At the beginning of 2007 we integrated the management of all our sales and service activities for the German consumer market. The focus is on seeing things more from the customer's perspective. We are consistently concentrating on the most important aspect in our market: our customers, their needs and their desires.

GROUP MANAGEMENT REPORT

Deutsche Telekom Group management report.

Net revenue for the Group up 2.9 percent year-on-year to EUR 61.3 billion; proportion of Group revenue generated outside Germany increased from 42.6 percent to 47.1 percent // Group EBITDA adjusted for special factors lower by 6.2 percent to EUR 19.4 billion, unadjusted EBITDA down by 18.9 percent to EUR 16.3 billion // Profit after income taxes adjusted for special factors decreased from EUR 5.1 billion to EUR 4.3 billion, profit after income taxes unadjusted for special factors decreased from EUR 6.0 billion to EUR 3.6 billion // Free cash flow before dividend payments down from EUR 5.7 billion to EUR 2.4 billion, including cash outflows of EUR 3.3 billion for the purchase of FCC licenses // Proposed dividend of EUR 0.72 at the same high level as prior year

Number of mobile customers, including newly acquired companies, grows to 106.4 million // Strong DSL growth: Broadband lines increased by 3.2 million, including DSL resale, to 11.7 million within and outside Germany // Business Customers strategic business area wins major new contracts with incoming new orders up by 3.8 percent to EUR 14.1 billion

Net revenue continues to grow.
For Deutsche Telekom, the 2006 financial year was marked by rapid technological change and tough competition in the telecommunications industry. These developments were driven by two opposing trends: The international sales markets of Deutsche Telekom enjoyed favorable development. This is especially true for the key market in the United States. In the domestic markets, both slower growth rates and an accelerated price decline in the telecommunications market are placing a burden on business.

In total, net revenue rose by 2.9 percent year-on-year to EUR 61.3 billion. The contribution to net revenue generated internationally was EUR 28.9 billion, or 47.1 percent. The decisive factors behind the development of revenue were, on the one hand, continued customer growth at T-Mobile USA and on the other, revenue generated by the subsidiaries gedas, tele.ring and PTC totaling EUR 1.2 billion were included for the first time. Domestic revenue, in contrast, declined from EUR 34.2 billion to EUR 32.4 billion as a result of strong competitive and price pressures.

Group EBITDA decreased in the reporting year by around EUR 3.8 billion or 18.9 percent to EUR 16.3 billion. It was negatively affected by special factors amounting to around EUR 3.1 billion. Expenses for staff-related measures had the greatest impact here (EUR 2.8 billion). Adjusted for special factors totaling EUR 3.1 billion, EBITDA decreased from EUR 20.7 billion to EUR 19.4 billion.

Profit after income taxes decreased year-on-year by EUR 2.4 billion to around EUR 3.6 billion. The major factor contributing to this development – in addition to EBITDA – was the loss from financial activities. Changes in income taxes, in particular, had a favorable effect on profit after income taxes. Adjusted for special factors, profit after income taxes for the reporting period amounted to around EUR 4.3 billion compared with EUR 5.1 billion in the prior year.

Besides the decrease in operating activities, the decline in free cash flow to EUR 2.4 billion is mainly attributable to the increased volume of investment, mainly as a result of the purchase of additional FCC licenses at T-Mobile USA for EUR 3.3 billion.

For the 2006 financial year, the Board of Management proposes a dividend of EUR 0.72 per share. The dividend will thus remain at the level paid out in the previous year.

The merger of T-Online International AG into Deutsche Telekom AG, which had been approved in 2005, became effective upon entry in the commercial register on June 6, 2006. The merger has brought the Broadband/Fixed Network strategic business area, which consists of T-Com and T-Online, a decisive step closer to an improved structure. Now that the merger has become effective, the Broadband/Fixed Network business area is broken down for reporting purposes into its domestic and international segments.

Mobile Communications remains the key growth driver.
In 2006, the Mobile Communications strategic business area was again the Group's growth driver. The T-Mobile group substantially increased both its revenue and its customer base. The first-time consolidation of tele.ring and of the Polish company PTC was a significant factor.

T-Mobile USA was again the most successful T-Mobile company with 3.4 million net additions. T-Mobile USA had a total of 25 million customers at the end of the year. In the reporting year, T-Mobile Deutschland recorded 1.4 million net additions, increasing its customer base to a total of 31.4 million. This success is mainly due to intensive marketing activities to win customers. For example, one success story was the marketing of calling plans with inclusive minutes (Relax calling plans). In the United Kingdom, T-Mobile UK (including Virgin Mobile) added around 0.9 million new customers. New calling plans such as Flext also contributed significantly to this increase. Customer numbers at T-Mobile Czech Republic also developed satisfactorily. In Austria, the number of customers increased significantly as a result of the acquisition of tele.ring. The major Eastern European mobile communication companies in Hungary, Slovakia, Croatia, Montenegro and Macedonia recorded appreciable growth of 0.8 million to over 10 million mobile customers in total. PTC in Poland has been fully consolidated since November 2006. As of the end of 2006, this subsidiary had 12.2 million customers.

T-Mobile USA took part in a spectrum auction held by the Federal Communications Commission (FCC) in the United States and purchased spectrum worth EUR 3.3 billion. This spectrum forms the foundation for T-Mobile USA to expand its customer base in the U.S. market and introduce innovative products on the basis of new technology.

Strong DSL growth in the Broadband/Fixed Network strategic business area.

Business development in the Broadband/Fixed Network strategic business area continued to be driven primarily by the dynamic growth of the broadband market. The number of broadband customers increased in 2006 in terms of both lines and rates:

The number of broadband lines in Germany and abroad (including Eastern and Western Europe) increased by around 36 percent to 11.7 million (2005: 8.6 million).

In Germany, the business area benefited from the general buoyancy of the broadband market. The number of customers also increased as a consequence of integrated all-inclusive offers of voice telephony, broadband Internet and TV entertainment (single-, double-, and triple-play packages) and new service offerings. A total of around 10.3 million (2005: 7.9 million) DSL lines provided by T-Com were in operation in Germany at the end of 2006, 2.4 million more than at the end of the previous year.

Nevertheless, competition in the broadband market continued to intensify in 2006. A consequence of this was a considerable drop in prices for ISP rates and, toward the end of the year, for complete packages. A characteristic feature of the entire broadband business was the entry into the market of an increasing number of European telecommunications companies and local loop operators.

T-Com benefited from dynamic market growth in particular in its DSL resale activities and the marketing of high bit rate unbundled subscriber lines. The number of DSL resale lines increased by 1.6 million year-on-year to 3.2 million.

Key financial figures for the Deutsche Telekom Group

millions of €	2006	2005	2004
Net revenue	61,347	59,604	57,353
Of which: international revenue	28,887	25,421	22,612
EBITDA [a]	16,321	20,119	19,392
EBITDA (adjusted for special factors) [a]	19,434	20,729	19,620
Profit after income taxes [b]	3,574	6,021	2,018
Profit after income taxes (adjusted for special factors) [a, b]	4,275	5,131	4,159
Net profit [b]	3,165	5,589	1,594
Net profit (adjusted for special factors) [a, b]	3,850	4,668	3,680
Shareholders' equity [b]	49,670	48,599	45,512
Net debt [c]	39,555	38,639	39,913
Free cash flow (before dividend payments) [d]	2,389	5,729	10,310
Employees (annual average)	248,480	244,026	247,559

[a] Deutsche Telekom defines EBITDA as profit/loss from operations before depreciation, amortization and impairment losses. For a detailed explanation of the special factors affecting EBITDA and adjusted EBITDA, as well as special factors affecting profit/loss and the adjusted profit/loss after income taxes and net profit, please refer to the "Development of business" section.

[b] Prior-year comparatives have been adjusted to reflect the change in policy in accounting for actuarial gains and losses. For further details, please refer to Note 29 in the consolidated financial statements.

[c] The "net debt" indicator is used by senior operating decision-makers at Deutsche Telekom to manage and control debt. Although many of Deutsche Telekom's competitors use this measure, its definition may vary from one company to another, however. For detailed information, please refer to the "Development of business" section.

[d] Deutsche Telekom is of the opinion that the "free cash flow (before dividend payments)" indicator is used by investors as a measure to assess the Group's net cash from operating activities after deduction of cash outflows for investments in intangible assets (excluding goodwill) and property, plant and equipment, in particular with regard to subsidiaries, associates and joint ventures, and the repayment of liabilities. "Free cash flow (before dividend payments)" should not be used to determine the financial position of the Group. There is only limited comparability between Deutsche Telekom's definition of free cash flow and methods of calculating this measure and similarly designated measures and disclosures of other companies. For detailed information, please refer to the "Development of business" section.

Since the merger of T-Online International AG into Deutsche Telekom AG, the Broadband/Fixed Network strategic business area has been able to offer fully integrated packages for voice and Internet communication. Following the launch of the complete packages in mid-September, T-Com gained 563,000 new broadband customers in the fourth quarter of the year, the highest quarterly growth in DSL since the technology was introduced. With the new rates, T-Com has increasingly succeeded in winning over formerly pure voice telephony or narrowband Internet customers to broadband technology.

T-Com entered the triple-play age in Germany in August: Using T-Com's VDSL network, customers in ten German conurbations now receive top-quality voice communication, Internet access, and Internet Protocol TV (IPTV) through a single line. In time for the soccer season, T-Com opened the doors to the new world of multimedia applications by launching "Bundesliga auf Premiere powered by T-Com," the IPTV broadcast of Bundesliga soccer games by pay TV operator Premiere. The second half of the year saw the introduction of the first triple-play packages on the market – not only in Germany but also in Eastern and Western Europe. In Western Europe, the launch of triple-play products in France and the further expansion of its proprietary infrastructure helped T-Com to capitalize substantially on the growth of this broadband market as well. The number of broadband lines in operation in Deutsche Telekom's own networks in Western Europe increased fivefold to 445,000 and by 424,000 in Eastern Europe to 992,000 at the end of 2006. In total, the number of broadband lines Deutsche Telekom operates outside Germany, i.e., in Western and Eastern Europe, more than doubled to 1.4 million.

The further expansion of the DSL rate customer base continued just as successfully as the development in the field of broadband lines. The number of DSL rate customers climbed by as much as 45 percent to a total of 8.0 million. Compared with the previous year, the DSL rate customer base in Germany grew by 1.8 million to 6.3 million. T-Com recorded strong growth in the fourth quarter in particular after introducing the complete packages. Overall, T-Com attracted more ISP rate customers than broadband line customers, an improvement in the customer base as the number of DSL lines with third-party ISP services is clearly in decline.

In the verticals sector – consumer brands that are specifically targeted at young growth markets – Musicload continued its growth trend as one of the leading providers of online music downloads. In September, Musicload launched a new subscription model that gives customers access to more than 1.8 million tracks for a monthly charge. For many users, the subscription solution represents an attractive alternative to purchasing individual tracks on the Internet. Gamesload's offering now includes more than 440 download games and over 120 games in the games flat rate. Musicload and Gamesload are among the leading German online platforms in their respective target groups. In November 2006, T-Com launched Softwareload, a new download portal for software programs. Softwareload provides a selection of more than 17,000 titles covering a range of applications.

The number of narrowband lines in Germany and abroad fell by 5.3 percent to 39.0 million in the course of the year (2005: 41.2 million). In Germany, the number of narrowband lines decreased by 5.7 percent year-on-year to 33.2 million (2005: 35.2 million). The main reasons for this decrease are customer churn in favor of fixed-network competitors as well as increasing substitution by mobile communications and cable network operators. At 9.0 million, the total number of T-ISDN lines decreased by a disproportionately high 8.2 percent year-on-year (2005: 9.8 million). This is attributable in part to DSL customers switching from T-ISDN to an analog T-Net line.

The development of call minutes in Germany experienced contrasting trends in 2006. By successfully marketing calling plans, T-Com increased minutes loyalty for all call types (local, national, international, and fixed-to-mobile). The number of calling plan customers[1] was 16.5 million at the end of the reporting period, representing a penetration rate[2] of almost 50 percent. In the course of the year, overall minutes loyalty[3] increased by 4.7 percentage points to a total of 68.4 percent. T-Com has therefore managed to defend itself against competitors' call-by-call and preselection offers. However, in spite of the positive development of call minutes retention, the absolute number of call minutes in T-Com's network continues to decline, due to the ongoing loss of lines and the effects of voice over IP and fixed-mobile substitution, for example.

Business with resellers (wholesale services) also saw diverging trends in 2006: Interconnection business declined due to increasing direct network interconnection between competitors, price reductions for interconnection, and losses of call-by-call and preselection minutes. This contrasted with sharp increases in the number of unbundled subscriber lines to 4.7 million (2005: 3.3 million) and in DSL resale lines to 3.2 million (2005: 1.6 million). Overall, business in the area of wholesale services continued to be subject to considerable regulatory intervention. Moreover, price reductions for subscriber lines and DSL resale products in particular had a negative impact. In its business with international network operators (International Carrier Sales & Solutions business), which is affected by price erosion, T-Com focused on high-margin services.

[1] Calling plans including PSTN rate options from the new "3x3 complete packages" and VoIP flat rates.
[2] PSTN calling plans (excluding VoIP) to narrowband lines.
[3] T-Com's average market share (local, national, international and fixed-to-mobile) based on the overall traffic generated in the T-Com PSTN network.

Business Customers strategic business area increases the level of new orders despite difficult market environment.
In the reporting year, the Business Customers strategic business area was exposed to increasingly intense competition, continued consolidation, as well as a huge slump in prices in the traditional telecommunications business. Nevertheless, new orders rose by a total of 3.8 percent year-on-year due to new contracts. Total revenue amounted to EUR 12.6 billion in the reporting year, down by just 1.8 percent. One of the principal reasons for this was the decline in revenues from the telecommunications services segment – for both multinational business customers in the Enterprise Services business unit and medium-sized customers in the Business Services unit. Furthermore, the downturn in intragroup revenues from services for PC workstation systems also made itself felt.

By contrast, international business performed very positively. In total, T-Systems recorded an 18.2-percent revenue increase in this sector compared to the prior year's figure. This growth was primarily due to the integration of gedas AG in 2006.

The volume of business with companies outside the Deutsche Telekom Group stabilized and remained at the prior-year level. Primary factors for this success included business with services for PC workstations and the development and integration of software systems in the Enterprise Services unit. The Business Services unit, which serves small and medium-sized enterprises, continues to lead the German market. The unit was able to increase its revenue from IT business by as much as 53.6 percent compared with the previous year. This positive development was unable to fully offset the decline in revenue in the traditional telecommunications business, however.

Growth was also driven by business with IP-based communications solutions. In total, however, the positive developments were not yet able to compensate for the downturn in traditional data communications services.

Group organization.

Merger of T-Online International AG into Deutsche Telekom AG effective since June 6, 2006 // KfW Bankengruppe sells Deutsche Telekom shares to Blackstone Group // Acquisition of gedas and tele.ring completed // PTC fully consolidated for the first time // Group's top management reorganized

Deutsche Telekom is an integrated telecommunications provider. The Group offers its customers worldwide a comprehensive portfolio of state-of-the-art services in the areas of telecommunications and IT. In 2005, the Group realigned its structures and processes with the three main growth sectors of the industry: Broadband/Fixed Network, Mobile Communications, and Business Customers.

Organizational structure and business activities.
The **Mobile Communications** strategic business area comprises all activities of T-Mobile International AG & Co. KG as well as other mobile communications activities of Deutsche Telekom in Central and Eastern Europe. T-Mobile is represented in Germany, the United States, the United Kingdom, the Netherlands, Austria, the Czech Republic, Hungary, Slovakia, Croatia, Macedonia, and Montenegro. The business area also has a subsidiary in Poland (PTC), which has been fully consolidated since November 2006. All T-Mobile entities offer digital mobile voice and data services to consumers and business customers. T-Mobile also sells hardware and other terminal devices in connection with the services offered. In addition, T-Mobile services are sold to resellers and to companies that buy network services and market them independently to third parties (mobile virtual network operators, or MVNOs).

The **Broadband/Fixed Network** strategic business area offers consumers and small business customers state-of-the-art infrastructure for traditional fixed-network services, broadband Internet access, and multimedia services. This strategic business area also conducts business with national and international network operators and with resellers (wholesale including resale). In addition, it provides wholesale telecommunications services for Deutsche Telekom's other strategic business areas.

When the merger of T-Online International AG into Deutsche Telekom AG became effective on June 6, 2006, T-Online ceased to report as a separate unit. However, in the market T-Online continues to be managed as a product brand. For reporting purposes, Broadband/Fixed Network has been broken down into its domestic and international segments since the second half of 2006. The Scout24 group is reported in the domestic segment as its parent company has its registered office in Germany.

Outside of Germany, the Broadband/Fixed Network strategic business area is represented in both Western and Eastern Europe: in France, Spain, Portugal, Austria, Switzerland, Hungary, Slovakia, Croatia, Macedonia, Montenegro, Bulgaria, and Romania.

In Germany, Broadband/Fixed Network operates one of the world's most modern and powerful infrastructures for fast, secure information exchange – an infrastructure that includes more than 200,000 kilometers of optical fiber and an IP network operating with forward-looking multi-protocol label switching (MPLS) technology.

The business area has expanded the network infrastructure for the broadband communications market of the future in large parts of Germany. As of the end of 2006, DSL technology for fast Internet access was available to almost 93 percent of all T-Com access customers. In addition to further expanding the T-DSL network, Broadband/Fixed Network increased the performance of broadband Internet access. In ten conurbations, it has used VDSL technology to build an ultra-modern optical-fiber infrastructure for high-speed Internet access. The lines offer transfer rates of up to 50 megabits per second (Mbit/s). By the end of 2006, around 6 million households in the ten conurbations were accessible via the high-speed network. Outside the high-speed coverage areas, T-Com is also increasing the transfer rates for T-DSL customers. The ADSL2+ technology used gives customers bandwidths of up to 16 megabits per second.

T-Systems is Deutsche Telekom's business customers segment. The **Business Customers** strategic business area is divided into two business units: T-Systems Enterprise Services, which supports around 60 multinational corporations and large public authorities, and T-Systems Business Services, which serves around 160,000 large and medium-sized enterprises. T-Systems is represented by subsidiaries in over 20 countries, primarily in Germany and Western Europe (France, Spain, Italy, the United Kingdom, Austria, Switzerland, Belgium, and the Netherlands).

As a service provider, T-Systems offers its customers a full range of information and communication technology (ICT) from a single source. It develops integrated ICT solutions on the basis of its extensive expertise in these two areas. For its key accounts, T-Systems develops and operates infrastructure and industry solutions. The business area also offers international outsourcing and takes over entire business processes (business process outsourcing), such as payroll accounting. Its offering for small and medium-sized enterprises ranges from low-cost standard products through to high-performance IP-based networks and the development of complete ICT solutions.

T-Systems' vertical, sector-specific services require in-depth knowledge of the industry and of the individual customer. The company serves the public sector and the telecommunications and automotive industries with vertical solutions along the entire value-added chain. T-Systems is also approaching further industries – with select, successful solutions. These include the areas of health, travel, transport, logistics, finance, aviation, and defense. Its extensive expertise in these sectors allows T-Systems to offer its customers the right balance of tailored and standardized services, thereby generating flexibility benefits in terms of quality, time, and cost.

In addition to the three strategic business areas, the organizational structure of the Deutsche Telekom Group also includes **Group Headquarters & Shared Services,** which comprises all Group units and subsidiaries that cannot be allocated directly to the strategic business areas. Group Headquarters is responsible for strategic management functions across the business areas. All other operating functions not directly related to the strategic business areas' core business are now the responsibility of Shared Services. These consist of the Real Estate Services unit, whose activities include the management and administration of Deutsche Telekom AG's real estate portfolio; DeTeFleetServices GmbH, a full-service provider of fleet management and mobility services; and Vivento, which manages surplus staff and employee placement and creates employment opportunities, including in its own business lines. Shared Services primarily has activities in Germany. Real Estate Services also has operations offering facility management services in Hungary and, since June 2006, in Slovakia. The main Shared Services subsidiaries include DeTe Immobilien Deutsche Telekom Immobilien und Service GmbH, GMG Generalmietgesellschaft mbH, DFMG Deutsche Funkturm GmbH, PASM Power and Air Condition Solution Management GmbH & Co. KG, DeTeFleetServices GmbH, Vivento Customer Services GmbH, and Vivento Technical Services GmbH. At the beginning of 2006, Deutsche Telekom AG reduced its interest in Sireo Real Estate Management GmbH from 51 percent to 25.1 percent.

Legal structure of the Deutsche Telekom Group.
Deutsche Telekom AG, Bonn, is the parent of the Deutsche Telekom Group and also its largest operating company. Its **shares** are traded on several stock exchanges, including Frankfurt, New York, and Tokyo. At December 31, 2006, 68.3 percent of the shares were in free float (2005: 62.51 percent), 14.83 percent were held by the Federal Republic of Germany (2005: 15.40 percent), and 16.87 percent were held by KfW Bankengruppe (2005: 22.09 percent). Accordingly, the shareholding attributable to the Federal Republic amounted to 31.70 percent (2005: 37.49 percent).

The change in the shareholdings over the previous year is principally attributable to the reduction in the interest held by KfW Bankengruppe resulting from the sale of a package of shares to the private investment company Blackstone Group in April 2006. The share held by The Blackstone Group totaled 4.39 percent at December 31, 2006. The Blackstone Group agreed with KfW Bankengruppe to lock up its holding for at least two years. In addition, KfW Bankengruppe has agreed to a one-year lock-up with respect to further sales of its shares in Deutsche Telekom.

As of December 31, 2006, the **share capital** of Deutsche Telekom AG totaled approximately EUR 11,164 million and was composed of some 4,361 million no par value registered ordinary shares. Each share entitles the holder to one vote. The voting rights are nevertheless restricted in relation to the treasury shares (around 1.9 million as of December 31, 2006) and the trust shares (around 21.5 million as of December 31, 2006). The trust shares are connected with the acquisition of VoiceStream and Powertel in 2001. As part of this acquisition, Deutsche Telekom issued new shares from authorized capital to trustees for the benefit of holders of warrants, options, and conversion rights, among others. As regards the shares issued to trusts, the trustee in question waived voting rights and subscription rights and, in general, dividend rights for the duration of the trust's existence. The shares issued to the trusts can be sold on the stock exchange on the instructions of Deutsche Telekom if the beneficiaries do not exercise their options or conversion rights or if these expire. The proceeds from the sale accrue to Deutsche Telekom.

The Articles of Incorporation authorize the Board of Management to increase the share capital with the approval of the Supervisory Board by up to EUR 2,399,410,734.08 by issuing up to 937,269,818 registered no par value shares for non-cash contributions in the period ending on May 17, 2009 (2004 authorized capital). They also authorize the Board of Management to increase the share capital, with the consent of the Supervisory Board, by up to EUR 38,400,000 by issuing up to 15,000,000 registered no par value shares for cash and/or non-cash contributions in the period ending on May 2, 2011. The new shares are to be issued for the sole purpose of granting shares to employees of Deutsche Telekom AG and lower-tier affiliated companies (employee shares) (2006 authorized capital) [http://www.deutschetelekom.com/dtag/cms/contentblob/dt/en/37314/blobBinary/dtag-articles-of-incorporation.pdf].

The shareholders' meeting on May 3, 2006 authorized the Board of Management to purchase up to 419,807,790 shares in the Company by November 2, 2007, with the amount of share capital accounted for by these shares totaling up to EUR 1,074,707,942.40, subject to the proviso that the shares to be purchased on the basis of this authorization in conjunction with the other shares of the Company which the Company has already purchased and still possesses or are to be assigned to it under § 71d and § 71e of the German Stock Corporation Act (Aktiengesetz – AktG) do not at any time account for more than 10 percent of the Company's share capital. The shares may also be purchased by dependent Group companies of Deutsche Telekom AG within the meaning of § 17 AktG or by third parties for the account of Deutsche Telekom AG or for the account of the dependent Group companies of Deutsche Telekom pursuant to § 17 AktG. The purchase may take place without prejudice to the principle of equal treatment through the stock exchange or using a public purchase offer addressed to all shareholders. By resolution of the shareholders' meeting of May 3, 2006, the Board of Management is authorized, with the consent of the Supervisory Board, to redeem Deutsche Telekom AG's shares purchased on the basis of the above authorization, without such redemption or its implementation requiring a further resolution of the shareholders' meeting [http://www.deutschetelekom.com/dtag/cms/content/dt/en/4788].

The main agreements entered into by Deutsche Telekom AG, which include a clause in the event of a takeover of Deutsche Telekom AG, principally relate to bilateral credit lines as well as to a loan agreement. In the event of a takeover, the individual lenders have the right to terminate the credit line and, if necessary, serve notice on it or demand repayment of the loan. A takeover is assumed when a third party, which can also be a group acting jointly, acquires control over Deutsche Telekom AG.

In addition, the other members of the Toll Collect consortium (DaimlerChrysler Services AG and Cofiroute SA) have a call option in the event that the ownership structure of Deutsche Telekom AG changes such that over 50 percent of its capital stock or voting rights are held by a new shareholder who previously did not hold them, and this change was not approved by the other members of the consortium. § 22 (1) of the Securities Trading Act (Wertpapierhandelsgesetz – WphG) similarly applies to the allocation of voting rights.

The principal subsidiaries and associates of Deutsche Telekom AG whose revenues, together with those of Deutsche Telekom AG, account for more than 90 percent of the Group, are listed in the notes to the consolidated financial statements ("Summary of accounting policies," paragraph on the **"Consolidated group"**). In addition to Deutsche Telekom AG, 71 German and 204 foreign subsidiaries are fully consolidated in Deutsche Telekom's consolidated financial statements (2005: 69 and 281). 18 associates (2005: 22) and 2 joint ventures (2005: 2) are also included using the equity method.

The changes in Deutsche Telekom's consolidated group relate to both acquisitions and divestments. Two new equity interests were added to the Mobile Communications business area: in May 2006, the Austrian mobile communications group tele.ring and in November 2006 the Polish company PTC, which was previously consolidated at equity. In the Broadband/Fixed Network business area, several companies were consolidated for the first time: in February 2006 the Bulgarian Internet service provider Orbitel and in April 2006 the Hungarian data center operator Dataplex. In addition, the third quarter of 2006 saw the consolidation of ITC service provider KFKI-LNX by Hungarian company Magyar Telekom and Internet service provider iskon Internet by T-Hrvatski Telekom in Croatia. The Business Customers business area also incorporated the IT company gedas for the first time in April 2006. Deutsche Telekom AG reduced its interest in Sireo Real Estate Asset Management GmbH to 25.1 percent at the start of 2006.

The merger of T-Online International AG into Deutsche Telekom AG, which had been approved in 2005, initially could not become effective due to lawsuits filed by some T-Online shareholders. However, with a final and conclusive ruling of the Federal Court of Justice (Bundesgerichtshof), made public on June 1, 2006, the so-called release proceedings initiated by T-Online International AG were successfully completed, enabling the merger to be entered into the commercial register on June 6, 2006 and thereupon to become effective.

Management and supervision.

The management and supervisory structures, as well as the compensation system for the Board of Management and the Supervisory Board, follow the statutory framework and are focused on the long-term performance of the Group. In particular, they comply with the recommendations of the German Corporate Governance Code.

Board of Management responsibilities are distributed across six Board departments. In addition to the central management areas assigned to the chairperson of the Board of Management, the Board member responsible for Finance, and the Board member responsible for Human Resources, three Board departments were established in December 2006 that combine business area-specific and Group-wide tasks: the Business Customers and Production board department, the T-Com, Sales and Service board department and the T-Mobile, Product Development and Product Innovation board department. The Supervisory Board of Deutsche Telekom oversees the management of business by the Board of Management and advises the Board. The Supervisory Board is composed of twenty members, of whom ten represent the shareholders and the other ten the employees.

Deutsche Telekom's Supervisory Board resolved at the end of 2006 to reorganize the Company's top management:

- With effect from November 13, René Obermann – previously the member of the Board of Management responsible for T-Mobile – was appointed as the new Chairman of Deutsche Telekom's Board of Management to succeed Kai-Uwe Ricke, who resigned with effect from November 12, 2006.

- Walter Raizner – responsible for the Broadband/Fixed Network business area – resigned from the Board of Management with effect from December 5, 2006. He was succeeded as of December 5, 2006 by Timotheus Höttges who assumes responsibility as a member of the Board not only for the Broadband/Fixed Network strategic business area, but also for Sales & Service at T-Com and T-Mobile in Germany.

- Hamid Akhavan was also appointed to the Board with effect from December 5, 2006. He is responsible for T-Mobile in Europe and also assumes responsibility for an integrated market approach in Hungary, Croatia, and Slovakia. Mr. Akhavan also manages Group-wide innovation and product development in the consumer business.

- T-Systems Chief Executive Officer Lothar Pauly continues to manage the network and IT strategy plus procurement in the infrastructure area, as well as the Business Customers area.

- Dr. Heinz Klinkhammer, Chief Human Resources Officer for many years, retired from the Board of Management as of January 1, 2007. Chief Financial Officer Dr. Karl-Gerhard Eick has provisionally managed the Human Resources Board department since January 1, 2007. He remains Chief Financial Officer and Deputy Chairman of the Board of Management.

The new management team will develop the Group's strategic thrust further, both nationally and internationally. The operational focus will be on improving service quality and customer satisfaction.

The appointment and discharge of members of the Board of Management is in accordance with § 84 and § 85 AktG. Amendments to the Articles of Incorporation are made pursuant to § 179 and § 133 AktG; the Supervisory Board is also authorized, without a resolution by the shareholders' meeting, to adjust the Articles of Incorporation to comply with new legal provisions that become binding for the Company and to make changes that merely affect the wording.

The six members of the Board of Management are entitled to fixed and annual variable remuneration as well as long-term variable components (Mid-Term Incentive Plan). Total remuneration is generally about 2/3 variable and about 1/3 fixed. The variable component is based on the extent to which each member of the Board of Management achieves the targets assigned to them by the General Committee of the Supervisory Board before the beginning of each financial year.

The total remuneration of Supervisory Board members is governed by § 13 of the Articles of Incorporation and includes a fixed annual component plus variable, performance-related remuneration with short-term and long-term components, depending on the development of net profit per share. The compensation of the members of the Board of Management and the Supervisory Board is reported individually in the notes to the consolidated financial statements under Note 45, broken down by the various components.

Group strategy and Group management.

Key strategic course set in 2006 // Sales campaign targeting growth segments // Aiming to become the service quality leader // Safeguarding a sustainable future through cost efficiency // Value-oriented management of the Group

Group strategy.

Deutsche Telekom's market and competitive environment continues to present huge challenges for our Group. This is partly due to the fact that the general conditions in the individual markets are subject to varying trends. Although the consumers segment is showing increasing signs of saturation, including in mobile communications throughout Europe, there are also growth markets in other areas such as the broadband market, mobile Internet use, and the mobile communications market in the United States. Yet competition is particularly tough for Deutsche Telekom in Germany, which is why the Company is challenged by a loss of market share and margin erosion. These developments are exacerbated further by government regulatory measures.

Previously separate markets and technologies are continuing to converge. One of the driving forces behind this development is the Internet Protocol (IP), a technology used to upload and download data in high-performance broadband networks. This entails both opportunities and risks for our Group. Whereas the ability of Deutsche Telekom as an integrated provider to shape this transformation of the industry constitutes an opportunity, the growing interchangeability of telecommunications offerings poses a major risk. This has prompted an increasing number of providers – also from related industries – to act, some with business models that may have serious implications for Deutsche Telekom. One example is the growing range of Internet-based communication technologies such as voice over IP.

Deutsche Telekom implemented a whole range of key measures during the reporting year that benefited the Group's strategic positioning. The merger of T-Online into Deutsche Telekom, which was successfully completed in 2006, has already substantially improved the range of products on offer from the customer's perspective. This only became possible through an integrated market presence in the highly competitive broadband market. By acquiring further spectrum rights in the United States, Deutsche Telekom prepared to increase its market share in terms of revenue in the U.S. mobile market in summer 2006. In the business customer segment, we further reinforced our core competence as a service provider for information and communications technology by expanding our footprint in the automotive industry with the integration of gedas' activities, for example.

In addition, we succeeded in placing a series of innovations on the market. The marketing kick-off of television content transmitted over the Internet Protocol (IPTV) using the new high-speed network in Germany represents a further milestone for the positioning of Deutsche Telekom in the broadband services market. Thanks to the introduction of HSDPA, mobile broadband has also become a reality in the mobile communications segment. Our sales drive increased the number of DSL customers in Germany to over ten million. With our "Telekom-Vorteil" customer loyalty scheme, customers can benefit from our strength as an integrated telecommunications group. Customers who combine our fixed telephony, mobile communications and broadband offers save on charges. Last but not least, the successful implementation of customer relationship management across business areas means that Deutsche Telekom is now able to tailor integrated offerings to the requirements of its customers even better than before.

To optimize service for our customers in the future, we are pulling out all the stops to achieve a sustainable improvement in the service culture at the customer interface. For Deutsche Telekom to become the most highly regarded service company, all employees have to focus squarely on the customers' needs. On this basis, market-related customer satisfaction will enhance the Group's financial goals.

In Germany's consumer market, our Group is concentrating on ensuring a sustainable level of income in an environment characterized by margin erosion and loss of market share. We will continue to defend our business with innovative calling plans and bundled products. In the broadband market, our goal is to advance business further, both in mobile communications (e.g., with UMTS) and in the fixed network (with T-DSL/VDSL). We will continue to expand our high-speed network for this purpose. We see ourselves as the driving force behind a new market that goes beyond voice telephony and broadband Internet access to provide interactive potential with high-definition television (HDTV).

To achieve these goals, we have to offer exclusive, attractively priced products, backed up with high-caliber customer service. To guarantee this, staffing at the call centers and T-Punkt stores will be adapted to market requirements. The number of T-Punkt stores will be significantly increased, for instance. As part of the T-Service project, some 35,000 people will look after the technical infrastructure and customer service, and a further 10,000 or so will be transferred from call center units. The aim is to offer high-quality service at competitive conditions, which also involves raising productivity in the interests of our customers. Optimized sales, top-quality service and innovative products will enable us to attract new customers.

In the long term, we as a Group will create the most modern range of products in the information and telecommunications industry, using a completely IP-based production architecture, that will include full interoperability between fixed-line and mobile communications. By optimizing our network infrastructure we are also laying an important foundation for sustainable cost efficiency in production. We are striving to achieve lean cost structures in both the consumers and the business customers area.

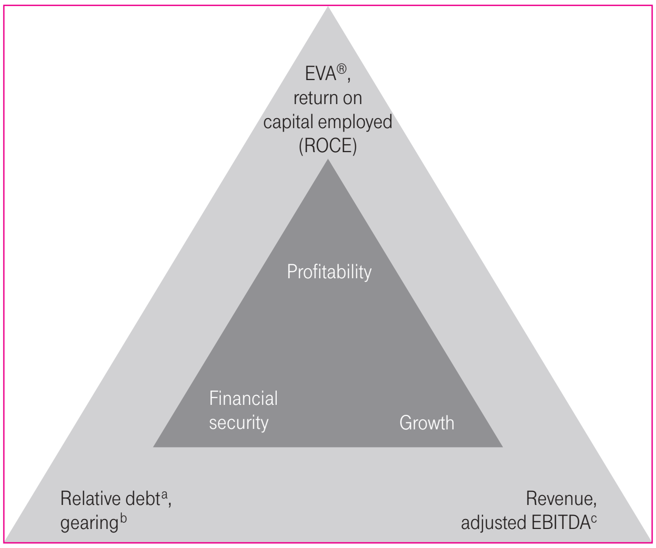
In the rest of Europe, our aim is to systematically increase our market share in terms of revenue. We are pursuing a very aggressive strategy in our mobile communications markets, both in respect of winning over market shares from other mobile operators and through substitution of fixed-line business. In doing so, we are placing particular emphasis on customer service and attractive offers. As an integrated telecommunications provider in Hungary, Croatia, and Slovakia, we will systematically market triple-play and quad-play packages in these markets as well. Triple play combines voice telephony, broadband Internet access, and TV-based entertainment services, while quad play adds a mobile communications component. Our goal is to further expand our excellent market position in Eastern Europe in specific areas.

In the United States, the mobile communications market as a whole is still experiencing strong subscriber growth, which means that Deutsche Telekom must first and foremost seek to grow faster than the market – in other words, to increase its market share. Average revenue per user has to be kept stable at the same time. The success of T-Mobile USA to date is attributable not least to the outstanding quality of its customer service. Now that we have acquired more frequency at the spectrum auction, our network capacity has increased. We will use this to add attractive services to our product portfolio.

In the business customer segment, we will forcefully defend our share of the telecommunications market and further expand it in the large and medium-sized customer segments. At the same time, we will introduce offers with standardized IT services and solutions for the middle market in the growth area of information technology and expand the IT outsourcing business with existing and new key accounts. The market-oriented steps already taken include strategic pricing measures and also the rapid expansion of IP services. On the production side, we will consolidate the platforms to tap additional potential efficiency. Systematically aligning production architecture and business processes will put us in an excellent position to serve the business customer market with a portfolio of competitive integrated IT and telecommunications solutions. This applies to horizontal solutions for specific parts in the value chain and also to industry-specific solutions, such as the automotive industry or the public sector.

Our goal is to make Deutsche Telekom the leading service provider in the industry. To do this, we will cement the service concept deep in our corporate culture throughout the Group. Our Company will prove its worth with exemplary quality of service both internally and, in particular, externally in direct contact with customers. Achieving this goal – service leadership – will be pivotal to sustaining our success in the face of competition.

Group management.
The financial management of the Group uses an integrated system of key figures based on a small number of closely related key performance indicators (KPIs). These performance indicators define the delicate balance of growth, profitability and financial security the Group has to maintain when pursuing its primary goal of profitable growth:



[a] The "relative debt" indicator is the ratio of net debt to EBITDA adjusted for special factors; for more information, please refer to the "Development of business" section.
[b] The "gearing" indicator is the ratio of net debt to equity; for more information, please refer to the "Development of business" section.
[c] Corresponds to EBITDA adjusted for special factors; for more information, please refer to the "Development of business" section.

Revenue growth forms the basis for almost every company's income statement and reflects the concept of substantive growth. A further KPI is EBITDA, which corresponds to profit/loss from operations excluding depreciation, amortization, and impairment losses. The Group uses EBITDA growth to measure its short-term operational performance and the success of its individual operations. The Group also uses the EBITDA margin – the ratio of EBITDA to revenue – as a performance indicator. This relative indicator enables a comparison of the earnings performance of profit-oriented units of different sizes.

The Group's focus on financial security ensures that it will continue to be able to repay its debt and remain financially sound. Financial security is primarily measured using the "gearing" and "relative debt" KPIs. One component of the indicators is net debt, which Deutsche Telekom uses as an important indicator for investors, analysts, and rating agencies.

To measure the profitability of business development, the Group uses the return on capital employed (ROCE) as a relative indicator and economic value added (EVA®) as an indicator of value creation.

ROCE shows the result obtained in relation to the assets employed in achieving that result. ROCE is calculated using the ratio of profit from operations after depreciation, amortization, impairment losses, and taxes (i.e., net operating profit after taxes, or NOPAT) to the average value of the assets tied up for this purpose in the course of the year (i.e., net operating assets, or NOA).

Deutsche Telekom's goal is to exceed the return targets imposed on it by lenders and equity suppliers on the basis of capital market requirements (superior shareholder return). Return targets are measured using the weighted average cost of capital (WACC). The cost of equity is the return an investor expects on an investment in the capital market with equivalent risk. The cost of debt is calculated on the basis of the Group's financing terms on the debt market, taking into account that interest on borrowed capital is tax-deductible.

The Group uses EVA® as its key indicator of value creation to measure the absolute contributions made by the operational units to the value of the Group. In general, it is also the main benchmark for focusing all operational measures on superior value.

The main elements are:

- Value-oriented growth in the strategic business areas that promise an appropriate return on capital employed: Each investment must generate a return that corresponds at least to the WACC. In addition, the business portfolio is optimized by focusing on the business areas that are expected to generate the highest returns in the medium term.

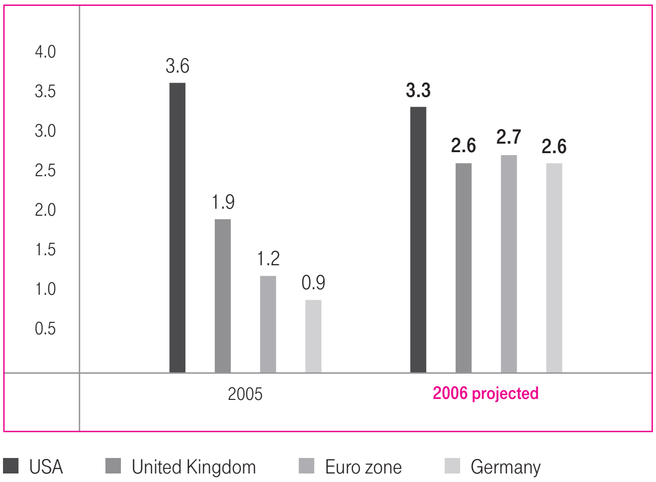
- Optimization of ongoing business activities. The Group continuously searches for significant gaps and potential with the aim of improving the value contribution of existing units and optimizing the employment of capital.

This ensures that all activities are focused on superior value. Value-oriented management thus implements the Group's commitment to growth in value-creating business areas down to the level of the operational units.

The economic environment.

Global economy growing at a high level overall // Mobile communications continues to drive growth in the telecommunications market despite falling prices // Broadband market is boosting the Internet as a mass medium

Gross domestic product
Changes over the prior year in real terms (%)



Global economic development.

The global economy continued to develop very robustly in 2006, though some worldwide momentum was lost after the summer. A clear cyclical divide between the major economic areas became apparent. While Europe experienced a dynamic upswing during the year, aggregate capacity utilization in the United States and Japan declined. In the EU accession countries, production continued its vigorous upward trend, although the pace of growth varied slightly in the individual countries. The euro strengthened against the U.S. dollar and the Japanese yen in 2006, reflecting an improvement in the euro zone's economic prospects.

An increasingly restrictive monetary policy had a dampening effect on the economies of almost all major industrial countries in 2006. However, the macroeconomic environment underwent a slight improvement in the third quarter of 2006 compared with previous quarters. While oil prices reached new highs in August 2006, they had rapidly slid back down again by the end of December 2006, even falling to below 2005 prices. Other raw material prices also stagnated or dropped around the end of the year. This pushed down the inflation rate in industrialized countries in the last few months of the year to such an extent that although the inflation rate in 2006 rose slightly on account of increasing acceleration in the wage drift, it was still exceedingly low.

According to estimates by the Institute for the World Economy, the real gross domestic product (the value of all services generated in a country) of the United States grew more or less as strongly as in 2005 at 3.3 percent, but aggregate capacity utilization fell substantially over the year as a result of a drop in housing investment. The economies in the euro zone experienced a strong upturn in 2006. The Institute for the World Economy estimated that GDP increased by 2.7 percent. The surge in economic growth also strengthened in the United Kingdom, where the Institute for the World Economy puts the increase in GDP at 2.6 percent. At an estimated 4.7 percent, expansion in the new Member States of the European Union is slightly higher than in the previous year.

Real GDP growth in Germany was an estimated 2.6 percent. In contrast to previous years, however, this growth was not driven by exports alone. The sharp increase in investments in noncurrent assets and the appreciable rise in consumer demand at the end of the year also contributed to this positive development.

Telecommunications market.
The liberalization of the telecommunications sector has led to intense price pressure. This is again reflected in the Federal Statistical Office figures for the price index for telecommunications services (fixed network, mobile communications, and Internet) for the period January to December 2006. Consumer prices for telecommunication services in 2006 were on average 3.0 percent lower than in the previous year. This was principally due to the year-on-year drop in prices for mobile telephony (10.7 percent) and for Internet use (5.1 percent). After declining in both 2004 and 2005, mobile telephony rates decreased again in 2006 with the advent of mobile communications discounters. In 2006, the price war among DSL providers affected prices for Internet access.

Mobile communications market.
The mobile communications business continued its global growth trend in 2006, although the pace of development varied in the individual regions. While growth tailed off in Western Europe's largely saturated markets, the United States and Eastern Europe continued to record strong growth in customers and revenue. There was also further consolidation among the providers on the market.

Generally speaking, three groups of providers are competing for customers in mobile communications markets: network operators, resellers, and companies that buy network services and market them independently to third parties (MVNOs). A precondition for operating mobile communications networks, and hence for offering mobile communication services, is a frequency spectrum license awarded by the government. Whereas these are normally awarded by the national authorities in Europe, the United States has a large number of license areas, even within the individual states. The number of licenses awarded limits the number of network operators in each market, subjecting mobile communications to a range of regulatory regimes including price regulation. The award of licenses, the prices of the licenses, and regulation significantly influence the mobile communications business.

In the United States, T-Mobile now competes with three major national providers – Verizon, AT&T/Cingular, and Sprint/Nextel, all with a much larger national customer base than T-Mobile.

Competition continues to be intense in most markets in Europe. This affects price, contract options, applications, network coverage, and quality of service. As markets approach saturation point, providers are increasingly focusing on strengthening existing customer relationships. At the European level, competition in mobile communications is increasing because of the introduction of Europe-wide services.

Despite the increasingly difficult market environment, T-Mobile USA again recorded above-average growth in 2006 and further expanded its market share. Furthermore, the foundation for further growth in the U.S. market was laid last year with the acquisition of additional spectrum. In Germany, on the other hand, T-Mobile was unable to maintain its revenues at the prior-year level on account of intense competition. By contrast, T-Mobile UK succeeded in acquiring further revenue market share in what was also a hard-fought market. T-Mobile remains the largest mobile communications company in Central and Eastern European markets in terms of customer numbers.

Broadband/fixed-network market.
In Germany, competition in the fixed-network market has intensified further. In addition to increasing competition from large European telecommunications companies and city network operators, pressure from cable operators is also growing. In addition, substitution by mobile communications continues. According to Bitkom, companies in Germany generated 4.5 percent less revenue from fixed-network calls in 2006. This source of revenue amounted to only EUR 18.8 billion, in contrast to the mobile communications market, which grew by 2 percent in 2006 to EUR 23.9 billion.

According to Bitkom, revenue from voice services in the telecommunications market is currently declining by EUR 1 billion per year. At the same time, Bitkom describes growth in data services as "dynamic." Together with mobile communications, which is growing moderately, revenue from telecommunication services in Germany increased by a modest 0.9 percent to EUR 56.6 billion in 2006.

In Europe's online markets, the Internet also remained an important growth driver for the fixed network. Jupiter Research estimates that the number of private Internet users in Western Europe increased from around 196 million to approximately 209 million in 2006, which equates to growth of 7 percent. This means that, overall, significantly more than 50 percent of Western Europe's population already has access to the Internet. The proportion of households in Western Europe with broadband access increased from 31 percent to 40 percent. The increase in the number of broadband households is accompanied by the growing use of data-intensive applications giving online access to entertainment programs such as films, music, and games, for example.

Despite these difficult market conditions, the Broadband/Fixed Network business area was able to maintain its strong foothold as a broadband provider with new integrated complete packages, especially after the merger of T-Online International AG into Deutsche Telekom AG, and to expand its excellent position in the hard-fought broadband market with a total of 11.7 million broadband lines (2005: 8.6 million). The 3x3 complete packages launched in mid-September 2006 are evidence of this business area's outstanding market success, with 3.6 million marketed customers by the end of 2006. Over 70 percent of the rates are sold as a complete package comprising a traditional voice line, an innovative broadband line and a voice and Internet component, as well as an Internet flat rate. Through up-selling and with new service packages, we have succeeded in addressing new customer groups, thus boosting the dynamic growth of the broadband market once more in the fourth quarter of 2006. In addition, the business area had over 16.6 million Internet customers throughout Europe with a billing relationship in 2006 (2005: 15.2 million).

A further decrease in the number of call minutes in the fixed network was recorded. According to a study by Dialog consult and analyses and forecasts by VATM, T-Com's competitors account for more than 50 percent of call minutes. The increase in competitors' market share of call minutes is primarily due to the higher sales of full-package lines on their part.

At T-Com, the development of call minutes in 2006 was marked by opposing trends. Firstly, T-Com increased minutes loyalty for all call types compared with the previous year, especially as a result of the successful marketing of calling plans and introduction of complete packages in fall 2006. This was also illustrated by the increase in overall minutes loyalty, which rose by 4.7 percentage points year-on-year to 68.4 percent. T-Com has therefore managed to defend itself against competitors' call-by-call and preselection offers. Secondly, the absolute number of call minutes in T-Com's network fell sharply again. This is attributable to the ongoing line losses, increasing substitution by mobile communications, and – albeit to a lesser extent – substitution by VoIP.

In 2006, the French market was again characterized by strong investment by market participants in the expansion of telecommunications networks and in customer acquisition, as well as by continued price competition. To set itself apart from its competitors in this market environment, the Broadband/Fixed Network business area pursued a very aggressive pricing strategy in France, while offering innovative products on the basis of a proprietary IP-based network, and ensuring service quality. This successful strategy helped Broadband/Fixed Network to grow faster than the market as a whole to acquire additional market share.

Spain also saw further consolidation of the broadband market in 2006. Here, the business area positively set itself apart from the competition on the basis of its own network, through both prices and products. With its company Ya.com, the Broadband/Fixed Network division is the third-largest ADSL network operator after its competitors Telefónica and the France Télécom unit Orange. As a result, the division was able to further cement and expand its share of the market in Spain.

In Eastern Europe, intense competition continues unabated on account of substitution by mobile communications, preselection and call-by-call providers, as well as cable network operators. In this difficult environment, T-Com focused on introducing attractive calling plans and flat rate offers as well as triple play, and on dynamic growth in the broadband market. This checked the downward trend.

More new competitors entered the market in Croatia and Slovakia in 2006. Increasing substitution by mobile communications has intensified competition in Slovakia, for example. In addition, more customers in Slovakia and Hungary switched over to cable network operators. IPTV was introduced in Croatia in the third quarter of 2006 and in Hungary and Slovakia in the fourth quarter of 2006 to develop new customer groups for the broadband business.

Business customer market.
Developments in the business customer market for information and communication technologies (ICT market) are closely linked to the macroeconomic and regional economic environment. The current economic climate in the ICT market further intensified competition in 2006 with continued price reductions in nearly all segments of the market. This resulted in further consolidation of the market, which currently consists of a handful of large IT and telecommunications providers and a number of fast-growing smaller providers.

In this market environment, T-Systems has held its ground well throughout Europe. In terms of total revenue, T-Systems is the German market leader in both the IT and the telecommunications sector. In Western Europe, the unit is one of the top five providers of IT services, together with IBM Global Services, EDS, HP Services, and Accenture. In the area of telecommunications services, T-Systems, BT Global Services, France Télécom/Equant, and Telefónica are the top four European providers. Globally, T-Systems is one of the top 20 IT and telecommunications providers in terms of total revenue.

Regulatory influence on Deutsche Telekom's business.
Deutsche Telekom's business activities are strongly affected by regulation, combined with extensive powers of government agencies to intervene in product design and pricing. The German Telecommunications Act (Telekommunikationsgesetz – TKG) stipulates far-reaching regulation for many areas of telecommunications services.

Under the TKG, the Federal Network Agency can impose obligations on companies with significant market power in individual markets regarding the services they offer on those markets. For example, such companies may be obliged to offer certain upstream products at prices that are subject to prior approval by the Federal Network Agency. Regulation therefore substantially encroaches on their entrepreneurial freedom.

In applying the TKG, the Federal Network Agency has so far refused to reduce the intensity of regulation. With the exception of a few cases, the regulations are applied unchanged and even extended to cover new services and markets. These regulations not only apply to services and markets that were not regulated in the past, but also to those that are just emerging. For example, the innovative voice over IP service is now part of the regulated voice telephony market. Similarly, VDSL lines have generally been allocated to the broadband wholesale services segment (a regulated market), although Deutsche Telekom has only just completed development of this technology. A new provision to be included in the TKG, which specifies that new markets should always be exempt from regulation, is expected to improve the regulatory framework. Final implementation of this regulation is still pending, given that the EU Commission has already instituted breach-of-contract proceedings alleging that the regulation is in conflict with the EU's legal framework. Deutsche Telekom will make its decisions on additional investments in broadband networks dependent not only on demand, but also on the regulatory environment.

Deutsche Telekom is subject to regulation not only in Germany; some of its subsidiaries abroad also have to comply with local regulations. For the fixed network, this applies in particular to subsidiaries in Hungary, Slovakia, and Croatia. In mobile communications, subsidiaries in the United States, the United Kingdom, the Netherlands, Austria, the Czech Republic, Hungary, Croatia, and Slovakia are subject to regulation.

Development of business in 2006.

Proportion of revenue generated outside Germany continues to rise // Profit after income taxes lowered by staff-related measures // Investments continue to grow // Deutsche Telekom rating by all major ratings agencies in the single A– range

Earnings situation of the Group.

Net revenue increased by EUR 1.7 billion year-on-year to EUR 61.3 billion. This corresponds to an increase of 2.9 percent. This continued net revenue growth was aided by effects relating to the composition of the Group (mainly gedas, tele.ring and PTC) in the amount of around EUR 1.2 billion. On the other hand, there were negative exchange rate effects totaling approximately EUR 0.2 billion, especially from the translation of U.S. dollars (USD) to euros.

The main contributor to net revenue – and revenue growth – was once again the Mobile Communications strategic business area. By contrast, the Broadband/Fixed Network strategic business area recorded a drop in revenue.

The proportion of international revenue continued to increase, rising year-on-year by around 4.5 percentage points to 47.1 percent. The key factor underlying this trend is the sustained positive business development at T-Mobile USA.

Contribution of the strategic business areas to net revenue

	2006 millions of €	Proportion of net revenue of the Group %	2005 millions of €	Proportion of net revenue of the Group %	Change millions of €	Change %	2004 millions of €
Net revenue	**61,347**	**100.0**	**59,604**	**100.0**	**1,743**	**2.9**	**57,353**
Mobile Communications	31,308	51.0	28,531	47.9	2,777	9.7	25,450
Broadband/Fixed Network	20,635	33.6	21,731	36.4	(1,096)	(5.0)	22,397
Business Customers	9,061	14.8	9,058	15.2	3	0.0	9,246
Group Headquarters & Shared Services	343	0.6	284	0.5	59	20.8	260

Development of revenue by geographic area

	2006 millions of €	2005 millions of €	Change millions of €	Change %	2004 millions of €
Net revenue	**61,347**	**59,604**	**1,743**	**2.9**	**57,353**
Domestic	32,460	34,183	(1,723)	(5.0)	34,741
International	28,887	25,421	3,466	13.6	22,612
Proportion generated internationally (%)	47.1	42.6			39.4
Europe (excluding Germany)	14,823	13,272	1,551	11.7	12,952
North America	13,700	11,858	1,842	15.5	9,301
Other	364	291	73	25.1	359

EBITDA for the Group decreased in the reporting year by around EUR 3.8 billion or 18.9 percent to EUR 16.3 billion.

In the reporting year, special factors had a net negative effect on EBITDA of EUR 3.1 billion. These mainly involved expenses in connection with staff-related measures. In the previous year, by contrast, positive special factors were recorded, mainly relating to the reversal of provisions in connection with new arrangements for the financing of the Civil Service Health Insurance Fund.

Excluding these special factors, adjusted EBITDA decreased by EUR 1.3 billion or 6.2 percent to EUR 19.4 billion. All business areas except Mobile Communications contributed to this decrease. The decline in the Broadband/Fixed Network business area was particularly a result of the drop in fixed-network revenue, increased customer acquisition costs, especially in the broadband area, and higher costs in connection with the launch of new products. This combined impact on adjusted EBITDA was partially offset by cost-cutting measures. The decrease in the Business Customers strategic business area is mainly attributable to persistently high price and cost pressures. In the Group Headquarters & Shared Services area, adjusted EBITDA declined mainly due to a price- and volume-driven decrease in real estate billings. Adjusted EBITDA at the Mobile Communications business area increased, particularly driven by favorable revenue trends in the wake of consistently strong customer growth as well as the first-time consolidation of PTC in Poland and of tele.ring.

At around EUR 3.6 billion, **profit after income taxes** for 2006 was down EUR 2.4 billion year-on-year. This development was affected by offsetting special factors.

Besides the aforementioned special factors that negatively affected EBITDA, some positive income tax-related special factors were recorded. In particular, these included tax income from the recognition of previously unrecognized deferred tax assets relating to loss carryforwards at T-Mobile USA and tax-related impacts on the special factors affecting EBITDA. In the previous year, the main special factors were goodwill impairment losses at T-Mobile UK and offsetting tax income from the reversal of impairment losses on deferred tax assets relating to U.S. loss carryforwards, plus the gain on the disposal of the remaining shares in MTS.

Adjusted for these special factors, profit after income taxes amounted to around EUR 4.3 billion compared with EUR 5.1 billion in the prior-year period.

Consolidated income statement and impact of special factors [a, b]

millions of €	2006	Special factors	2006 excluding special factors	2005	Special factors	2005 excluding special factors	2004	Special factors	2004 excluding special factors
Net revenue	61,347		61,347	59,604		59,604	57,353		57,353
Cost of sales	(34,755)	(1,400)[c]	(33,355)	(31,862)	(535)[i]	(31,327)	(31,544)	(1,325)[q]	(30,219)
Gross profit	**26,592**	**(1,400)**	**27,992**	**27,742**	**(535)**	**28,277**	**25,809**	**(1,325)**	**27,134**
Selling expenses	(16,410)	(790)[d]	(15,620)	(14,683)	(276)[j]	(14,407)	(12,870)	(24)	(12,846)
General and administrative expenses	(5,264)	(841)[e]	(4,423)	(4,210)	(262)[k]	(3,948)	(4,476)	(137)[r]	(4,339)
Other operating income	1,257	20	1,237	2,408	824[l]	1,584	1,718	84[s]	1,634
Other operating expenses	(888)	(145)[f]	(743)	(3,635)	(2,297)[m]	(1,338)	(3,916)	(2,524)[t]	(1,392)
Profit from operations (EBIT)	**5,287**	**(3,156)**	**8,443**	**7,622**	**(2,546)**	**10,168**	**6,265**	**(3,926)**	**10,191**
Loss from financial activities	(2,683)	196[g]	(2,879)	(1,403)	1,059[n]	(2,462)	(2,695)	1,230[u]	(3,925)
Profit before income taxes	**2,604**	**(2,960)**	**5,564**	**6,219**	**(1,487)**	**7,706**	**3,570**	**(2,696)**	**6,266**
Income taxes	970	2,259[h]	(1,289)	(198)	2,377[o]	(2,575)	(1,552)	555[v]	(2,107)
Profit after income taxes	**3,574**	**(701)**	**4,275**	**6,021**	**890**	**5,131**	**2,018**	**(2,141)**	**4,159**
Profit attributable to minority interests	409	(16)	425	432	(31)	463	424	(55)	479
Net profit	3,165	(685)	3,850	5,589	921	4,668	1,594	(2,086)	3,680
Profit from operations (EBIT)	5,287	(3,156)	8,443	7,622	(2,546)	10,168	6,265	(3,926)	10,191
Depreciation, amortization and impairment losses	(11,034)	(43)	(10,991)	(12,497)	(1,936)[p]	(10,561)	(13,127)	(3,698)[w]	(9,429)
EBITDA	**16,321**	**(3,113)**	**19,434**	**20,119**	**(610)**	**20,729**	**19,392**	**(228)**	**19,620**
EBITDA margin (%)	**26.6**		**31.7**	**33.8**		**34.8**	**33.8**		**34.2**

[a] Prior-year comparatives for the items profit/loss from financial activities, profit before income taxes, income taxes, profit after income taxes, and net profit have been adjusted to reflect the change in policy in accounting for actuarial gains and losses. For further details, please refer to Note 29 in the consolidated financial statements.

[b] EBITDA for the strategic business areas and the Group as a whole is derived from profit/loss from operations (EBIT). This measure of earnings before profit/loss attributable to minority interests, income taxes, and profit/loss from financial activities is additionally adjusted for depreciation, amortization and impairment losses to calculate EBITDA. It should be noted that Deutsche Telekom's definition of EBITDA may differ from that used by other companies. In this definition, profit/loss from financial activities includes finance costs, the share of profit/loss of associates and joint ventures accounted for using the equity method, and other financial income/expense. As it is based on profit/loss from operations, this method of computation allows EBITDA to be derived in a uniform manner on the basis of a measure of earnings in accordance with IFRS published for the strategic business areas and the Group as a whole. In the reporting period as well as the comparable prior-year period, Deutsche Telekom's net profit/loss as well as the EBITDA of the Group and of the strategic business areas were affected by a number of special factors. Deutsche Telekom defines EBITDA adjusted for special factors as profit/loss from operations (EBIT) before depreciation, amortization, and impairment losses and before the effects of any special factors. The underlying concept involves the elimination of special factors that affect operational business activities and thus impair the comparability of EBITDA and net profit/loss with the corresponding figures for prior periods. In addition, a statement about the future development of EBITDA and net profit is only possible to a limited extent due to such special factors. Adjustments are made irrespective of whether the relevant income and expenses are reported in profit/loss from operations, profit/loss from financial activities, or in tax expense. Income and expenses directly relating to the items being adjusted are also adjusted. To compare the earnings performance of profit-oriented units of different sizes, the EBITDA margin and the adjusted EBITDA margin are presented in addition to EBITDA and adjusted EBITDA. The EBITDA margin is calculated as the ratio of EBITDA to net revenue (EBITDA divided by net revenue).

Special factors in 2006:

[c] Expenditures for staff-related and restructuring measures, mainly in Broadband/Fixed Network (EUR – 0.8 billion) and Business Customers (EUR – 0.5 billion).

[d] Expenditures for staff-related and restructuring measures, mainly in Broadband/Fixed Network (EUR – 0.5 billion) and Business Customers (EUR – 0.2 billion).

[e] Expenditures for staff-related and restructuring measures, primarily in Broadband/Fixed Network (EUR – 0.1 billion) and Business Customers (EUR – 0.1 billion), as well as Group Headquarters & Shared Services (EUR – 0.6 billion).

[f] Expenditures for staff-related and restructuring measures, primarily in Group Headquarters & Shared Services (EUR – 0.1 billion).

[g] Retroactive income from the sale of Celcom in Group Headquarters & Shared Services (EUR 0.2 billion).

[h] Positive tax effects from the recognition of previously unrecognized deferred tax assets relating to loss carryforwards at T-Mobile USA (EUR 1.3 billion) and from expenditures for staff-related and restructuring measures (EUR 1.2 billion) are offset by negative tax effects, mainly from valuation allowances on deferred tax assets relating to loss carryforwards at T-Mobile in Austria and at Broadband/Fixed-Network in France and Spain (EUR – 0.2 billion).

Special factors in 2005:

[i] Expenditures for staff-related measures, primarily in Broadband/Fixed Network (EUR – 0.4 billion) and Business Customers (EUR – 0.1 billion), as well as Group Headquarters & Shared Services (EUR – 0.1 billion).

[j] Expenditures for staff-related measures, primarily in Broadband/Fixed Network (EUR – 0.2 billion) and other strategic business areas (EUR – 0.1 billion).

[k] Expenditures for staff-related measures, mainly in Broadband/Fixed Network (EUR – 0.1 billion) and Business Customers (EUR – 0.1 billion).

[l] Primarily income from the reversal of provisions in connection with the Civil Service Health Insurance Fund (EUR 0.8 billion).

[m] Goodwill impairment losses at T-Mobile UK (EUR –1.9 billion), additions to out-of-court settlement payments at Group Headquarters & Shared Services (EUR – 0.1 billion) and in particular expenditures for staff-related and restructuring measures (EUR – 0.3 billion).

[n] Gains on disposal, mainly from the sale of MTS (EUR 1.0 billion; Mobile Communications) and comdirect bank (EUR 0.1 billion; Broadband/Fixed Network).

[o] Positive tax effects from the reversal of impairment losses on deferred tax assets in connection with loss carryforwards at T-Mobile USA (EUR 2.2 billion) and from expenses for staff-related measures (EUR 0.5 billion) are offset by negative tax effects from the reversal of provisions for the Civil Service Health Insurance Fund (EUR – 0.3 billion; Group Headquarters & Shared Services).

[p] Primarily goodwill impairment losses at T-Mobile UK (EUR –1.9 billion).

Special factors in 2004:

[q] Goodwill impairment losses on U.S. mobile communications licenses of just under EUR –1.3 billion as well as expenditures for staff-related measures of less than EUR –0.1 billion (Broadband/Fixed Network).

[r] Expenditures for staff-related measures in Broadband/Fixed Network as well as other risks (EUR – 0.1 billion in total).

[s] Retroactive income from the sale of Virgin Mobile (EUR 0.1 billion; Mobile Communications).

[t] Goodwill impairment losses at T-Mobile UK (EUR –2.2 billion) and Slovak Telekom (EUR – 0.2 billion) as well as expenditures for staff-related measures at Broadband/Fixed Network and Group Headquarters & Shared Services (EUR – 0.1 billion in total).

[u] Gain on disposals of shares, primarily in MTS (EUR 1.0 billion; Mobile Communications) and in SES (EUR 0.2 billion; Group Headquarters & Shared Services).

[v] Tax income primarily from the above-mentioned expenditures for staff-related measures (EUR 0.1 billion) and impairment losses on U.S. mobile communications licenses (EUR 0.5 billion).

[w] Goodwill impairment losses at T-Mobile UK (EUR – 2.2 billion) and Slovak Telekom (EUR – 0.2 billion) as well as impairment losses on U.S. mobile communications licenses (EUR –1.3 billion).

Earnings development in the strategic business areas

millions of €	Mobile Communications			Broadband/Fixed Network			Business Customers			Group Headquarters & Shared Services		
	2006	2005	2004	2006	2005	2004	2006	2005	2004	2006	2005	2004
Net revenue	**31,308**	**28,531**	**25,450**	**20,635**	**21,731**	**22,397**	**9,061**	**9,058**	**9,246**	**343**	**284**	**260**
Intersegment revenue	732	921	1,077	4,050	4,304	4,615	3,560	3,792	3,716	3,331	3,221	3,266
Total revenue	**32,040**	**29,452**	**26,527**	**24,685**	**26,035**	**27,012**	**12,621**	**12,850**	**12,962**	**3,674**	**3,505**	**3,526**
Profit (loss) from operations (EBIT)	**4,504**	**3,005**	**1,524**	**3,307**	**5,142**	**5,551**	**(881)**	**409**	**554**	**(2,043)**	**(840)**	**(1,441)**
Depreciation, amortization and impairment losses	(5,358)	(6,696)	(6,943)	(3,869)	(4,034)	(4,399)	(932)	(896)	(955)	(932)	(928)	(885)
EBITDA	**9,862**	**9,701**	**8,467**	**7,176**	**9,176**	**9,950**	**51**	**1,305**	**1,509**	**(1,111)**	**88**	**(556)**
EBITDA margin (%)	30.8	32.9	31.9	29.1	35.2	36.8	0.4	10.2	11.6	(30.2)	2.5	(15.8)
Special factors affecting EBITDA	(40)	(71)	68	(1,576)	(683)	(220)	(1,179)	(281)	(121)	(708)	423	(8)
EBITDA adjusted for special factors	**9,902**	**9,772**	**8,399**	**8,752**	**9,859**	**10,170**	**1,230**	**1,586**	**1,630**	**(403)**	**(335)**	**(548)**
EBITDA margin adjusted for special factors (%)	30.9	33.2	31.7	35.5	37.9	37.6	9.7	12.3	12.6	(11.0)	(9.6)	(15.5)
Employees*	**54,124**	**49,479**	**47,417**	**108,956**	**112,872**	**115,292**	**55,687**	**51,744**	**51,978**	**29,713**	**29,931**	**32,872**

* Annual average.

Mobile Communications (T-Mobile).
T-Mobile increased its **net revenue** by 9.7 percent or EUR 2.8 billion over the prior year. In addition to the first-time consolidation of the Polish mobile communications company PTC in November, this increase was principally attributable to revenue growth of more than 15 percent at T-Mobile USA. With 3.4 million net additions in the 2006 financial year, T-Mobile USA increased its customer base to 25.0 million by year-end. The subsidiaries in Slovakia and the Czech Republic also recorded a double-digit increase in revenue. In the United Kingdom, the aggressive marketing of new calling plans resulted in renewed revenue growth of over 8 percent. The full consolidation of tele.ring in 2006 also had a positive effect on revenue development. In Germany, revenues declined as a result of falling prices and cuts in termination charges imposed by the regulatory authorities. Revenue in Hungary also decreased as a result of falling prices.

Intersegment revenue declined by EUR 0.2 billion to EUR 0.7 billion in 2006 and was mainly generated with mobile terminated calls in Germany.

EBITDA in the Mobile Communications strategic business area rose by almost EUR 0.2 billion to EUR 9.9 billion. This corresponds to EBITDA growth at T-Mobile of around 2 percent in the 2006 financial year, while **adjusted EBITDA** increased by 1.3 percent, also to around EUR 9.9 billion. This positive development is primarily attributable to revenue growth and the first-time consolidation of PTC in Poland and of tele.ring, although this effect was partly offset by higher cost of sales and selling expenses, particularly at T-Mobile USA. In the 2006 financial year, T-Mobile USA again made the largest contribution to EBITDA from mobile communications with EUR 3.7 billion, followed by T-Mobile Deutschland (EUR 3.3 billion) and T-Mobile UK (approximately EUR 1.0 billion).

Profit from operations (EBIT) increased by EUR 1.5 billion to EUR 4.5 billion in the 2006 financial year. This reflects the positive development of EBITDA and the year-on-year decrease in depreciation, amortization, and impairment losses. In 2005, EBIT had been significantly impacted by impairment losses on intangible assets. T-Mobile UK alone recognized goodwill impairment losses of EUR 1.9 billion in the 2005 financial year. Depreciation and impairment of property, plant and equipment increased by EUR 0.3 billion year-on-year, mainly as a result of the continued expansion of the network in the United States. **EBIT adjusted** for special factors was also around EUR 4.5 billion and decreased by EUR 0.4 billion year-on-year as the positive development of EBITDA was offset by depreciation, amortization and impairment losses to a much greater extent than in the prior year.

Broadband/Fixed Network.
In the 2006 financial year, **net revenue** in the Broadband/Fixed Network strategic business area decreased by EUR 1.1 billion to EUR 20.6 billion. **Intersegment revenue** declined by EUR 0.3 billion to EUR 4.1 billion in 2006, largely as a result of a decrease in prices and volumes in the Business Customers business area. Revenue from other business areas accounted for 16.4 percent of the total revenue generated by the Broadband/Fixed Network strategic business area.

In Germany, net revenue declined by EUR 1.2 billion to EUR 17.9 billion, a year-on-year decrease of 6.1 percent. This drop is mainly attributable to lower call revenues and a reduction in the number of narrowband lines, but also to declines in interconnection services and price erosion in the ISP market. Despite heavy price reductions, the revenue shortfall was partly offset by volume growth in DSL resale and leased subscriber lines. Changed customer retention periods in the network communications, wholesale, and IP/Internet revenue clusters also had a positive effect of EUR 0.2 billion on revenue in 2006.

Total revenue in the Broadband/Fixed Network strategic business area declined by 5.2 percent to EUR 24.7 billion. In Germany revenue decreased by 6.1 percent to EUR 21.8 billion.

Revenue from network communications in Germany fell by EUR 1.1 billion (9.0 percent) to EUR 11.2 billion in 2006. The slight revenue decline of EUR 79 million or 1.0 percent in narrowband lines is attributable to continued line losses as a result of intense competition. Most of these losses were balanced out by higher monthly charges for calling plans, as efforts to market these plans as a component of access lines were stepped up also to improve customer retention. The sharp decrease in call revenues was attributable to the decline in call minute volumes due to continuing narrowband line losses, mobile and VoIP substitution, the decrease in average call minute prices due to the higher penetration of calling plans, and the reduction in termination charges for fixed-to-mobile calls which was passed on to end customers. Overall, call revenues declined by EUR 1.0 billion to EUR 3.4 billion, making them the main driver of the revenue decline in Network Communications.

Revenue development in wholesale services was marked by contrasting effects. In total, revenue fell by 1.3 percent or EUR 55 million compared with 2005. The significant volume-driven growth in revenue from leased subscriber lines and the DSL resale product had a positive effect. By contrast, revenue decreased due to price reductions imposed by the regulatory authorities such as the 9.8 percent rate reduction for subscriber lines that took effect on April 1, 2005, the reduction in interconnection fees by an average of 10 percent, which came into force on June 1, 2006, and the lower prices for the DSL resale product in 2006. This was compounded by volume effects of the increase in direct network interconnection between competitors, plus shrinking volumes due to call-by-call providers' losses of market share. Revenues from wholesale originating services for Internet service providers were negatively impacted by migration from narrowband to broadband and by price cuts in the broadband sector.

IP/Internet revenue amounted to EUR 3.0 billion in 2006. Volume growth in terms of DSL lines was unable to fully offset the price erosion. Customers increasingly opted for complete packages with a flat rate component. Due to the one-time effect relating to the customer retention period, revenues remained at the prior year level.

Data communications revenues benefited from a number of developments including higher revenue from the intragroup settlement of services provided for the Business Customers strategic business area due to the transition to capacity-based business models. Overall, revenue generated by this business area rose by 2.6 percent to EUR 1.3 billion.

Value-added services revenue decreased by EUR 124 million to EUR 945 million, mainly due to a new billing model for the Premium Rate Service product, where all revenue was billed based on commission from January 2006 onwards. Otherwise, traditional services such as public telephony and directory inquiries declined.

Revenues from terminal equipment declined by EUR 92 million to EUR 333 million due to the decrease in the rental business. As terminal equipment prices have dropped dramatically in recent years and terminal devices are increasingly sold at a reduced price as part of complete packages involving lines and calling plans, there has been virtually no new business with rental devices.

Revenue generated outside Germany rose by EUR 64 million to EUR 2.9 billion, driven by buoyant customer growth in the broadband business in Western and Eastern Europe and the first-time consolidation of entities in Eastern Europe. Revenue in the Western European subsidiaries in Spain and France increased in 2006 by almost 50 percent year-on-year to EUR 350 million, which is attributable to the expansion in the broadband market.

Despite dynamic broadband growth and a number of smaller acquisitions in 2006, at EUR 2.5 billion Eastern European revenues remained 1.8 percent under the prior-year level due to competition and price pressure, which had a strong negative impact on the traditional fixed-network business. The first-time consolidation of the acquisitions delivered a revenue contribution of approximately EUR 50 million in 2006. The acquisitions served to further develop expertise in the field of IT and ISP solutions. Another positive effect came from the first-time full-year inclusion of Telekom Crne Gore (Montenegro), which has been part of Magyar Telekom since April 1, 2005. In all countries the traditional fixed-network business continues to be dominated by intense competition from mobile communications, compounded by increased competition in the consumer business from call-by-call, preselection, and cable providers. In Hungary, revenue was also impacted by a weak exchange rate.

In 2006, the Broadband/Fixed Network strategic business area recorded **adjusted EBITDA** of EUR 8.8 billion, down EUR 1.1 billion on the previous year. The main factors here were a revenue decline in the traditional fixed-network area, increased customer acquisition and marketing costs in the course of broadband expansion, and higher expenses in connection with developing and launching new products. These negative effects were only partially offset by lowering the costs of telecommunications services, maintenance, IT, billing, and bad debt losses.

In 2006, **EBITDA** including special factors amounted to EUR 7.2 billion, impacted by negative effects in the amount of EUR 1.6 billion. These mainly consisted of expenses for staff-related measures in connection with the early retirement scheme for civil servants, partial retirement and voluntary redundancy and severance payments.

Domestic adjusted EBITDA amounted to EUR 7.9 billion compared with EUR 8.9 billion in the previous year. This decline is principally the result of lower revenues in the traditional fixed-network business in Germany. Negative effects compared with the previous year included the change in the reporting of customer acquisition costs in the broadband area as well as higher costs in connection with the launch of new products such as T-Home, the new entertainment product, and the new VDSL network. EBITDA was positively impacted by cost reduction measures, optimized data processing systems and improved receivables management. Billing and collection costs as well as maintenance costs also decreased. Savings were also made on revenue-related costs such as telecommunication services. In addition, other operating income resulting from the transfer of Telekom Direkt from Group Headquarters & Shared Services to the management control of T-Com had a positive impact on adjusted EBITDA. The transfer also improved sales support.

Domestic EBITDA in 2006 was EUR 6.4 billion, impacted by expenses in connection with early retirement arrangements for civil servants (EUR 1.1 billion), voluntary redundancy and severance payments (EUR 0.2 billion), and top-up payments for the partial retirement scheme (EUR 0.2 billion).

Outside Germany, adjusted EBITDA declined by EUR 65 million to EUR 849 million. This was primarily attributable to targeted advertising and sales activities, the change in the recognition of customer acquisition costs, and continued network expansion in Western Europe. At EUR 1.0 billion, adjusted EBITDA in Eastern Europe remained at the prior year level.

In 2006, the Broadband/Fixed Network strategic business area generated profit from operations **(EBIT)** of EUR 3.3 billion compared with EUR 5.1 billion in the prior year. The decline is mainly attributable to the aforementioned special factors in the amount of EUR 1.6 billion. Adjusted for special factors, EBIT in 2006 amounted to EUR 4.9 billion, EUR 0.9 billion lower than in the previous year. This decline was primarily due to the development of EBITDA in the reporting year. Despite the increase in capital expenditure, the decrease in depreciation, amortization and impairment losses due to the expiration of the depreciation or amortization periods of a number of assets had an offsetting effect.

At the reporting date, the number of employees at Broadband/Fixed Network had declined by 7,481 full-time equivalents (FTEs) to 103,786 FTEs. In Germany, the headcount was reduced by 6,406 FTEs to 82,112 FTEs. Despite several acquisitions, the number of employees outside Germany dropped by 1,075 FTEs, mainly due to optimized performance processes and the outsourcing of services.

Business Customers (T-Systems).

At EUR 9.1 billion, **net revenue** in the 2006 financial year remained at the prior-year level. The encouraging stabilization of net revenue was the result of positive trends in the Enterprise Services business unit, where net revenue was up year-on-year by 2.9 percent or EUR 0.1 billion. By contrast, Business Services recorded a decline in revenue of 3.2 percent to EUR 4.1 billion, down some EUR 0.1 billion on the prior year. In particular, Systems Integration, which is part of the Enterprise Services business unit, increased net revenue by 23.1 percent in the 2006 financial year, predominantly due to the consolidation of gedas AG from March 31, 2006 onwards. Revenues from PC workstation-related services rose 3.5 percent year-on-year. However, this encouraging net revenue trend was unable to offset the decline in revenues from telecommunications services – for both multinational business customers in the Enterprise Services business unit and medium-sized customers in the Business Services unit. The decline in revenue from telecommunications services is primarily due to continuing competition in the market. The sustained good performance in IP, the implementation of the IT strategy for small and medium-sized enterprises, and the reacquisition of customers for telecommunication services did not fully offset the decline in traditional data communication services at Business Services.

Intersegment revenue generated by the Business Customers strategic business area decreased by 6.1 percent or EUR 0.2 billion. This is mainly due to a decline in business with existing customers in connection with PC workstation-related services within the Deutsche Telekom Group, resulting from the IT cost-savings program and the reduction in the number of employees.

Despite substantial savings from improved procurement terms and conditions, Business Customers **EBITDA** decreased by EUR 1.3 billion or 96.1 percent year-on-year to EUR 51 million. The negative special factors affecting EBITDA of EUR 1.2 billion in the 2006 financial year were EUR 0.9 billion higher than in the previous year. They mainly relate to measures in connection with restructuring expenses, early retirement pensions, and provisions for onerous contracts.

In the 2006 financial year, the Business Customers strategic business area (T-Systems) generated **adjusted EBITDA** of approximately EUR 1.2 billion, down 22.4 percent compared with the previous year. The decline was attributable to both Business Services and Enterprise Services. Adjusted EBITDA at Enterprise Services decreased by 10.7 percent, mainly due to continued competitive pressure and the resulting offer of discounts. Any contract extensions and new contracts hence yielded lower margins. Adjusted EBITDA at Business Services by decreased 83.5 percent year-on-year. Here, too, the main reasons were the competition situation and the introduction of new but lower-margin products.

A **loss from operations (EBIT)** of EUR 0.9 billion was recorded in the reporting year, a change of EUR 1.3 billion from the profit recorded in the prior year. This was due in particular to a slight decline in revenue and higher expenses for staff-related measures.

Group Headquarters & Shared Services.
At EUR 0.3 billion, **net revenue** generated by Group Headquarters & Shared Services increased by around 21 percent year-on-year. The increase is mainly due to Real Estate Services, which saw an increase in rentals to third parties, and DeTeFleetServices which generated higher proceeds from the sale of used vehicles to bring down the average age of the vehicle fleet. Net revenue accounted for approximately 9 percent of total revenue.

Intersegment revenue also increased slightly to EUR 3.3 billion, mainly due to higher revenues at Vivento resulting from continued business expansion at Vivento Customer Services and Vivento Technical Services. In addition, DeTeFleetServices revenue was up marginally because of an increase in the average number of fleet vehicles. Intersegment revenues generated by the shared service Real Estate Services also rose slightly, largely due to the transfer of facility management activities from the strategic business areas to Real Estate Services. However, these increases were partially offset by a decline in the billing volume of the real estate group vis-à-vis the strategic business areas, caused by lower service volumes and prices as well as the impact of new leasing agreements with the strategic business areas.

Adjusted EBITDA decreased from EUR –0.3 billion to EUR –0.4 billion year-on-year. This is primarily due to lower volume and price-related billing volumes in the real estate area that were not balanced out by revenue increases in the low-margin facility management business and higher proceeds from property sales. Despite an increase in revenues, EBITDA at Vivento did not improve. Although EBITDA benefited from lower staff-related costs due to the reduced headcount at Vivento, this positive effect was offset by higher expenses relating to business expansion and the transfer of Telekom Direkt from Vivento to the Broadband/Fixed Network strategic business area in the first quarter of 2006. In addition, EBITDA benefited from the reversal of a provision in connection with the housing assistance program (Wohnungsfürsorge), after the pending arbitration proceedings between Deutsche Telekom AG and Deutsche Post AG were resolved by an arbitral award in the first quarter of 2006. This positive effect was however offset by higher expenses for centralized marketing and IT measures.

Unadjusted EBITDA declined year-on-year by EUR 1.2 billion to EUR –1.1 billion as a result not only of the development of adjusted EBITDA, but also of the increase in special factors negatively affecting EBITDA. Special factors in the reporting period had a negative net effect of EUR 0.7 billion and included primarily expenses for voluntary redundancy and severance payments, early retirement, and partial retirement. In the previous year, special factors had a positive net effect of EUR 0.4 billion, mainly attributable to the reversal of provisions as a result of the reduction in future liabilities relating to the annual deficit compensation for the Civil Service Health Insurance Fund (PBeaKK; EUR 0.8 billion). Income from insurance refunds and transfer payments to Vivento also had a positive effect in 2005. These positive effects on earnings in the prior year were offset by charges and provisions for severance and voluntary redundancy payments already implemented and those arising in conjunction with the Group's planned staff-restructuring measures, as well as expenses for other staff-related measures, of approximately EUR 0.3 billion. Expenses related to a capital increase for the Deutsche Telekom Foundation also had a negative impact of EUR 0.1 billion in 2005.

At EUR 1.3 billion, the adjusted loss from operations **(EBIT)** was slightly down on the previous year, mainly due to the aforementioned effects of the decrease in adjusted EBITDA. Unadjusted EBIT in the 2006 financial year was EUR –2.0 billion, reflecting above all the causes of the decrease in unadjusted EBITDA.

The Board of Management proposes a dividend of EUR 0.72.
In general, internationally operating groups focus their reporting on their consolidated financial statements. However, dividend payments at Deutsche Telekom are based on the single-entity financial statements of Deutsche Telekom AG*. Under the German Stock Corporation Act (Aktiengesetz – AktG), the amount payable to shareholders as a dividend is based on unappropriated net income as reported by Deutsche Telekom AG in its German GAAP annual financial statements. The Board of Management proposes that a dividend of EUR 0.72 per no par value share carrying dividend rights be paid from the unappropriated net income amounting to EUR 3,160 million, and that the remaining balance be carried forward.

* The single-entity financial statements of Deutsche Telekom AG will continue to be prepared in accordance with the accounting principles under the German Commercial Code. The single-entity financial statements of Deutsche Telekom AG are published in the electronic Federal Gazette (Bundesanzeiger) and can also be accessed on the website of the register of companies. The financial statements are available upon request from Deutsche Telekom, Investor Relations, Postfach 2000, D-53105 Bonn, Germany, fax + 49 (0) 228 181-88899.

Net worth and financial position of the Group.

In 2006, total assets of the Deutsche Telekom Group increased year-on-year by 1.3 percent or EUR 1.7 billion to EUR 130.2 billion.

On the **asset side,** the increase is primarily attributable to a rise in intangible assets of EUR 5.3 billion, partly offset in particular by a decline of EUR 2.2 billion in cash and cash equivalents and a decrease of EUR 1.9 billion in property, plant and equipment. The growth of intangible assets mainly reflects the acquisition of additional FCC mobile communications licenses in the United States (approximately EUR 3.3 billion) as well as the first-time consolidation of gedas, tele.ring, and PTC. This was partly offset, in particular, by exchange rate effects (EUR 1.9 billion). The decrease in property, plant and equipment was mainly due to total depreciation expenses exceeding investments, as well as exchange rate effects.

Investments in property, plant and equipment, and intangible assets (excluding goodwill) increased by a total of EUR 1.7 billion year-on-year to approximately EUR 12.0 billion. Investment mainly centered on the acquisition of additional mobile communications licenses. Higher capital expenditure also resulted from the roll-out of the high-speed network in the Broadband/Fixed Network strategic business area. More than half of the investments were made in Mobile Communications and Broadband/Fixed Network, predominantly in the United States and Germany. The high level of investments in the prior year related primarily to the purchase of networks in California and Nevada.

In 2006, cash and cash equivalents were used mainly for the acquisition of mobile communications licenses, the payment of the dividend, the acquisition of tele.ring, gedas and PTC, as well as the repayment of bonds. In addition to the free cash flow, the issuance of bonds and medium-term notes had an offsetting effect.

The increase in **liabilities and shareholders' equity** was attributable to a rise in shareholders' equity of EUR 1.1 billion and a total increase of EUR 0.6 billion in provisions. The increase in shareholders' equity was mainly attributable to net profit and the conversion of the mandatory convertible bond. Offsetting factors included not only the distribution of the dividend and negative exchange rate effects on the currency translations of financial statements prepared in foreign currencies recognized under other comprehensive income, but also treasury shares previously acquired under a share buy-back program. Current and non-current provisions in total rose EUR 0.6 billion year-on-year. This increase mainly reflects additions to provisions for employee expenses.

Consolidated balance sheet *

as of Dec. 31 of each year	2006 millions of €	2006 %	2005 millions of €	2005 %	Change millions of €	2004 millions of €	2004 %
Assets							
Current assets	**15,951**	**12.3**	**16,668**	**13.0**	**(717)**	**18,864**	**15.0**
Cash and cash equivalents	2,765	2.1	4,975	3.9	(2,210)	8,005	6.4
Trade and other receivables	7,753	6.0	7,512	5.8	241	6,731	5.3
Miscellaneous assets	5,433	4.2	4,181	3.3	1,252	4,128	3.3
Non-current assets	**114,209**	**87.7**	**111,800**	**87.0**	**2,409**	**106,614**	**85.0**
Intangible assets	58,014	44.6	52,675	41.0	5,339	50,745	40.5
Property, plant and equipment	45,869	35.2	47,806	37.2	(1,937)	46,294	36.9
Miscellaneous assets	10,326	7.9	11,319	8.8	(993)	9,575	7.6
Total assets	**130,160**	**100.0**	**128,468**	**100.0**	**1,692**	**125,478**	**100.0**
Liabilities and shareholders' equity							
Current liabilities	**22,088**	**17.0**	**24,958**	**19.5**	**(2,870)**	**26,272**	**20.9**
Financial liabilities	7,683	5.9	10,374	8.1	(2,691)	12,592	10.0
Trade and other payables	7,160	5.5	6,902	5.4	258	6,116	4.9
Provisions	3,093	2.4	3,621	2.8	(528)	3,546	2.8
Other liabilities	4,152	3.2	4,061	3.2	91	4,018	3.2
Non-current liabilities	**58,402**	**44.9**	**54,911**	**42.7**	**3,491**	**53,694**	**42.8**
Financial liabilities	38,799	29.8	36,347	28.3	2,452	38,498	30.7
Provisions	9,341	7.2	8,203	6.4	1,138	7,571	6.0
Other liabilities	10,262	7.9	10,361	8.0	(99)	7,625	6.1
Shareholders' equity	**49,670**	**38.1**	**48,599**	**37.8**	**1,071**	**45,512**	**36.3**
Total liabilities and shareholders' equity	**130,160**	**100.0**	**128,468**	**100.0**	**1,692**	**125,478**	**100.0**

* Prior-year comparatives for the items other current assets, non-current provisions, and shareholders' equity have been adjusted to reflect the change in policy in accounting for actuarial gains and losses. For further details, please refer to Note 29 in the consolidated financial statements.

Deutsche Telekom's **financial management** ensures the Group's ongoing solvency and hence its financial equilibrium. The fundamentals of Deutsche Telekom's financial policy are established each year by the Board of Management and overseen by the Supervisory Board. Group Treasury is responsible for implementing the finance policy and for ongoing risk management.

The primary instruments used for the Group's medium to long-term financing are bonds and MTNs. The main additions in 2006 were a EUR 1.5 billion fixed-interest bond, a USD 2.5 billion bond in two fixed-interest tranches of USD 0.5 billion and USD 1 billion and a variable-interest tranche of USD 1 billion, a EUR 750 million MTN, five MTNs each worth EUR 500 million, a EUR 20.8 million MTN, a GBP 250 million MTN, and a HUF 47.4 billion European Investment Bank credit. The individual terms and conditions for the most important financial instruments are explained in the notes to the consolidated financial statements under Note 25 "Financial liabilities."

A liquidity reserve in the form of credit lines and cash is maintained to guarantee the solvency and financial flexibility of Deutsche Telekom at all times. For this purpose, the Company entered into standardized bilateral credit agreements with 29 top-ranked banks amounting to a total of EUR 17.4 billion. The bilateral credit agreements have a maturity of 36 months and can, after each period of 12 months, be extended by a further 12 months to renew the maturity of 36 months. EUR 6 million had been drawn down as of December 31, 2006.

To manage its financial stability Deutsche Telekom essentially uses two key performance indicators: gearing and relative debt. One component of the indicators is net debt, which Deutsche Telekom uses as an important indicator for investors, analysts, and rating agencies.

Net financial liabilities increased in the reporting year from EUR 38.6 billion to EUR 39.6 billion. Major factors contributing to this development included investments in FCC licenses and payment of the purchase price for gedas, tele.ring, and PTC. This was offset, in particular, by the free cash flow and currency translation effects related mainly to liabilities denominated in U.S. dollars.

All of the major rating agencies have given Deutsche Telekom AG a single A– long-term rating. Standard & Poor's has changed the outlook from "stable" to "negative," but the other major rating agencies regard the outlook as "stable."

Net debt*

millions of €, as of Dec. 31 of each year	2006	2005	2004
Bonds	36,288	37,255	39,820
Liabilities to banks	2,348	2,227	3,082
Promissory notes	680	645	651
Liabilities from derivatives	562	678	1,159
Lease liabilities	2,293	2,373	2,487
Liabilities arising from ABS transactions	1,139	1,363	1,563
Other financial liabilities	377	106	79
Gross debt	**43,687**	**44,647**	**48,841**
Cash and cash equivalents	2,765	4,975	8,005
Available-for-sale/held-for-trading financial assets	122	148	120
Derivatives	359	445	396
Other financial assets	886	440	407
Net debt	**39,555**	**38,639**	**39,913**

* Net debt is used by senior operating decision-makers at Deutsche Telekom as a key financial figure to manage and control debt. Although many of Deutsche Telekom's competitors use this measure, its definition may vary from one company to another.

Financial security*

as of Dec. 31 of each year	2006	2005	2004
Gearing Net debt / Shareholders' equity	0.8	0.8	0.9
Relative debt Net debt / EBITDA (adjusted for special factors)	2.0	1.9	2.0

* Calculated and rounded on the basis of millions for the purpose of greater precision.

Long-term rating of Deutsche Telekom AG

	Standard & Poor's	Moody's	Fitch
2004	BBB+	Baa1	A–
2005	A–	A3	A–
2006	A–	A3	A–
Outlook	negative	stable	stable

Consolidated cash flow statement (condensed) [a]

millions of €	2006	2005	2004
Net cash from operating activities	**14,195**	**14,998**	**16,720**
Cash outflows for investments in intangible assets (excluding goodwill) and property, plant and equipment	(11,806)	(9,269)	(6,410)
Free cash flow (before dividend payments) [b]	2,389	5,729	10,310
Net cash used in investing activities	**(14,278)**	**(10,058)**	**(4,501)**
Net cash used in financing activities	**(2,061)**	**(8,039)**	**(12,881)**
Effects of exchange rate changes	(66)	69	(17)
Net decrease in cash and cash equivalents	(2,210)	(3,030)	(679)
Cash and cash equivalents	2,765	4,975	8,005

[a] Calculated and rounded on the basis of millions for the purpose of greater precision.

[b] Deutsche Telekom is of the opinion that the “free cash flow (before dividend payments)” indicator is used by investors as a measure to assess the Group’s net cash from operating activities after deduction of cash outflows for investments in intangible assets (excluding goodwill) and property, plant and equipment, in particular with regard to subsidiaries, associates, and joint ventures, and the repayment of liabilities. “Free cash flow (before dividend payments)” should not be used to determine the financial position of the Group. There is only limited comparability between Deutsche Telekom’s definition of free cash flow and methods of calculating this measure and similarly designated measures and disclosures of other companies.

Net cash from operating activities.
Net cash from operating activities amounted to EUR 14.2 billion in the reporting period, compared with EUR 15.0 billion in the prior year. This decrease is predominantly due to the decline in profit from operations. This effect was partially offset by lower net interest payments and changes in working capital.

Net cash used in investing activities.
Net cash used in investing activities totaled EUR 14.3 billion as compared with EUR 10.1 billion in the same period in the previous year. This increase was mainly caused by cash outflows for intangible assets which were up by EUR 2.8 billion; the purchase of FCC licenses at T-Mobile USA in particular accounted for EUR 3.3 billion. In addition, cash inflows from non-current assets (disposal of shares) decreased by EUR 1.4 billion. While inflows of EUR 1.6 billion were recorded in 2005 from the sale of shares in MTS, comdirect, Intelsat and DeASat, inflows of only EUR 0.2 billion were recorded in 2006 for the prior sale of shares in Celcom.

Net cash used in financing activities.
Net cash used in financing activities amounted to EUR 2.1 billion in the reporting period, compared with EUR 8.0 billion in the prior year. This decrease is mainly attributable to an increase in proceeds from the issue of financial liabilities of EUR 1.4 billion and to a reduction in repayments of current and non-current financial liabilities of EUR 5.5 billion; this was partly offset by an increase in dividend payments of EUR 0.3 billion and a share buy-back amounting to EUR 0.7 billion following the merger of T-Online International AG into Deutsche Telekom AG.

Statement on business development in 2006.
For Deutsche Telekom, the 2006 financial year was marked by rapid technological change and tough competition in the telecommunications industry. These developments were driven by two opposing trends: While Deutsche Telekom’s international sales markets enjoyed favorable development, the telecommunications market in Germany was burdened by rapidly falling prices.

Research and development.

Focus on innovation activities // 5i as key elements of our research and development strategy // Positive development at Deutsche Telekom Laboratories // Successful innovation transfer to the strategic business areas // Innovations successfully launched on the market

Innovation activities that focus intensely on customer requirements are Deutsche Telekom Group's key factor in becoming the leading service provider in the European telecommunications and information technology industry. This is why we are continually on the lookout for and developing top-quality, highly efficient, innovative products and services. Our goal is to deliver the highest possible benefit to our customers at all times.

Focus of innovation activities in the Group.
Innovation activities are managed overall by the realigned Innovation, Research & Development central department, which is responsible for the innovation strategy, innovation management across the Group, innovation marketing, Group-wide research and development, and corporate venture capital.

The department derives the Group's innovation strategy from systematically gleaned knowledge of customers, technologies and markets, and thus guarantees a holistic view. The major topics of innovation the Group will concentrate on in 2006 and the future are IPTV, mobile Internet and ICT services. In addition, the Group is systematically tapping the potential for fixed-mobile convergence products and innovative business ideas such as IP value-added services.

Central innovation management ensures the successful transfer of innovation strategies, and research and development activities to the market via our strategic business areas.

Innovation marketing creates insights, both internally and externally, into the Group's portfolio for the future, while generating synergy effects, impetus, and new ideas. T-Gallery is a forward-looking forum that enables products and services to be experienced from a customer perspective. With these products and services, Deutsche Telekom intends to shape the day-to-day lives of its consumers in the future and promote the development of the society of tomorrow. Thanks to the work done in this area, major savings and efficiency potentials have been identified and a large number of new projects and business models launched to promote new business for the future.

Two important organizational innovation units, real drivers of innovation, complement the Group's future-oriented approach: Deutsche Telekom Laboratories acts as a central research and development unit, while the venture capital company T-Venture finances and supports innovative start-ups in the telecommunications and IT sectors.

5i as key elements of research and development activities.
In 2006, Deutsche Telekom once again concentrated its research activities on the five existing areas of innovation (known as 5i):

- Inherent Security meets customers' demands for end-to-end security of their communication applications. Deutsche Telekom identifies technologies and applications to offer network-based security solutions. Harmful software programs are stopped before they get near the PC, connections are secure, and the backbone network hardware is made failsafe. Users are able to identify with whom they are communicating so that they can execute secure transactions or conclude agreements.

- Intuitive Usability ensures that services and functions that are currently still complicated to use will be easy for all customers to use in the future. Services and functions are to be adapted to the needs of users and not the other way round.

- Intelligent Access aims to ensure that customers are offered the best service available, independent of the terminal device used – anywhere at any time and without requiring action on their part. Users are no longer forced to establish complex connections to the network manually – the network does it for them automatically.

- Integrated Communication focuses on relieving people of routine tasks through the automatic technical networking of everyday objects and the automatic integration of electronic object and Internet information.

- Infrastructure Development expands and optimizes technological platforms to satisfy customer needs in terms of bandwidth, mobility, and security as efficiently as possible.

Positive development at Deutsche Telekom Laboratories.
Launched in 2005, Deutsche Telekom Laboratories established itself as a central research and development institute and an international science institution in the course of 2006. This is underlined by the continuous flow of project results to the strategic business areas as well as the regular contribution of technical papers to scientific publications.

Deutsche Telekom Laboratories is divided into two areas: the Innovation Development Laboratory and the Strategic Research Laboratory. Both are organized to ensure the uninterrupted transfer of knowledge and findings from academic research into product design in the Group's business areas.

To this end, the Innovation Development Laboratory has become the Group's general contractor for applied research and development. On the basis of the five innovation areas (5i), it manages Deutsche Telekom's R&D portfolio and prepares the ground for new products and services. It develops and assesses innovative ideas, implements test environments, demonstrators, and prototypes, costs business models, and transfers results into the business areas.

The Strategic Research Laboratory carries out long-term and applied fundamental research and technology research and through this sphere of activity provides important basic insights for the development of innovative products and solutions. To this end, the Berlin Technical University (TU Berlin) and Deutsche Telekom have set up four fields of research at the university, each under an endowed chair. The research topics include Usability, Security in Telecommunications, Service Centric Networking, and Intelligent Networks and Management of Distributed Systems.

Both areas also continued to expand their partner network. The first subsidiary university institute was established: Deutsche Telekom Laboratories at Ben Gurion University. This venture intensifies the cooperation, started in 2005, with Israel's Ben Gurion University and focuses its research there primarily on network security. Ben Gurion University is one of the world's top universities for research in this field. Initial results in the area of network security allow, for example, the identification and elimination of attackers, such as viruses and worms, in the network before they reach the computers or mobile phones of users.

Other ventures include the collaboration with the German Research Center for Artificial Intelligence (DFKI), Stanford University, whose Prof. Girod chairs the Steering Committee of Deutsche Telekom Laboratories, the Massachusetts Institute of Technology (MIT), and EPFL in Lausanne. Deutsche Telekom cooperates with German universities, including Leipzig University, where Deutsche Telekom sponsors an endowed chair for applied telematics/e-business, and Bonn University, where Prof. Buse holds the endowed Heinrich Hertz chair, which is financed by Deutsche Telekom.

Institutions such as the European Center for Information and Communication Technologies (EICT), which was founded in June 2006, also actively promote the consistent pooling of scientific and applied research with the development expertise of leading companies in industry. Deutsche Telekom Laboratories are the Group's interface to the EICT, a public-private-partnership company whose five founding partners – Deutsche Telekom, Siemens, DaimlerChrysler, Fraunhofer-Gesellschaft, and TU Berlin – pool research and development activities in the area of ICT and turn them into joint projects.

Intensive transfer of results to the strategic business areas.
The Group innovation unit at Deutsche Telekom's Headquarters and Deutsche Telekom Laboratories focus primarily on issues that are relevant to all strategic business areas and on new technologies that are expected to be launched or ready for the market in two to five years. The strategic business areas are primarily responsible for product innovations that are near to market launch, i.e., with a development lead time of up to 24 months.

The transfer of results, a decisive criterion for the success of the centralized Group innovation unit at Deutsche Telekom's Headquarters and Deutsche Telekom Laboratories, was driven forward in 2006 and significant results were integrated into the activities of the strategic business areas.

T-Mobile focuses on expanding mobile broadband communication.
The UMTS networks were upgraded in 2006 during the first roll-out phase of the HSDPA technology, which facilitates transmission rates of up to 1.8 Mbit/s. This technology is available to customers throughout the networks in Germany, the United Kingdom, the Netherlands, Austria, Poland and Hungary. The second roll-out phase, in which transmission rates of up to 3.6 Mbit/s will be achieved, was also launched during 2006.

T-Mobile started modernizing and improving its GSM network by upgrading the German network with the EDGE technology, which is expected to be concluded by the end of 2007. This allows broadband data communication with a speed four times that of ISDN, even in rural areas. It also enables customers who reside in large urban areas but do not yet use UMTS to use mobile broadband applications and T-Mobile's mobile Internet (web'n'walk). EDGE is also available in T-Mobile's networks in Croatia, Poland, the Czech Republic, Slovakia, Hungary and the United States.

The quality of voice communication will be continuously enhanced at the same time with the successful testing of the AMR wideband technology. In the first half of 2006, T-Mobile's quality lead was underlined by the "Mobile Operator of the Year" award it received for the seventh consecutive year from readers of "connect" magazine. The hugely successful T-Mobile@home package was launched in early 2006, enabling mobile communications to be used in the home at fixed-network costs.

In terms of terminal equipment, T-Mobile was the first operator in Europe to introduce the MDA Vario II, a compact, high-performance multi-media pocket computer that supports the broadband technologies GPRS, EDGE, UMTS, and WLAN, as well as HSDPA. The offer of a mobile notebook PC with fully integrated broadband functionality based on UMTS/HSDPA, which was promoted in cooperation with Fujitsu-Siemens, Sony, and other computer manufacturers, was aimed at business customers in particular. In addition to mobile services for business such as the push e-mail function or secure access to corporate intranets, T-Mobile has continually expanded its consumer range of web'n'walk-enabled devices for mobile Internet use.

Other innovations in 2006 included a new HotSpot service on London's Heathrow Express trains, which will enable travelers to use the Internet during their journey via WLAN with a long-distance connection on mobile broadband networks starting in early 2007, as well as the demonstration of mobile TV via DVB-H on pre-series mobile terminals during the FIFA 2006 World Cup™ in Germany. During this time, T-Mobile commercially launched mobile TV streaming (comparable with IPTV, see also T-Home from T-Com), facilitating mobile television viewing via UMTS, HSDPA, and EDGE.

Broadband/Fixed Network business area delivers important innovations to the market.
In the 2006 financial year, the Broadband/Fixed Network business area introduced compelling, forward-looking innovations, products, and services on the market. T-Com now provides broadband lines with transfer rates of between 1 and 16 Mbit/s to 93 percent of all access customers, an increase of 1.6 percent year-on-year. In its broadband strategy, T-Com not only envisages the expansion of the DSL network, but is also working on substantially increasing the performance of fast Internet connections. The most important infrastructure-related measure in 2006 was the roll-out of the high-speed VDSL-based network. The VDSL network installed in recent months will initially provide bandwidths of up to 50 Mbit/s in Germany's ten largest conurbations – Berlin, Hamburg, Hanover, Leipzig, Frankfurt, Düsseldorf, Cologne, Stuttgart, Munich, and Nuremberg – as well as in the cities of Offenbach and Fürth. This is enabling T-Com to systematically develop a new market that will allow it to offer innovative TV and broadband services in Germany as well.

T-Com's new complete packages (Max 06) proved to be a huge success, with around 3.6 million customers subscribing for one of the new packages in the three months since marketing began last September. By introducing T-Home, T-Com as the pioneer in Germany is following the key trend on European markets toward triple-play services and the related interest in bundled products. Subscribers to the T-Home complete packages have access to individually retrievable entertainment services, such as live TV, on-demand TV, pay TV, and video on demand. By connecting the broadband line to the customer's conventional television set via a media receiver, T-Home enables the broadcast of live television on the Internet. Besides the wide variety of programs on offer, T-Home allows users to tailor television viewing to their individual needs and schedules. IPTV sets new standards of convenience and comfort in particular. Additional services such as time-shift allow users to watch TV content whenever they wish. The bandwidth available can also display live TV in high definition (HD), and an electronic program guide and the picture-in-picture function (where several programs can be watched on a screen simultaneously) provide the ultimate in convenience. These technically sophisticated value-added services, which are revolutionizing television viewing, are designed for customers' ease of use.

The growing penetration of high-bit-rate lines is opening up opportunities for new business models such as for online games. Gamesload launched a range of games in time for the Games Convention that has been optimized for the image resolution of a television screen and can be played with the remote control. In November 2006, T-Com launched Softwareload, a new download portal for software programs. Softwareload provides a selection of more than 17,000 titles covering a range of applications. Following in the footsteps of the first two successful download platforms, Musicload and Gamesload, Softwareload is the third brand to join the T-Com product family in this segment. Another innovative product of 2006 is the test version of "t-community.com," a social community where customers can store their personal profiles and use features such as blog, chat, and media archives.

The unbundling of the DSL line from the telephone line was also announced in 2006. The market launch is planned for 2007. The new product will consist of the following core components: IP access, voice/data rate, non-voice services (voice/videobox, text messaging), and an integrated access device (IAD).

Localized and interest-specific web TV applications and services, based largely on user-generated content, will round off T-Com's broadband-based entertainment offering in 2007.

Business Customers business area focuses on driving new ICT solutions.
2006 saw the development of a large number of ICT innovations, their piloting at customers' premises and the start of marketing activities. Some of the areas our experts focused on were fixed-mobile convergence, the dynamic provisioning of the IT infrastructure and applications, as well as the industry-specific end-to-end optimization of business processes.

New solutions in the area of fixed-mobile convergence now bring together what used to be divergent communication channels in a company (fixed network, mobile communications, and Internet access) into an innovative integrated solution. For our customers and their employees, this leads in particular to better communication processes and productivity, e.g., through the seamless integration of mobile employees into all corporate processes. One example is Universal Secure Access solution developed for high-security, cross-network access to corporate networks. A further focus is on the integration of mobile handsets into PABXs. The solutions developed by T-Systems enable our customers to use the mobile handset as a fully operational extension in the stationary PABX.

Dynamic services was another focal point of the innovation activities. ICT managers in all companies are faced with the challenge of providing business units with adequate ICT resources at all times, without having to reserve unneeded, expansive capacity. The motto for the new dynamic services solutions is: “Only use and pay for what you really need – consistently secure, fast, and inexpensive.” Dynamic services works for many standard enterprise applications such as SAP®, Microsoft Navision®, Microsoft Exchange®, IBM Lotus Domino®, etc. and also for archiving solutions through to Web applications and databases. Enterprises can also use dynamic services for a large number of stand-alone applications.

Another area where substantial advances were made was the development of innovative solutions to support industry-specific processes. One example from the insurance sector: “Personalized vehicle insurance” has been developed as a solution for insurance companies on the basis of modern telematics. The solution will allow insurance companies to offer policies that are based on distances driven and driving behavior based on the principle that low-risk, low-mileage drivers pay lower insurance premiums. The first pilot project with a customer has been completed successfully.

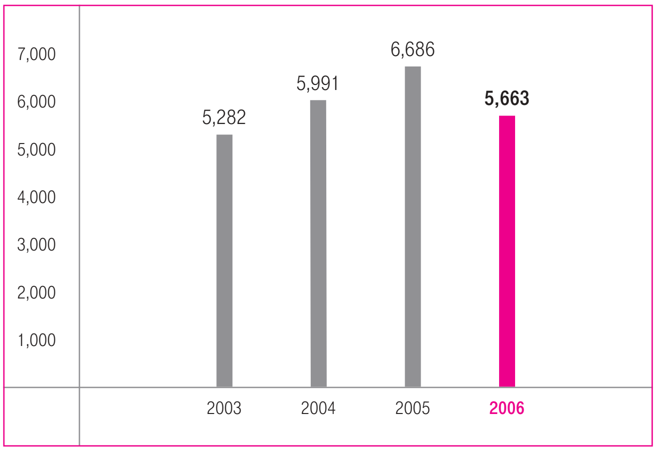
Research and development expenditure and investment.
Research and development expenditure amounted to EUR 0.2 billion in the 2006 financial year, the same level as in the previous year. Typical research and development activities included the development of new data transmission processes and innovative telecommunications products. The investments in internally generated intangible assets to be capitalized rose by EUR 0.1 billion year-on-year to EUR 0.3 billion. These investments principally relate to internally developed software, with the vast majority being attributable to the Broadband/Fixed Network and Mobile Communications business areas.

In the past financial year, over 2,200 employees were involved in projects and activities to create new products and market them efficiently to customers.

Patent applications and intellectual property rights.
In the market for mobile and fixed-network telephony, intellectual property rights play an extremely important role, both nationally and internationally. For this reason, the Group focuses intensively on in-house development and third-party acquisition of such rights.

The number of patent applications increased by around 35 percent year-on-year to 557. The intellectual property rights held (inventions, patent applications, patents, utility models, and design models) are reviewed on a regular basis and those rights that are no longer relevant are eliminated. This led to a reduction to 5,663 rights in the reporting year. Management of these intellectual property rights is governed by strict cost/benefit considerations.

Intellectual property rights



Employees.

Consistent staff restructuring ensures future viability // Socially responsible staff adjustments using a number of different tools // Vivento remains important vehicle for staff restructuring // Collective bargaining outcome aims to increase efficiency and productivity // T-Service to substantially improve customer service // Better management quality and service focus thanks to human resources development and culture change // Commitment to training remains high

In light of the immense changes in the market, the Group's human resources strategy in 2006 targeted three areas: staff restructuring, an improved personnel cost ratio, i.e., the ratio between personnel costs and revenue, and a focus on leadership quality and customer service.

Staff restructuring contributes to future viability.
As announced in 2005, Deutsche Telekom launched the necessary staff restructuring program. Under this program, around 32,000 employees in Germany are expected to leave the Group between 2006 and 2008. At the heart of this program is the provision of socially responsible staff restructuring tools such as partial retirement arrangements, voluntary redundancy and severance payments, and early retirement. Another key component of staff restructuring at Deutsche Telekom is the creation of new employment opportunities in promising market segments, such as the roll-out of the VDSL network. New employment opportunities will also be generated by the expansion of the T-Punkt organization through T-Punkt Vertriebsgesellschaft. This also includes the intensified marketing of products and services, and comprehensive customer support in the T-Punkt stores. The number of T-Punkt stores will increase further over the next few years to reinforce Deutsche Telekom's clear customer orientation and strengthen customer retention. Around 1,000 T-Punkt stores are to serve customers nationwide in the medium term. New jobs will be created as the T-Punkt organization expands. 1,000 new jobs were created in the T-Punkt stores in 2006, and more are to be added in the medium term. Overall, these activities and the roll-out of the VDSL network may create up to 8,000 additional jobs (some of them on a temporary basis), most of which will give existing employees the chance of future-safe jobs.

The adjusted personnel cost ratio in the financial year was 22.3 percent of revenue, representing a year-on-year decrease of 0.4 percentage points.

In addition to effects resulting from changes in the composition of the Group, the rise in personnel costs is attributable in particular to collectively agreed increases in wages and salaries as well as increased staff levels, primarily at T-Mobile USA.

In addition, expenses for staff-related measures totaled approximately EUR 2.8 billion in the 2006 financial year. These relate primarily to expenses for voluntary redundancy and severance payments (EUR 0.7 billion) and expenses in connection with early retirement arrangements for civil servants (EUR 1.8 billion). In the prior year, the expenses for staff-related measures amounted to around EUR 1.2 billion, mainly attributable to provisions for voluntary redundancy and severance payments for employees in the context of the staff restructuring program announced in the fourth quarter of 2005.

Workforce development (as of Dec. 31)

Employees in the Group	2006	2005	2004
Total	**248,800**	**243,695**	**244,645**
Of which: Deutsche Telekom AG	92,575	106,604	110,979
Broadband/Fixed Network	103,786	111,267	114,083
Mobile Communications	60,429	51,410	47,797
Business Customers	56,397	52,041	51,173
Group Headquarters & Shared Services	28,188	28,977	31,592
Breakdown by geographic area			
Germany*	159,992	168,015	170,951
International	88,808	75,680	73,694
Of which: other EU member states	45,144	37,273	38,736
Of which: rest of Europe	9,014	9,169	9,848
Of which: North America	31,049	27,851	23,788
Of which: rest of world	3,601	1,387	1,322
Net revenue per employee			
Development of productivity (thousands of €)	247	245	234

* The Scout24 group is reported under Germany. Prior-year comparatives have been adjusted.

Personnel costs in the Group

billions of €	2006	2005	2004
Personnel costs in the Group	16.5	14.3	13.3
Special factors	2.8[a]	1.2[b]	0.2[c]
Personnel costs in the Group, adjusted for special factors[d]	13.7	13.1	13.1
Net revenue	61.3	59.6	57.3
Adjusted personnel cost ratio (%)[d]	**22.3**	**21.9**	**22.9**

Special factors (billions of €):
[a] Expenses for staff-related measures (severance and redundancy payments, partial and early retirement arrangements etc.) at Broadband/Fixed Network (– 1.5), Business Customers (– 0.6), and Group Headquarters & Shared Services (– 0.7).
[b] Expenses for staff-related measures (severance and redundancy payments, partial retirement etc.) at Broadband/Fixed Network (– 0.6), Business Customers (– 0.2), Mobile Communications (– 0.1) and Group Headquarters & Shared Services (– 0.3).
[c] Expenses for staff-related measures, primarily at Broadband/Fixed Network (– 0.2).
[d] Calculated and rounded on the basis of millions for the purpose of greater precision.

Implementation of socially responsible staff adjustments using a number of different tools.

The Group uses a package of innovative human resources (HR) tools in its staff restructuring measures. Each measure is aimed at making any workforce reductions socially responsible.

A special voluntary redundancy payment program, "Abfindung spezial," formed a significant part of the package put in place to reduce surplus staff. This voluntary redundancy payment offer for employees of Deutsche Telekom AG aged between 40 and 55 was limited to the period March 1, 2006 through August 31, 2006. Deutsche Telekom AG offered eligible employees increased severance payments of up to EUR 225,000 if they agreed to leave the Group. As well as restructuring the workforce, this special voluntary redundancy program also aimed to bring down the high average age of the workforce, particularly at T-Com.

In addition, employees due to reach retirement age within the next two years were offered participation in the Pension minus 2 ("Rente minus 2") early retirement plan, under which Deutsche Telekom compensates for 50 percent of any shortfalls in the employee's pension as a result of early retirement with a special credit that is paid into the company pension scheme. Another attractive offer for employees and civil servants approaching retirement is the partial retirement program.

The need for rationalization also applies to the Business Customers strategic business area, which has launched its own range of measures to encourage staff restructuring, in particular at the T-Systems Enterprise Services business unit. These include customized severance packages tailored to the needs of the unit and arrangements for partial retirement and early retirement. T-Systems Enterprise Services offered employees three times the standard severance payment until the end of July 2006, and two times the standard amount until December 2006. Similar offers have also been made to employees at T-Systems Business Services. DeTe Immobilien is likewise participating in the staff restructuring process, and successfully offered its own voluntary redundancy models based on the programs offered at Deutsche Telekom AG.

Civil servants are also included in the staff restructuring process. The Second Act to Amend the Act for the Improvement of the Staff Structure at the Residual Special Asset of the Federal Railways and the Successor Companies of the Former Deutsche Bundespost (Zweites Gesetz zur Änderung des Gesetzes zur Verbesserung der personellen Struktur beim Bundeseisenbahnvermögen und in den Unternehmen der Deutschen Bundespost) came into effect on November 16, 2006. One of the aims of this Act is to help correct the negative consequences of a structural feature of the successor companies to Deutsche Bundespost. These companies employ a high proportion of civil servants in Western Germany, while staff covered by collective agreements make up the majority of the workforce in Eastern Germany. The Act allows Deutsche Telekom to include its civil servants in the staff restructuring process in a socially responsible manner. The law will not affect the federal budget. According to this law, civil servants of all service grades who are working in areas where there is a surplus of staff and for whom employment in another area is not possible or cannot reasonably be expected in line with civil service legislation will be able to apply for early retirement from the age of 55.

The workforce has responded well to these offers, which are designed to avoid compulsory redundancies. By the end of 2006, Deutsche Telekom had implemented around one-third of the overall workforce reduction plan which runs until 2008. In addition to natural attrition and the deconsolidation of parts of the Vivento business models, this was achieved in particular through voluntary measures. Approximately 8,700 employees decided to leave the Company on the basis of the available voluntary workforce reduction instruments. In addition, numerous contracts have been signed, which will lead to employees leaving in 2007.

Vivento remains an important vehicle for staff restructuring.

Vivento, the internal service provider for managing surplus staff and employee placement, continues to play an important role in staff restructuring. Vivento is the driving force behind the Group's internal labor market, and a number of its forward-looking projects have had a significant influence on shaping staff restructuring in the Deutsche Telekom Group.

By liaising with the Group, Vivento was able to continually match staff surpluses to vacancies to optimize the pre-placement of staff between the strategic business areas, i.e., the placement at an early stage of employees affected by restructuring measures in vacancies in the Group before these employees are transferred to Vivento. Employment opportunities are also sought outside the Group.

In the second quarter of 2006, Vivento established Vivento Interim Services GmbH, whose aim is to fill temporary gaps caused by staff restructuring where no other suitable employees are available. The newly formed company is staffed by junior Deutsche Telekom employees on fixed-term contracts who have successfully completed their training but have yet to find a follow-up position and can thus gain further professional experience in the Group through Vivento Interim Services.

In a ruling dated June 22, 2006, the German Federal Administrative Court clarified the legal situation regarding the transfer of civil servants to Vivento, declaring the transfer not legally permissible. Since then, no more civil servants have been transferred to Vivento. The situation for the civil servants already transferred will remain unchanged – they will stay at Vivento and will continue to be given temporary employment or a new permanent position inside or outside the Group. The transfers made to Vivento to date are legally valid because the transfer process is completed.

Staff restructuring at Deutsche Telekom nevertheless continued as before, covering non-civil servants and civil servants alike. For civil servants who are affected by rationalization measures and for whom transfer to Vivento is impermissible according to the ruling of the German Federal Administrative Court, the original organizational unit will use Vivento's expertise to offer them counseling and job placement services.

The deconsolidation of five locations of Vivento Customer Services GmbH – Aachen, Dresden, Halle, Lübeck, and Magdeburg – is the first step in the sale of Vivento business models as announced in 2004 and a continuation of Deutsche Telekom's staff restructuring. Around 600 employees were transferred to walter ComCare, a company of the walter TeleMedien group. This transfer of operations as of December 1, 2006 was accompanied by a contract commitment and therefore safeguards the jobs of the staff concerned until the end of 2011. Further sales of Vivento locations and business models are planned to ensure that the Group remains efficient and competitive in the long term by focusing on its core business and optimizing structures.

Collective bargaining agreement aims to increase efficiency and productivity.
The collective bargaining agreement that Deutsche Telekom AG reached in its negotiations with the trade unions will lead to an increase in productivity and thus safeguard the Group's position in the face of fierce competition. For employees covered by collective agreements, the agreement provides for a one-time payment of EUR 350, a pay freeze until October 2006, and a 3-percent increase in salaries starting November 2006. The collective wage agreement will run for 16 months until July 31, 2007. Separate arrangements have been agreed for civil servants, including a one-time payment of up to EUR 735 depending on their salary grade. To improve productivity and thus enhance competitiveness, paid breaks for staff using workstation monitors were reduced and paid recuperation times abolished in some areas. This has helped to cushion the cost of the pay increase. The additional capacity generated by these measures will then be used to reduce outsourcing to third parties in the areas of services and installation going forward.

T-Service to substantially improve and professionalize customer service.
Deutsche Telekom is planning a range of measures to make customer service more efficient and align it even more closely with its customers' needs. In 2007 around 45,000 employees are to be transferred from T-Com as part of the T-Service project. These employees will come from the technical service units and call center units. Concentrating these service units enables Deutsche Telekom to focus on the quality of its service under conditions that reflect the market situation. The aim is to safeguard the competitiveness of the Company and, at the same time, protect jobs in the Group. The Group also aims to systematically align working conditions and remuneration systems with market levels.

Human resources development for improved management quality and heightened service focus.
Human resources development at Deutsche Telekom in 2006 focused on continuing the STEP up! program (Systematic & Transparent Executive Development Program) and introducing Go Ahead!, a staff development program for expert careers. In addition, the Company drove forward its staff restructuring with demand-based training.

The first measures under the STEP up! program started at the end of 2005. STEP up! is a Group-wide program for the development of executive staff. The program ensures an end-to-end perspective, which integrates all the steps in the process from recruitment to executive development, through to target management and personnel marketing. STEP up! creates uniform standards and procedures for executive development to be applied throughout the Group, thus ensuring that development and staffing processes become highly transparent to all concerned. The Group is committed to a policy of systematically encouraging top performers and high potentials. The full implementation of the program for all executives, including those at the Group's international subsidiaries, is set to be completed by the end of 2007.

Deutsche Telekom recognizes the importance of advancement for experts as a way to meet changing market requirements while offering interesting career prospects to valued employees. Go Ahead! is a special framework model established by the Group together with employee representatives, which takes tried-and-trusted HR development tools and refines them for the targeted development of expert careers. A focus on service as a vital general skill is being increasingly promoted in all expert careers. With its systematic, Group-wide career architecture, Go Ahead! is a roadmap for expert careers within the Deutsche Telekom Group. Go Ahead! clearly demonstrates how much Deutsche Telekom values the abilities and skills of its professional employees and proves that it offers them the same degree of development opportunities as executives.

Telekom Training, the Group's in-house provider of further training, offers training programs for expert and executive staff. Demand-based training aligned with its staff restructuring and strategic HR development play a critical role in this regard. Even with major projects – such as seminars on the development of the new VDSL high-speed network – training is tailored to demand.

In the past financial year, a total of 150,533 employees took part in 16,061 seminars. Classroom seminars were increasingly replaced by e-learning components and web-based training, and prepared and complemented by virtual classrooms and conference rooms.

Further training provided by Telekom Training

	2006	2005	2004
Seminars	16,061	12,826	14,109
Participants	150,533	122,379	95,705
Participant days	393,962	403,178	295,168
Global Teach sessions *	707,743	555,696	744,229

* Global Teach is an in-house e-learning platform.

Introduction of the Code of Conduct as an element of culture change.

On April 19, 2006, Deutsche Telekom introduced and implemented the Code of Conduct in all of its 111 majority shareholdings worldwide. This Code is applicable to the Group's entire workforce and lays down binding rules for value-oriented, legally correct behavior in day-to-day business. On the one hand, the Code of Conduct puts the Group's T-Spirit values into concrete terms, providing guidance on the Group's internal regulations for employees on the other. The Code of Conduct was developed in cooperation with the employee representatives. The value-oriented and law-abiding behavior of the Group and its employees is to promote trust in the Group in the long term. At the same time, we are fulfilling the requirements made of us as a company listed in the United States (Sarbanes-Oxley Act). A Group-wide Code of Conduct violations portal was introduced to give all employees and stakeholders the opportunity to report violations of the Code of Conduct. Implementation is measured on the basis of the annual, global employee survey, which was carried out for the first time in 2006. The Group's executives receive detailed training on this topic.

Number of suggestions for improvement increased again.

In the reporting year, the Deutsche Telekom Group generated savings of around EUR 74 million from a total of 8,600 suggestions for improvement (new submissions and subsequent approvals). The number of suggestions for improvement thus increased substantially again compared with the previous year.

Innovations

	2006	2005	2004
Number of suggestions for improvement	8,600	7,821	7,737
Savings (millions of €)	74	98	87
Number of patent applications	557	412	374

Commitment to training as a contribution to the future of German society.

On September 1, 2006, around 4,300 young people started their training at Deutsche Telekom in a total of twelve different professions and in various dual study courses. The Company has added a new vocational track, namely that of dialog marketing assistant which focuses on product and service advice and sales in call centers. Deutsche Telekom's training programs boast a high level of quality and a large number of participants. Every year, the chambers of commerce number Deutsche Telekom-trained staff among the best in their intake. Deutsche Telekom's training goes far beyond its own requirements. In 2006, some 1,000 trainees were taken on by the Group. At the end of 2006, Deutsche Telekom had about 11,700 trainees in Germany, meaning that trainees accounted for approximately 8 percent of its domestic workforce excluding Vivento.

Sustainability and environmental protection.

Group receives award for sustainability and climate protection // Purchasing renewable energy certificates helps protect the environment // International cooperation to identify resource-efficient technologies // Research and development lead to successful energy-saving projects

Deutsche Telekom considers climate protection one of the most important tasks of our time and is committed to implementing the Kyoto Protocol. The Group therefore aims to minimize the emission of greenhouse gases that are harmful to the climate by implementing a comprehensive package of strategies and actions. The main objective is to sever the link between power consumption and CO_2 emissions. Deutsche Telekom campaigns massively for reducing the emission of climate-impacting greenhouse gases in spite of rising energy consumption.

Award for sustainability and climate protection.
As an enterprise with international operations, Deutsche Telekom's goals are to maximize the sustainability of its management, tap potential for climate protection both within the Group and at customers and suppliers, and make a contribution to society as a whole with its environmental policy. Deutsche Telekom's sustainability strategy receives international recognition as demonstrated by its leading positions in the sustainability ranking of the Swiss agency INrate and in the sustainability ranking of the DAX companies based on a study by the Scoris rating agency published in January 2006 in the economics and finance magazine €uro.

CO_2 emissions reduced further with renewable energy certificates.
By taking a number of measures, Deutsche Telekom has already achieved a significant reduction in CO_2 emissions. The Group will continue to pursue such actions in the future. Through its inhouse service provider PASM (Power and Air Condition Solutions Management GmbH & Co. KG), Deutsche Telekom makes sure that it purchases environmentally friendly energy: By buying RECS (Renewable Energy Certificate System) certificates, PASM managed the procurement of one billion kilowatt hours of electricity from renewable energy sources with a virtually neutral impact on the climate in 2006. This corresponds to around one-third of the Group's total electricity consumption in Germany. Using RECS certificates, PASM aims to halve CO_2 emissions from power generation for Deutsche Telekom in Germany by 2010, compared with 1995 levels. In addition, the natural gas-powered fleet was actively expanded with the aim of reducing the Group's emissions. DeTeFleetServices runs the largest natural gas-powered fleet in Germany with more than 800 vehicles. The number of vehicles that run on alternative power is to be increased to 2,500 by 2009. Thanks to its climate protection efforts, Deutsche Telekom has been included in the KLD Global Climate 100 Index by KLD Research & Analytics Inc.

Approximately 100,000 additional tons of greenhouse gases were produced by the soccer World Cup in Germany. As one of the main sponsors of this event, Deutsche Telekom felt it had a responsibility to offset some of these emissions and therefore purchased emissions certificates for 20,000 tons of carbon dioxide, thus compensating for 20 percent of the emissions produced during the World Cup. The money paid for the certificates will go to two climate protection projects in South Africa that focus on renewable energies.

International cooperation for resource-efficient technologies.
As a member of ETNO (European Public Telecommunications Network Operators' Association), Deutsche Telekom is involved in a project to identify potential energy savings in digital switching technology. As part of this project, Deutsche Telekom wants to work together with system manufacturers to develop binding criteria for purchasing resource-efficient technologies that are easy to reuse or can be disposed of in an environmentally friendly manner.

Commitment to science and research.
Deutsche Telekom is promoting the development of environmentally friendly technologies by testing alternative sources of energy under real-life conditions: Firstly, Deutsche Telekom is working closely together with manufacturers in testing mobile and stationary fuel cells. T-Com, for instance, used environmentally friendly telestations run by fuel cells during the World Cup and tested them under live conditions. The innovative LED lamps of the telestations use around 50 percent less energy for the same light output. Secondly, a feasibility study commissioned by PASM successfully investigated the generation of heat, cooling, and power with geothermal energy. PASM is planning to analyze the research results as part of a pilot project.

Risk and opportunity management.

Continued price erosion in the core business // Growing importance of bundled products // Quality of service a success factor

The risk and opportunity management system.
Deutsche Telekom employs a holistic risk and opportunity management system so that it can systematically leverage its opportunities without losing sight of the related risks. In accordance with the Group's principles of risk management, risks are taken in a controlled manner – and only if an appropriate level of added value can be expected. The early identification, assessment, and management of risks and opportunities are an integral component of the Group-wide planning, control, and monitoring systems. Opportunities are analyzed primarily within the framework of strategy and innovation development activities. Deutsche Telekom attaches particular importance to detailed market studies, scenarios, projections, the relevant drivers and critical success factors, using them to derive specific potential opportunities for its strategic business areas and markets.

Risks and opportunities are regularly analyzed by the strategic business areas and also centrally at Group Headquarters. The risk early warning systems used in this process are based on prescribed Group-wide methods and are tailored to individual requirements. Potential deviations in the planning period are analyzed to determine the potential scope and probability of occurrence, using methods such as scenario modeling. The reference variables for the potential scope are the Group's target values (including EBITDA). The Group's "aggregate risk" is determined from the totality of the individual risks. The individual risks are aggregated into an overall risk potential using combination and simulation processes and taking probabilities of occurrence and correlations into account. An indicator system that captures all material risk areas is used to determine the change in aggregate risk. The analysis also includes what are known as "issues" – topics that could adversely affect the Group's image and reputation.

Reporting of the principal risks and opportunities is on a standard quarterly cycle, with additional ad hoc reports generated in the event of unexpected risks. Specific materiality thresholds for risks are defined for each reporting level. Corporate Risk Management is in charge of the methods and systems used for this Group-wide, standardized risk reporting system and ensures that it works efficiently. The Board of Management, Supervisory Board, and Audit Committee are informed on a quarterly basis about all material risks and the Group's overall risk position.

To reduce risks relating to fraud within the Group, Deutsche Telekom's Group Board of Management passed a resolution in 2005 to set up a standardized Group-wide anti-fraud management process. The tasks of this anti-fraud management process are to improve Group-wide structures for the prevention, exposure, and penalization of fraud in the Company and to ensure that these risks and the requirements placed on the Group are dealt with appropriately. Training and awareness-raising activities were held throughout the Group in 2006 and specific measures were introduced, for example in the field of procurement.

Deutsche Telekom also attaches particular importance to managing risks arising from financial positions. All treasury activities – in particular the use of derivatives – are subject to the principle of risk minimization. For this reason, all financial transactions and risk positions are managed in a central treasury system. The Group management is informed about these positions on a regular basis. Derivatives are used to hedge interest rate and currency exposures which could have an effect on cash flow.

Certain financial transactions require the prior approval of the Board of Management, which is also regularly briefed on the severity and amount of the current risk exposure. Simulations are performed using different market and worst case scenarios to estimate the effects of different conditions on the market. Selected derivative and non-derivative hedging instruments are used to hedge market risk, depending on the risk assessment. However, Deutsche Telekom only hedges the risks that affect the Group's cash flow. Derivatives are used exclusively as hedging instruments, i.e., not for trading or other speculative purposes.

The efficiency of risk management processes and compliance with the regulations and guidelines defined in Deutsche Telekom's Risk Management Manual are regularly reviewed by the Corporate Audit department. Within the scope of the legal mandate to audit the Company's annual financial statements, the external auditors examine whether the risk management system is able to identify at an early stage risks and developments that could jeopardize the continued existence of the Company as a going concern. The system ensures that business risks and opportunities are identified early on and that the Group is in a position to deal with them actively and effectively. It complies with the statutory requirements for an early warning system and conforms to German corporate governance principles.

The risks.

Of all the risks that have been identified for the Group, those risk areas or individual risks that could, as it stands today, materially affect Deutsche Telekom's financial position and results are examined below.

Competition.

Intensified competition and technological progress have dramatically reduced prices for fixed-network (telephony, Internet) and mobile communications. This affects both voice communication and data traffic, as shown by the price erosion in Internet flat rates. There is a danger that this dip in prices will not be compensated for by corresponding volume growth.

Competitive pressure could rise even further as a result of a significant expansion of coverage by (regional) local loop operators, the continuing trend toward bundled products, technological innovations, reductions in wholesale prices for competitor products, and ongoing substitution, assisted by price erosion and flat rates for mobile communications as well as convergence products. Moreover, up to now pure mobile communications providers in Germany have increasingly offered fixed-network and DSL products on the market. Another possibility is that cable operators may corner a larger share of the market, for example by offering attractive triple-play services. In addition, a general competitive trend is emerging where Deutsche Telekom increasingly has to compete with players that do not belong to the telecommunications sector as such, including major companies from the consumer electronics and Internet sectors. Despite having lost some market shares already, Deutsche Telekom believes that it is exposed to the risk of further loss of market shares and falling margins. Apart from other factors, Deutsche Telekom's future competitive position depends in particular on the quality of the service it provides. There is still room for improvement in this area.

Ongoing price-cutting initiatives are now a regular feature of the European mobile communications market. This is attributable to both low-cost providers such as MVNOs and new calling plans offered by established network operators. Continued price erosion in the mobile communications sector could put T-Mobile's targets at risk. In addition, T-Mobile increasingly faces competition abroad from integrated providers that include both mobile communication services and fixed-network products (e.g., DSL) in their portfolios. In the United States, T-Mobile competes with three significantly larger providers. T-Mobile faces particular challenges regarding its product and service quality and pricing if it is to counter its competitors' economies of scale. Since T-Mobile USA is a crucial growth driver for Deutsche Telekom, risks to its competitiveness may also have a negative impact on the Group's ability to reach its targets.

The ICT market in the Business Customers segment is experiencing declining prices and long sales cycles. This represents a risk of lower revenues and margins for T-Systems. T-Systems' international presence in terms of its brand awareness is limited, especially compared with certain competitors who are already better established in such markets. This could adversely affect T-Systems' ability to realize potential growth, especially considering the growing importance of business with multinational corporations outside Germany.

Products, services, and innovations.

As a result of rapid technological progress and increasing technological convergence, it is possible that new and established technologies or products may not only complement, but in some cases even substitute one another. This may lead to lower prices and revenues in both voice and data traffic.

There is also a risk that Deutsche Telekom will not be able to convince customers sufficiently of the benefits of current and future services or raise the level of acceptance of these services among customers. Identified market demand may not be satisfied quickly enough, or only with insufficiently matured products. These risks also constitute a threat to our potential growth drivers in the fixed network, such as the triple-play product T-Home.

The acquisition of UMTS licenses in several European countries created the basis for the introduction of the third generation of mobile communications. Whether these investments will pay off depends on increased usage and revenues in mobile communications, especially in the area of mobile data communications. Additional services and applications are to be developed for this purpose, both by ourselves and in cooperation with third parties (content providers). There is a risk, however, that target earnings will not be generated with these applications. Customer perception is equally crucial for the success of multimedia offerings. Falling behind the competition could lead to a loss of particularly high-volume customers.

Economy and industry.

The general state of the economy in Germany, Europe, and the United States also influences Deutsche Telekom's business performance. For Deutsche Telekom's largest markets, Germany and the United States, current economic forecasts predict that growth will slow down slightly in 2007. If economic growth proves to be lower than expected, this may have an adverse effect on both the willingness of business customers to invest and consumer spending by Deutsche Telekom's residential customers. As a consequence, revenue targets might not be reached, e.g., for the higher-value, DSL-based access products in the fixed network (double play, triple play, etc.) and for mobile Internet access.

Regulation.
Existing network access and price regulation relates to telecommunications services offered by network operators with “significant market power.” In Germany, Deutsche Telekom is considered to be a company with significant market power and is therefore subject to strict regulation in broadband/ fixed-network communications. Its European subsidiaries are also subject to corresponding regulatory regimes in the fixed-network and mobile areas.

This situation is exacerbated by the extensive powers of government agencies to intervene in product design and pricing, which can have a drastic effect on operations. Deutsche Telekom is able to anticipate such intervention, which may further intensify existing price and competitive pressure, to a limited extent only.

The regulatory framework is currently being reviewed at European level. To date, regulation has been scaled back only in markets of minor significance, such as the German market for fixed-network international calls. There is no indication of any significant efforts being made for further sector-specific deregulation. Rather, it is feared that the outcome of the ongoing review will increase the extent of regulation. A tendency toward increased regulation can be seen, for example, in the EU Commission’s plan to impose strict regulation on roaming rates in wholesale and retail markets. In the mobile communications sector, regulating rates for international roaming in this way could entail substantial price and revenue risks for Deutsche Telekom.

Even after termination prices were regulated – in Germany by the Federal Network Agency in November 2006 – a further reduction in termination prices is possible in the future, as is an extension of the regulation of mobile termination, for example to include text messaging.

Regulatory intervention is also on the horizon for investments in new infrastructures, e.g., in the high-speed fiber-optic network as a platform for new broadband applications (triple play). Regulated wholesale services for broadband access to competitors in the end customer market also entail considerable revenue and cost risks. In this context there is a substantial risk that future investments will not pay off and product innovations will not deliver a first-mover advantage if they have to be made available to competitors at the same time. Relief is promised by a new regulation in the Telecommunications Act according to which new products will in principle not be subject to regulation.

Further regulatory intervention could also affect content and media offerings. Since Deutsche Telekom offers products that also include the transmission of television programs, media regulation could become a significant factor for the Company. Regulation in this area could lead to restrictions in the Company’s media services offering and/or additional costs for implementing technical measures to comply with regulatory requirements.

Should regulation become this intense, Deutsche Telekom’s flexibility in the market could be compromised, especially with regard to pricing and product design.

In addition, the European Union passed an EU-wide directive on data retention in 2006 that sets minimum standards for the type of data to be retained by network operators and for applicable retention periods. The EU requirements now have to be translated into national law in each EU member state. In Germany the first bill has already been drawn up. This will lead to substantial capital expenditure and costs, depending on how the national statutory provisions are ultimately formulated. Whether these costs will be reimbursed remains unclear.

Human resources.
Deutsche Telekom announced a staff restructuring program for its operations in Germany in November 2005, under which approximately 32,000 employees are scheduled to leave the Group by 2008. Some of these employees will leave Deutsche Telekom and, together with their jobs, join another employer as part of a deconsolidation of business models from Vivento. With these staff restructuring measures, Deutsche Telekom AG will continue to comply with the agreement reached with the trade unions to avoid compulsory redundancies until the end of 2008. The Group realized approximately one-third of the planned staff reductions in 2006; the continued implementation depends on various framework parameters.

The staff restructuring is being realized using voluntary, target group-specific measures. Part of it is realized through partial retirement arrangements for employees subject to collective agreements (non-civil servants). Employees will also have the opportunity to leave the Group on a bilateral voluntary basis with severance packages. The severance models offered in 2006, including the “Abfindung Spezial” program, were very well received by the employees.

More employees are to leave the Group with severance packages by 2008. The implementation of these plans will depend on general developments on the labor market and on the details of the severance offers.

Since November 16, 2006, the “Second Act to Amend the Act for the Improvement of the Staff Structure at the Residual Special Asset of the Federal Railways and the Successor Companies of the Former Deutsche Bundespost” has made it possible to include civil servants in the socially responsible staff restructuring program. Civil servants aged 55 and over who work in areas with excess personnel and who cannot be deployed in other areas may apply for early retirement; there is no legal entitlement for them to do so.

December 1, 2006 saw the first operational handover of five Vivento Customer Service (VCS) sites. Around 600 employees were transferred to the walter TeleMedien group. This represented the first step in a deconsolidation strategy. Nevertheless, there are risks associated with the planned further deconsolidation of sites of Vivento's business lines.

Deutsche Telekom is planning a range of measures to make customer service more efficient and align it even more closely with its customers' needs. In 2007 around 45,000 employees are to be transferred from T-Com as part of the T-Service project. These employees will come from both the technical service units and the call centers of T-Com. The transfers enable Deutsche Telekom to focus on the quality of its service under conditions that reflect the market situation. The aim is to safeguard the competitiveness of the Company and, at the same time, protect jobs in the Group. The Group also aims to systematically align working conditions and remuneration systems with market levels. Constructive support by the unions and the works councils is equally crucial for the successful implementation of the three goals – quality, competitiveness, and safeguarding of jobs.

Health and the environment.
Electromagnetic fields are repeatedly associated with potential environmental and health damage. This is a controversial issue and the subject of public debate. Existing public acceptance problems affect networks and the use of terminal equipment, and have an effect on T-Mobile, particularly with regard to network structure and intensity of usage. In addition to legal risks, the Company fears regulatory measures to implement the precautionary principle in the area of mobile communications.

The World Health Organization has declared that, on the basis of current scientific knowledge, there are no known adverse effects on health below the international threshold standards. Nor does it expect any serious dangers to arise in the future, though it does recommend continued research due to ongoing scientific uncertainties.

Deutsche Telekom aims to overcome doubts among the general public by pursuing an objective, scientifically well-founded, and transparent information policy. Deutsche Telekom's efforts to provide state-of-the-art technologies therefore include funding scientific research that aims to detect possible risks at an early stage. Among other things, Deutsche Telekom is involved in Informationszentrum Mobilfunk (IZMF), an industry initiative by mobile communications enterprises, as well as in the German Research Association for Radio Applications (Forschungsgemeinschaft Funk – FGF), which supports independent research into the biological effects of electromagnetic fields. In addition, the EMF policy adopted in 2004 has enabled T-Mobile to take measures in the areas of transparency, information, involvement, and research funding that minimize both potential legal and regulatory problems as well as acceptance problems among the public.

IT/telecommunications infrastructure.
Deutsche Telekom's production processes are supported by information and telecommunications technology (data centers, switching nodes, transmission systems, etc.) and software applications that are subject to constant innovative development to increase competitiveness and exploit additional cost savings potential, for example by developing a cross-product shared IP platform for fixed-network and mobile communications.

The products, services, and IT/telecommunications networks used by Deutsche Telekom itself and those offered in the competitive market may be subject to malfunction and outages, e.g., due to hacker attacks, sabotage, power failures, natural disasters, technical faults, or other events. This could affect Deutsche Telekom's mobile communications, Internet, ICT, and fixed-network products and services. Deutsche Telekom counteracts these risks by employing a large number of measures, including back-up systems, protective systems such as firewalls and virus scanners, regular technical network tests, building security, and organizational precautions. Early warning systems ensure that automated and manual countermeasures can be initiated in the event of disruptions. In addition, organizational and technical emergency procedures are in place to minimize damage. Group-wide insurance programs have also been established to cover operational interruptions and damage to current and non-current assets.

Purchasing.
As an ICT service provider, operator, and provider of IT/telecommunications products, Deutsche Telekom cooperates with a broad variety of suppliers of technical components (e.g., software, hardware, transmission systems, switching systems, outside plant, terminal equipment for fixed-network and mobile communications applications). The Company employs a large number of organizational, contractual, and procurement strategy measures as precautions to counteract potential risks, such as supplier default or dependence on individual suppliers.

Litigation.
Deutsche Telekom is party to several proceedings both in and out of court with government agencies, competitors, and other parties. The proceedings listed below are of particular importance from Deutsche Telekom's point of view.

More than 2,000 lawsuits have been filed against Deutsche Telekom in Germany by shareholders who claim to have bought shares of Deutsche Telekom on the basis of the offering prospectuses dated May 28, 1999 and May 26, 2000. Many of these lawsuits also allege improper recognition of the carrying amount of the real estate assets. Some of these lawsuits are also directed at KfW Bankengruppe and/or the Federal Republic of Germany. The aggregate amount of the claims filed under these lawsuits is approximately EUR 76.0 million. The Frankfurt/Main Regional Court has issued two certified questions to the Frankfurt Higher Regional Court pursuant to the German Capital Investor Model Proceedings Act (Kapitalanleger-Musterverfahrensgesetz – KapMuG). Moreover, several thousand additional investors have initiated conciliatory proceedings with a state institution in Hamburg, the “Öffentliche Rechtsauskunfts- und Antragsstelle der Freien und Hansestadt Hamburg.”

After the merger of T-Online International AG into Deutsche Telekom AG became effective on June 6, 2006, Deutsche Telekom AG was served around 250 applications for a court review of the fairness of the exchange ratio stipulated in the merger agreement dated March 8, 2005. Under the German Reorganization and Transformation Act (Umwandlungsgesetz), former shareholders of T-Online can request the Frankfurt/Main Regional Court to review the fairness of the exchange ratio in the course of appraisal rights proceedings (Spruchverfahren). If the outcome of these proceedings shows that the exchange ratio for the T-Online shares was too low, the Regional Court will stipulate a supplementary cash payment that Deutsche Telekom would be required to pay to all former shareholders of T-Online whose shares were exchanged for shares of Deutsche Telekom within the framework of the merger.

In the arbitration proceedings filed by the Federal Republic of Germany against Deutsche Telekom AG, DaimlerChrysler Financial Services AG, and Toll Collect GbR (in which Deutsche Telekom AG holds a 45-percent stake) regarding disputes relating to the truck toll collection system, Deutsche Telekom received the Federal Republic's statement of claim on August 2, 2005 in which the Federal Republic maintains its claim to lost toll revenues of approximately EUR 3.5 billion plus interest, alleging – among other things – that it was deceived as to the likelihood of operations commencing on September 1, 2003. The total of the asserted claims for contractual penalties was increased to approximately EUR 1.65 billion plus interest. The contractual penalties are based on alleged violations of the operator agreement (lack of consent to subcontracting, delayed provision of on-board units and monitoring equipment). The defendants responded on June 30, 2006.

The Federal Republic is refusing to issue the final operating permit on the grounds that alleged further obligations under the operating agreement, specifically the assignment of certain industrial property rights to Toll Collect GmbH, have not been fulfilled. As a consequence of the refusal to grant the final operating permit, the Federal Republic of Germany considers itself entitled, effective December 21, 2006, to initiate proceedings for the termination of the operating agreement by serving notice of termination. The operating agreement entitles the Federal Republic to do so if the final operating permit is not granted within 12 months from the granting of the interim operating permit. The right of termination on the part of the Federal Republic assumes that Toll Collect GmbH does not alleviate the grounds for termination within a certain period from receipt of the termination notice. The right of termination is limited to a period of 6 months after the Federal Republic becomes aware of the grounds for termination. There are presently no indications that the Federal Republic will file a termination notice.

On May 3, 2005, Vivendi Universal SA (formerly Vivendi Universal S.A., referred to hereinafter as Vivendi) took legal action against Deutsche Telekom and T-Mobile International AG & Co. KG. Vivendi alleges that the defendants unlawfully broke off negotiations on the acquisition of a 48-percent stake in Polska Telefonia Cyfrowa Sp.z o.o. (PTC) in order to then obtain these shares at a lower price. The value in dispute is approximately EUR 2.27 billion. The action is pending before the Commercial Court in Paris. Numerous other lawsuits and arbitrational proceedings are pending in connection with the disputed PTC shares.

On April 13, 2006, in line with the rules of the International Chamber of Commerce in Paris, Vivendi filed arbitration proceedings with the international court of arbitration in Geneva against Deutsche Telekom AG, T-Mobile International AG & Co. KG, T-Mobile Deutschland GmbH, T-Mobile Poland Holding No. 1 B.V. and others. This complaint is aimed at a declaratory judgment that on or before March 29, 2006 a verbal agreement was reached between the parties concerning, inter alia, putting an end to all legal disputes relating to the investment in PTC, or that pre-contractual obligations were breached. Vivendi is demanding performance of the contract or compensation.

On October 23, 2006, Vivendi filed a suit against Deutsche Telekom AG, T-Mobile USA Inc., T-Mobile International AG, T-Mobile Deutschland GmbH and others with the U.S. District Court in Seattle, Washington State, claiming that the defendants had colluded illegally to cause Vivendi to lose its alleged interest in PTC. The lawsuit is based on the Racketeer Influenced and Corrupt Organizations (RICO) Act. In the lawsuit, Vivendi is seeking, among other things, damages of approximately USD 7.5 billion.

On October 19, 2005, following enforcement proceedings, Deutsche Telekom received a claim for damages of approximately EUR 86.1 million from telegate AG. telegate alleges that Deutsche Telekom charged excessive prices for the provision of subscriber data between 1997 and 1999, which resulted in telegate AG having insufficient funds available for marketing measures and preventing it from achieving its planned market share. Following enforcement proceedings, Deutsche Telekom received a claim for damages of approximately EUR 328.63 million from Dr. Harisch, also on October 19, 2005. Dr. Harisch alleges that due to the excessive prices for the provision of subscriber data between 1997 and 1999, the equity ratio of telegate AG fell significantly on several occasions, resulting in the need for capital increases. This required Dr. Harisch and another shareholder to release shares from their own holdings, thereby diluting their remaining shareholdings.

A notice of action was served on January 19, 2006 by Arcor AG & Co. KG seeking damages of approximately EUR 223.0 million on grounds of an alleged price squeeze between wholesale prices and the prices charged to end customers. This legal dispute has been adjourned pending a legally enforceable ruling by the European courts in administrative penalty proceedings that are decisive for the proof of claim.

On May 29, 2005, Deutsche Post AG filed a request for arbitration against Deutsche Telekom relating to a warranty for defects from an acquisition agreement concerning logistics sites. Deutsche Post AG is seeking damages of approximately EUR 37.0 million as well as the determination of other unquantified damages for alleged lack of building permissions, quantified at approximately EUR 68.0 million before the hearing.

On October 31, 2005, the satellite operator Eutelsat sued Deutsche Telekom AG, T-Systems Business Services GmbH and SES Societé Européenne des Satellites S.A. for compensation amounting to approximately EUR 141.5 million. The plaintiff is basing its claim on an alleged breach of contractual duty. The action is pending before the Commercial Court in Paris.

Furthermore, Deutsche Telekom intends to defend itself and/or pursue its claims resolutely in each of these court, conciliatory, and arbitration proceedings.

Financial risks.
Deutsche Telekom is exposed to financial risks, particularly liquidity, default, currency, and interest rate risks. The primary instruments used for medium- to long-term financing are bonds and medium-term notes issued in a variety of currencies and jurisdictions. A liquidity reserve in the form of credit lines and cash is maintained to guarantee the solvency and financial flexibility of Deutsche Telekom at all times. As of December 31, 2006, Deutsche Telekom had access to credit lines totaling EUR 17.4 billion, provided by 29 banks. The bilateral credit agreements have a maturity of 36 months and can, after each period of 12 months, be extended by a further 12 months to renew the maturity of 36 months. Spreading the maturities over the year significantly reduces the loan extension risk. Deutsche Telekom believes that there is only a minor risk that it will have difficulty in accessing the capital markets due to a decline in its ratings. For detailed information on financial risks, please refer to Note 43 in the notes to the consolidated financial statements.

Impairment of Deutsche Telekom's assets.
The value of the assets of Deutsche Telekom and its subsidiaries is reviewed periodically. In addition to the regular annual measurements, any time it can be assumed that (as a result of changes in the economic, regulatory, business, or political environment) the value of goodwill, intangible assets, or items of property, plant and equipment has possibly decreased, Deutsche Telekom checks whether it is necessary to carry out certain impairment tests, which may lead to the recognition of impairment losses that do however not result in disbursements. This could impact to a considerable extent on Deutsche Telekom AG's results, which in turn may depress the Deutsche Telekom share and ADS prices.

Sales of shares by the Federal Republic and KfW Bankengruppe.
As of December 31, 2006, the Federal Republic, together with KfW Bankengruppe, holds approximately 31.7 percent of Deutsche Telekom's shares. On April 24, 2006, The Blackstone Group purchased an interest in Deutsche Telekom's registered equity from KfW Bankengruppe. The share held by The Blackstone Group totaled 4.39 percent at December 31, 2006. In this connection, KfW Bankengruppe and Blackstone agreed on a one-year lock-up for further sales of KfW's shares in Deutsche Telekom. Blackstone agreed with KfW Bankengruppe to lock up its Deutsche Telekom shareholding for two years.

It is possible that the Federal Republic will continue its policy of privatization and sell further equity interests, including shares in Deutsche Telekom AG, in a manner designed not to disrupt the capital markets and with the involvement of KfW Bankengruppe. For Deutsche Telekom, there is a risk that the sale of a significant volume of Deutsche Telekom shares by the Federal Republic or KfW Bankengruppe, or speculation to this effect on the markets, could have a negative short-term impact on the price of Deutsche Telekom shares.

Aggregate risk position.
The assessment of the aggregate risk position is based on a consolidated review of all significant risks or risk areas. Considering the continued high level of competition and price pressure, regulatory conditions, and major challenges in terms of service quality and personnel restructuring, the Group's aggregate risk position has not changed significantly over the previous year. As it stands today, there is no risk to the Company's continued existence as a going concern.

All three rating agencies maintained Deutsche Telekom's long-term rating at A– or A3, as in 2005. However, S&P has changed its outlook to "negative." For more information on ratings, please refer to the "Development of business" section.

The opportunities.
Some of the most important aspects of the Group's wide variety of opportunities are highlighted below.

Although the German and Western European markets are largely saturated in many areas, Deutsche Telekom still has substantial growth potential in the emerging countries of Central and Eastern Europe, as well as with its main growth driver T-Mobile USA. Deutsche Telekom can benefit significantly from this development due to its strong presence in Central and Eastern Europe. Innovative bundled products as well as convergence products are also areas of opportunity for Deutsche Telekom. As a large, integrated ICT group, Deutsche Telekom is not only able to cope with substitution risks better than specialized providers; it can also offer new bundled products such as triple play or quadruple play.

Deutsche Telekom also sees potential opportunities in the main trends in the industry such as convergence products (particularly based on IP technology), IPTV, mobile Internet, and multi-access IP value-added services (participation in the fast-growing online advertising market). Another trend is "real ICT" in the business customers segment, i.e., end-to-end telecommunications and IT solutions from a single source.

Civic, social, and ecological considerations such as a state-of-the-art health care system, efficient climate protection, mobility geared to seniors, citizen-oriented administration, mobile working, or even transparent goods traceability (e.g., commodity online services) are further starting points for the development of new products and services. In particular, IP-based solutions or, for example, the use of RFID facilitate new business models that can reduce the quantities of resources used and also the costs to the environment and society. Here, Deutsche Telekom makes a further contribution to the sustained development of society.

With projects such as T-City, the Deutsche Telekom Group is demonstrating its capabilities and its customer service, presenting state-of-the-art networking technology and enabling its customers to experience a host of products in everyday use. Much improved locational factors in cities, towns, and regions provide new opportunities for small and medium-sized enterprises as well as potential sources of revenue for Deutsche Telekom. Through cooperation with municipalities, for example, DSL can be expanded to cover as yet undeveloped regions and its market potential increased.

In addition to opportunities in terms of products and projects, Deutsche Telekom has considerable potential to substantially improve its customer service in particular. Please refer to the information in the "Group strategy and Group management" section of this report.

Highlights after December 31, 2006.

Further sites of Vivento Customer Services GmbH sold.
Vivento Customer Services GmbH sold two more sites – Suhl and Cottbus – with around 480 employees to the walter TeleMedien group on January 26, 2007. Transfer of operations, which is scheduled for April 1, 2007, is accompanied by a contract commitment, thus safeguarding the jobs of the staff concerned until the end of 2012.

PTC: Deutsche Telekom's legal position unchanged.
On January 18, 2007, the Polish Supreme Court overturned two rulings by courts of lower instance which had acknowledged the validity of the verdict of the Vienna arbitrational court of November 2004 in Poland. The case was remitted to the first instance to be heard anew. This decision was solely the result of a procedural error by the court of first instance and, in relation to the case itself, affects neither the content nor the validity of the Vienna arbitrational verdict of November 2004. Furthermore, with this decision, the Polish Supreme Court has not ruled in favor of Vivendi's claimed ownership of the disputed 48-percent stake in PTC. Deutsche Telekom's legal position concerning the ownership of the stake in PTC thus remains unchanged.

Outlook.*

Market environment remains tough // Sustainable improvement of service culture // Mobile Communications will remain growth engine // Broadband business to be further expanded // Business Customers: Safeguarding telecommunications business and expanding IT business

Economic outlook.

In spite of the good starting position resulting from the current economic upswing, the fall bulletins for 2007 by Germany's six leading economic research institutes are predicting that economic growth in Germany will slow to 1.4 percent because of the increase in the VAT rate. Structural problems, such as high unemployment and stagnating consumer spending, will dampen economic growth. Driven by the global economy – which is expected to cool slightly in 2007 but will still grow by 3.1 percent – the institutes' economists believe that exports will rise by 6.2 percent. In addition to export-driven growth, increases in capital expenditure on plant and equipment will remain an important growth factor for economic performance in Germany.

For the euro zone, the economic research institutes expect rapid economic expansion to continue in 2007, although the declining boom in the global economy will pull growth back slightly to 2.3 percent. For the United States, economists are also predicting that economic expansion will probably slow to 2.7 percent in 2007.

Market expectations.

Growth in Deutsche Telekom's international sales markets continues unabated, particularly in the key markets of the United States and the United Kingdom. Deutsche Telekom's domestic sales markets are still dominated by extremely intense competition and prise erosion on the telecommunications market as a whole, both for consumer DSL and business voice telephony, and for mobile communications.

Consequences for corporate management.

Deutsche Telekom is responding to the challenges of rapid technological changes and strong competition in the telecommunications industry with specific measures to ensure the long-term sustainability of customer relationships and thus revenue and profit growth. In particular, a sustainable improvement of the customer care culture, investments in future product areas, and simplified price structures will safeguard Deutsche Telekom's customer relationships and in turn its revenues. Additional cost reductions through increased rationalization investments, such as in new, more cost-efficient IP-based networks, will result in a corresponding development of profit and therefore ensure the long-term sustainability of cash flow. These measures assist Deutsche Telekom in pursuing its goal of continuing to offer its shareholders an attractive dividend. The immense changes in Deutsche Telekom's market environment – in particular the rapid technological change – are forcing it to adjust its workforce structure by cutting jobs in a socially responsible manner. The workforce reduction will be implemented using voluntary instruments such as partial retirement arrangements, severance payments and early retirement.

Mobile communications will remain the growth engine.

The Mobile Communications strategic business area will remain the growth engine of the Group. The further development of the business area will again be driven in particular by the U.S. market, which is recording relatively high customer growth rates. For Europe, despite strong price pressure we expect to be able to expand our market share, primarily through higher usage on the part of our customers. An important growth lever will be to offer advanced mobile data services, especially an enhanced, attractively priced web'n'walk offering with new equipment.

Based on these assumptions, we expect the positive earnings trend in the Mobile Communications business area to continue in the next two years, supported by further savings. Regulatory decisions and the further development of the U.S. dollar and sterling (GBP) exchange rates may have an effect on T-Mobile's revenue and profit measured in euros.

The Group's capital expenditure activities in 2007 will continue to focus on its mobile communications business. In Europe, key areas will include improvements in the quality of existing GSM networks and the further expansion of our UMTS networks. In the United States, we are driving the enhancement of network quality and network coverage and the rapid roll-out and launch of 3G mobile communications networks in order to ensure growth in customer numbers and revenue.

Broadband business to be further expanded.

In the DSL business, we will defend our market share and expect a significant increase in the number of our lines. Additionally, we want to establish our triple-play products offered under the name T-Home. A major element of this strategy will be the expansion of our high-speed Internet infrastructure, provided that such an investment is economically viable in the regulatory environment in the medium term. Aside from the VDSL roll-out, investments in 2007 will focus on expanding the DSL and IP network and maintaining and extending the existing network infrastructure.

In 2007, the traditional fixed-network business will continue to be affected by competition-induced loss of market share, fixed-mobile substitution, price cuts due to regulatory requirements, and market-related price erosion. Broadband/Fixed Network will launch a quality and service campaign in 2007 to safeguard and defend the core voice and access business and extend its broadband business to include new, innovative products. We are also preparing to migrate the old PSTN environment to the new IP-based environment and thereby introduce an innovative, competitive IP connection that will facilitate many additional functions for customers such as video telephony.

Based on these assumptions, we expect the negative earnings trend for the Broadband/Fixed Network strategic business area to initially continue.

To make our service function more efficiently and to optimize its alignment with customer needs, some 35,000 employees in Germany are to be spun off during 2007 as part of the T-Service project; they will be responsible for technical infrastructure and customer service. Around 10,000 jobs currently in T-Com's call center unit are also to be spun off. These spin-offs allow Deutsche Telekom AG to focus on the quality of its service under conditions that reflect the market situation. The goal is to maintain the Company's competitiveness in the long term, while safeguarding jobs both in the Group and in Germany. The Group also aims to systematically align working conditions and remuneration systems with market levels and to increase productivity.

Business Customers: Safeguarding telecommunications business and expanding IT business.

The Business Services unit will focus on safeguarding its telecommunications business in a hotly contested market. In our telecommunications core business (voice, data, IP) we will focus on winning back customers. This strategy will be accompanied by efforts to expand areas such as LAN Solutions, i.e., network solutions for connecting workstations at a company's site. The Business Services unit is expecting growth in its IT business. The goal is to substantially intensify our cooperation in particular with small and medium-sized enterprises. Capital expenditure will be guided by the technical integration of the IT environment and the introduction of value-added services.

As regards the Enterprise Services unit, we plan to significantly expand our market share in the telecommunications business through integrated IT and telecommunications sales activities. In the IT business, we intend to grow primarily by expanding outsourcing activities, in particular through large-scale contracts and continued business process outsourcing with a focus on the Automotive (global), Public (Germany, United Kingdom, Spain), and Telecommunications (Germany and Western Europe) industry lines. We are planning to increase capital expenditure also in Enterprise Services, particularly through the assumption of assets in conjunction with business process outsourcing.

We currently expect earnings in the Business Customers area to develop positively as these new growth opportunities in the IT business are leveraged. In the telecommunications business, we expect the improved cost structure to lead to a stabilization in earnings, in particular due to initially slower growth in the market for IP solutions and intensified domestic price pressure.

Group Headquarters & Shared Services.

Earnings at Group Headquarters & Shared Services are influenced largely by Vivento (including the development of the business models and the realization of internal and external employment opportunities) and by continued staff restructuring in the Group. Other influential factors include measures to achieve centralized cost savings and improve efficiency at Shared Services.

General statement on the business development in the Group.

In view of the expected market situation in the individual business areas, Deutsche Telekom aims to again achieve positive earnings for the entire Group.

* Outlook contains forward-looking statements that reflect management's current views with respect to future events. Words such as "assume," "anticipate," "believe," "estimate," "expect," "intend," "may," "could," "plan," "project," "should," "want" and similar expressions identify forward-looking statements. These forward-looking statements include statements on the expected development of net revenue, earnings, and personnel figures for 2007 and 2008. Such statements are subject to risks and uncertainties, such as an economic downturn in Europe or North America, changes in exchange and interest rates, the outcome of disputes in which we are involved, and competitive and regulatory developments. Some uncertainties or other imponderabilities that might influence Deutsche Telekom's ability to achieve its objectives, are described in the "Risk and opportunity management" section in the management report and in the "Forward Looking Statements" and "Risk Factors" sections in the Annual Report on Form 20-F and the disclaimer at the end of this Annual Report. Should these or other uncertainties and imponderabilities materialize or the assumptions underlying any of these statements prove incorrect, the actual results may be materially different from those expressed or implied by such statements. We do not guarantee that our forward-looking statements will prove correct. The forward-looking statements presented here are based on the current structure of the Group, without regard to significant acquisitions, dispositions or business combinations Deutsche Telekom may choose to undertake. These statements are made with respect to conditions as of the date of this document's publication. We do not intend or assume any obligation to update forward-looking statements.