixed and variable manufacturing costs, climbed to almost 80% of revenue. As a result, EBITDA dropped accordingly, from €248.7 million in 2007 to €40.5 million in 2010 – this is less than one fifth!

But even more decisive for the debt situation was the sharp decline in operating cash flow.

It was under pressure not only from crisis-induced developments in sales volume and margins. Again, the financial crisis intensified our operational and strategic problems.

The key factors include the complexity of our internal structures, the regressive capacity utilization, and difficulties with some of our investments.

The decision to expand activities in North America, especially, was not crowned with success. The reason for this was that several underlying conditions had changed. Some were crisis-induced, such as exchange rate developments. Others were structural, for example, the problems in the run-up to investments. Consumer behavior in individual markets had also changed.

Low operating cash flow, combined with high investments, ultimately led to a drastic increase in debt and a clear deterioration of the financial situation. In said period, the net debt of the Pfeleiderer Group increased from about €618 million in 2007 to around €960 million in 2010.

Of course, we made every effort to counter this trend with all the means at our disposal.

From 2008 to 2010, we applied many measures throughout all departments and reduced costs by a nine-figure sum. The savings in freight, personnel, production, administration, and sundries alone came to a mid-eight-figure sum.

However, this was not enough to compensate for the massive decline in sales during the crisis years. Also, in this market environment, the rising cost of materials could only be absorbed by long-deferred price increases, and then only in part.

Very fast restructuring is necessary due to three factors:

Firstly, the liquidity position: The financing requirements for the current fiscal year amount to around €200 million.

Secondly, the current debt.

As part of our growth strategy, we had committed to a covenant that caps the company's debt at no more than three times EBITDA. This means that senior debt is to be roughly equivalent to three times the operating result. This covenant was reflected in our credit agreements. Even after the major acquisitions of Kunz and Pergo, our fiscal debt at the end of 2007 remained below this benchmark - specifically at 2.5 times EBITDA.

With onset of the crisis and the aforementioned effects – particularly with EBITDA decreasing by around €200 million - the Group's opportunities for securing outside financing were drastically curtailed: In the last three years, debt capacity shrank by more than half a billion euros.

Without financial restructuring and as a result of impairments and restructuring costs, equity amounted to around negative €390 million at the end of 2011.

Thirdly – and this is the decisive point: Without restructuring, the company's very existence is at imminent risk.

The earnings situation prevented us from fulfilling the banks' credit terms at the end of the year. This would have entitled the banks to immediately call in their loans and sell their securities. That would, in fact, have been the end - for the company and for your investment.

We succeeded in negotiating a standstill agreement with our creditors, and working out a restructuring concept. With the help of the management consulting firm Roland Berger, we were able to substantiate the company's capacity for recovery and convince the banks of the restructuring concept's viability. A copy of Roland Berger's confirmation of restructuring feasibility is available for inspection at the speaker registration desk and on our website.

After lengthy negotiations, the creditors finally agreed to waive a significant share their claims and provide new funds on the condition that the holders of hybrid bonds and you, ladies and gentlemen, contribute to the company's restructuring. As you are aware, the holders of the hybrid bond had voted in favor of the waiver at the creditor meeting convened for this purpose on June 20. In return, holders of the hybrid bond will be entitled to acquire up to 4% of Pfeleiderer AG's equity after the planned capital increase has been carried out.

Now I would like to explain to you in detail the benchmarks of the restructuring concept. The proposed actions are structured in a financial and a strategic and operational restructuring concept, respectively.

The short-term priority is clearly to secure liquidity. It is important that we gain room to maneuver for the operating business.

In order to achieve a turnaround, we must also secure the company's long-term financial stability.

To this end, the following has been arranged with the financing banks:

The creditors agree to waive their claims to financial liabilities in the amount 40% of utilized credit lines, plus part of the accumulated interest and fees. With receivables totaling €763 million on May 5, 2011, the creditors are therefore waiving their claims to around €305 million in receivables, plus about €75 million in accumulated interests and fees.

On the basis of the new financing structure, the interest burden will be reduced by €52 million in 2011 and another €30 million in 2012. Exempted repayments amount to €97 million this year and another €102 million in 2012. Fees will also be reduced by around €10 million on balance.

The financial restructuring calls for – alongside the capital increase which I will discuss in a moment – the creditors to also grant an additional super senior credit line of €100 million. Half of it is to be paid back in the form of an extraordinary redemption. Given a maximum capital increase in 2011, the available liquidity will increase by more than €300 million to around €92 million overall.

As you can gather, the creditors are not only relinquishing considerable claims, they are also supporting our efforts by providing further funding for the restructuring of Pfeleiderer AG. The bondholders too had waived all their rights to bond claims at the aforementioned creditor meeting, thereby providing further debt relief for the Pfeleiderer Group of around €330 million. In return, they will receive about 4% of share capital after the capital increase. But as I said earlier, the waiver is subject to the condition that you, ladies and gentlemen, also waive your claims. This is why the executive board and the supervisory board today are asking you to approve a capital cut.

I had informed you in April about this capital cut as part of the proposed restructuring concept. In recent weeks, we negotiated intensively with the creditors concerned to work out the details and terms of the restructuring, which I would like to now address.

As a result of the proposed capital cut, shareholders will initially retain only around 0.8% of current equity. However, they have the option of increasing their share of equity up to around 16% as part of a capital increase against a cash contribution of up to €40 million. This means they can subscribe 20 new shares for every amalgamated share. A total of 7.8 million shares are to be offered to the old shareholders at a price of €5.11 each.

To restore a sound equity base after the capital cut, up to € 100 million are to be raised by way of a cash capital increase, with up to €40 million to be raised by other third parties and the old shareholders of

Pfleiderer AG, and up to €60 million by senior secured creditors. This cash injection of up to €100 million is to be guaranteed by senior secured creditors. These creditors are also prepared to provide a further first-lien loan called a super senior credit of up to €40 million to ensure the projected injection of funds of up to EUR 100 million is guaranteed in any event. They would thereby cover that part of the capital increase which is not raised by the shareholders or other third parties.

The creditors are to hold at least 80% of Pfleiderer AG's increased equity upon completion of the capital increase. This percentage may increase to the extent that neither the old shareholders nor third parties subscribe to their allotted shares in the capital increase. The terms of these capital measures were negotiated among the creditor groups concerned. The creditors' substantial shareholdings reflect not only the cash investment, but also the waiver of claims as well as the extension of further credit lines.

Next to those creditors who will participate directly in the capital increase, there are creditors who will waive 40% of their claims but do not wish to participate directly, instead receiving options to acquire shares a later date. They will be afforded the opportunity to subscribe to a bond with warrants. Attached to this bond are negotiable options granting the right to acquire, within a certain period, shares at a minimum purchase price of €7.49 each.

Now I would like to explain to you what prompted us to opt for this particular financial restructuring concept.

The creditors and the company worked out and intensively negotiated this restructuring concept. Without the shareholders' approval of these resolutions, the holders of the hybrid loan will not waive their rights, the creditors will not waive their claims, and the remaining measures set forth in the restructuring agreement will not be implemented. At this stage I should like to state clearly once again that if the restructuring agreement is not implemented, the current standstill agreements will terminate, the current loans will be due for redemption, and the company will be at risk of imminent insolvency.

In the event of the company's insolvency, the shareholders would be at risk of forfeiting their entire investment.

The business rationale underlying the restructuring agreement is that the alternative investors are not prepared to waive senior secured claims, which take precedence over the hybrid bond and current equity, and to invest new share capital in the company if this restores value to the hybrid bond and outstanding shares, which in view of a looming insolvency are presently, apart from a certain hope value, worthless.

Consequently, the alternative investors are only prepared to relinquish their claims and inject new share capital if the shareholders approve the proposed measures.

This means that the exclusion of subscription rights for the cash capital increase and for bonds with warrants is necessary to enable the restructuring concept to be implemented. If for the cash capital increase the old shareholders were granted a subscription right under the same terms, the alternative investors could not be guaranteed a fixed equity interest. This, however, was a prerequisite for their participation in the capital increase and the restructuring loan. And this loan is indispensable to prevent insolvency. In view of the company's situation, interim credits loans from lenders other than the existing creditors were unattainable because our credit rating had been downgraded. Other measures such as selling holdings or assets could not have been implemented fast enough to achieve the necessary liquidity at short notice.

Without the possibility and guarantee of a fixed equity interest, the alternative investors would have no assurance of receiving fair consideration for waiving their claims.

Allow me to now address the different subscription prices for shares within the framework of the capital increase. I would like to answer the question of why the new share is offered to you at €5.11 while the alternative investors can purchase it for around €1.37.

The subscription price of € 1.37 is the result of negotiations with the creditor groups concerned who wish to participate in the restructuring. The parties also took into account the waiver of claims. It stands to reason that a price negotiated among third parties is appropriate and fair.

The executive board proceeded as follows to determine if this price is appropriate pursuant to Section 255, Paragraph 2 of the German Stock Corporation Act: The executive board ascertained the company's value on the basis of a business plan developed by it with Roland Berger Strategy Consultants following a successful financial restructuring; that is, after the proposed capital measures and waiver of claims have been carried. The intrinsic value per share was extrapolated from this value assigned to the company. This intrinsic value per share was then compared with the consideration to be paid by the alternative investors. This includes the cash payment of around € 1.37 per new share, the waiver of claims by the alternative investors, and the contribution of the hybrid bond to the company. The latter contribution must also be credited to the alternative investors.

The subscription price fixed in the resolution on the capital increase of €1.37, plus the value of the waiver of claims by the alternative investors, plus the value of the hybrid bond amounts to a consideration exceeding the intrinsic value per share. The executive board has had this valuation and the appropriateness of the subscription price confirmed in a Fairness Opinion by Duff & Phelps.

This evaluation shows that the price of €5.11 at which around 7.8 million new shares are to be offered for purchase to the old shareholders is still less than the intrinsic value of the new shares. This means that

the old shareholders also have the opportunity, by acquiring new shares at a price of €5.11, to benefit from the value that the restructuring adds to the company.

As you can gather from the invitation to the shareholders' meeting, the financing concept also calls for the issue of a bond with warrants. Those banks that participate in the waiver of claims, but not however in the share capital, are entitled to it. To ensure that they are also afforded the potential for value gains, these bonds can be converted into shares – however, only at an exercise price starting at around €7.49. This also reflects a certain share price expectation on the part of banks.

Now I would like to explain our operative restructuring concept to you. It consists of four elements:

Firstly, we are investigating the sale of the North American business in order to stop the losses and reduce complexity in the company. Our goal is to clearly focus on our core markets in Europe. We aim to use the proceeds from the sale of the North American business to reduce our debt.

Secondly, we are restructuring our Business Center West / Flooring Europe to restore stable cash flows in the region. Significant parts of the restructuring have already been implemented in the Business Center Western Europe. Realized measures include the reduction of our plants in Germany from eight to five. Better capacity utilization enabled us to improve margins in the first quarter of 2011. Although these decisions were very painful for everyone involved, we would not have achieved sufficient production capacity utilization without these capacity shutdowns.

Thirdly, we are continuing our efforts to increase the efficiency of indirect support functions, for example, by standardizing our IT infrastructure.

Fourthly, we are investigating the possibility of completing the Novgorod II works already under construction in Russia in order to continue participating in Eastern European growth markets. The furniture market in Eastern Europe promises estimated growth rates of about 4% in the period from 2010 to 2013. Market observers also expect demand for particleboard to increase 5% and demand for medium-density fiberboard 7% by 2013. This is why we are aiming to have our Polish plants operating at full capacity and for their profitability to return to a pre-crisis level.

The operational restructuring of the Pflaederer Group is in full swing and the results of the first three months show that these measures are indeed taking effect. The Group's revenue in the first quarter of the current fiscal year was increased by about 10% to more than €390 million. The earnings performance in this period also gives us confidence. We were able to achieve EBITDA of €20 million.

We expect that upon completion of the restructuring, we will again achieve operating margins in line with the industry average of the best competitors.

Ladies and gentlemen, Pfeiderer AG will only survive as a whole if all the proposed measures I have just described are approved and carried out. To put it clearly, this means that the entire plan cannot be realized without your approval.

For us on the executive board, there has never been any doubt that our company is capable and worthy of being turned around, and I am grateful that everyone involved is doing their part so we can put Pfeiderer back on a successful track - our employees at home and abroad, our suppliers, our customers, our creditors, our bondholders, and of course you, our shareholders.

I would like to take this opportunity to thank you all wholeheartedly - also on behalf of my colleagues on the executive board - for your support in this very difficult phase for our company.

Thank you for your attention.