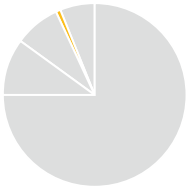
IT Services business segment

↗ The market for airline IT stabilised in 2011, but pressure on margins remains intense. ↗ Realignment enabled Lufthansa Systems to raise its competitiveness significantly. ↗ The success of Jetzt! can be seen in the sharp rise in operating profit and stabilised revenue figures. ↗ Lufthansa Systems wants to return to profitable growth and is selectively making use of partnerships.

Share of Group revenue 0.8%



↗ Leading IT service provider for the air transport industry

Key figures IT Services

		2011	2010	Change in %
Revenue	€m	599	595	0.7
of which with companies of the Lufthansa Group	€m	369	363	1.7
Operating result	€m	19	10	90.0
Adjusted operating margin	%	4.0	1.8	2.2 pts
Segment result	€m	21	−6	
EBITDA	€m	58	45	28.9
CVA	€m	23	−23	
Segment capital expenditure	€m	55	36	52.8
Employees as of 31.12.	number	2,820	2,935	−3.9
Average number of employees	number	2,855	2,974	−4.0

599 €m

Revenue

19 €m

Operating result

Business and strategy

IT services provider with focus on the airline industry
Lufthansa Systems offers its clients consultancy and IT services. The company focuses on the airline industry, where it is a global leader, as well as on the areas of transport and logistics, industry, media and publishing, energy, healthcare and tourism. Its customer base includes around 200 airlines around the world and more than 100 companies from other sectors, of which a large number has worked with Lufthansa Systems for many years.

The company is headquartered in Kelsterbach near Frankfurt. Additional sites in Germany and in 16 other countries ensure the proximity to the customer and the rapid response times that are essential for a global IT services provider. An international production base also contributes to lower production costs and makes the company more competitive. Lufthansa Systems operates its own data centres at various sites around the world. Its data centre in Kelsterbach is one of the most modern and powerful in Europe.

Broadly diversified range of services
As a full-service provider, Lufthansa Systems offers its customers the entire spectrum of IT services – from consultancy via the development and implementation of custom-built applications through to systems operations in its own data centres. All its services and IT solutions are aimed at generating direct added value for the customer in the form of efficiency gains, cost reductions or higher yields.

The key factors of the company's success on the market is its combination of IT know-how and the ability to understand all the customer's relevant business processes.

Locations Lufthansa Systems

Thanks to its many years of experience in the airline industry Lufthansa Systems is for example the only provider with solutions to cover the entire air transport process chain.

Its understanding of complex business processes, in-depth technological knowledge and expertise in managing projects of all sizes also come to the fore in other sectors. Examples include the optimisation of sales processes, the development of sophisticated online solutions and the introduction of completely new IT environments for industrial companies with international operations.

Markets and competition

Competition remains intense
The IT market is very competitive and this is reflected in high pressure on prices and margins. Providers from emerging markets such as India benefit from the ongoing trend towards outsourcing thanks to their comparative cost advantages.

For several years the market for airline IT contracted, but in 2011 it stabilised at around the EUR 7.5bn mark. Airlines spend around 50 per cent of this total on operating services, 30 per cent on projects and 20 per cent on IT products. There is still no sign of any lasting change in airlines' general disinclination to invest.

With a share of 30 per cent of outsourced airline IT services, Lufthansa Systems has a leading position in the EMEA region (Europe, Middle East, Africa). In Asia and America the market share is 3 per cent respectively.

The main competitors in the airline IT market are Sabre Airline Solutions, Amadeus, HP, SITA and the Boeing subsidiary Jeppesen. However, none of them has such a wide-ranging product portfolio as Lufthansa Systems. New players in this market include Google, Amazon and Apple.

Prompted by the economic upswing at the beginning of the year German industry increased its IT investment in 2011. The trend towards cloud computing also boosted the growth rate. In total the volume of the German market for IT Services came to EUR 34.2bn, according to BITKOM, the industry association. This represents year-on-year growth of 3.5 per cent. Lufthansa Systems competes successfully in this market against all the major providers of consultancy services and IT outsourcing. In 2011 the company again achieved a place in the top 5 in the well-known "Lünendonk-Listen", a register of IT advisory and systems integration companies in Germany.

Sales and customers

Tailored solutions for customers all over the world
Around the world, more than 300 customers rely on the IT competence and services from Lufthansa Systems. Some 200 of them are airlines, representing the whole spectrum of business models: international network carriers, low-cost airlines and regional operators. Outside the airline industry, products such as VI&VA for publishers and media companies and infotainment for cruise ships are well established on the market.

The customer base at Lufthansa Systems is very stable. The relationships with many customers go back a long way, in some cases ten years and more. Vattenfall Europe for instance has put its trust in the IT know-how from Lufthansa Systems for more than 15 years. Since 2000, the company has realised a large number of joint SAP projects with Vattenfall Europe Information Services, a subsidiary of the energy utility, and developed an internet portal for its consumers as a new distribution channel.

In the airline sector the relationships sometimes even predate the spin-off of Lufthansa Systems. This is the case for Ryanair and Croatia Airlines, for instance. Emirates is a good example of the way many customer relationships develop. In 1996 the company selected the flight route planning system Lido/Flight and today it uses a wide range of products from Lufthansa Systems in its flight operations. Even if a customer is a member of another airline alliance, this has no impact on the quality and stability of the business relationship, as demonstrated by the oneworld member Finnair. The Finnish airline decided to work with Lufthansa Systems for the first time in 1997 and has continued to extend the scope of the partnership ever since.

Four regional management units are responsible for airline customers: Europe, Middle East/Africa, Asia/Pacific and America. These were set up in 2011 and are an important part of the company's realignment under the Jetzt! programme. Regional managers are the primary point of contact for customers and have broad decision-making authority. Their remit covers the entire account and service management as well as sales.

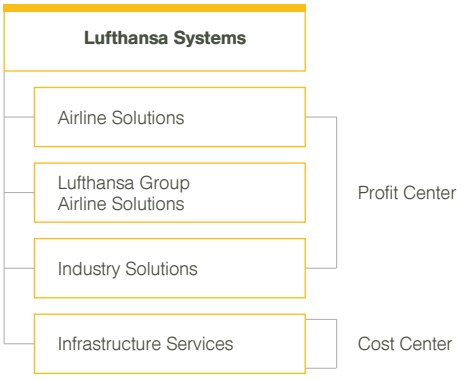
As the largest single customer, Lufthansa Passenger Airlines is managed by the profit centre Lufthansa Group Airline Solutions, which was also created in 2011. The Industry Solutions unit has organised its sales on the basis of key account management.

Course of business

New structure brings new focus
The restructuring of the company under the Jetzt! programme introduced in 2010 enabled Lufthansa Systems to increase its competitiveness significantly in an operating environment defined by margin pressure and unrelenting consolidation. The realignment of the company structure was completed with the implementation of a new customer-oriented structure following the merger of five subsidiaries with Lufthansa Systems AG. The aim of the realignment is to reduce complexity and thereby to cut costs in all areas. The company now delivers its services through the three profit centres Airline Solutions, Industry Solutions and Lufthansa Group Airline Solutions, as well as through the cost centre Infrastructure Services.

In recent months Lufthansa Systems has been working on four central aspects to bolster its competitiveness and return to a growth path. At the same time revenue was boosted by short-term activities. Expenses were also reduced even further compared with the previous year. In the field of innovation many new products were presented or initiated. Specific partnerships with global IT companies were explored to secure the company's future success.

New organisational structure of Lufthansa Systems



Contracts with new customers and product innovation
In a challenging climate still defined by economic uncertainty, Lufthansa Systems was able to report new customer wins and expand its business with existing customers. A major contract was signed with Malaysia Airlines to take over its global data network. Numerous new customers such as Aerolineas Argentinas and Adria Airways decided to purchase various IT solutions to optimise their operating processes. Lufthansa renewed the licence agreements for network planning, medium and short-term flight planning, code-share management and flight plan distribution solutions, which have been running for more than ten years.

The highly successful product innovations last year included the wireless in-flight entertainment system BoardConnect. It is based on a wireless network using the common WiFi standard. Passengers can use their own devices to access films, audio files and other information or to make use of all the opportunities offered by the internet. The first customer for BoardConnect is Condor and more airlines are to follow, with Virgin America and Qantas set to deploy the system in 2012.

Another innovative solution that makes use of the unbroken trend towards mobile devices is the Lido/iRouteManual, which turns an iPad into a mobile pilot's case and obtained operating approval from the US civil aviation authority in 2011.

Lufthansa Systems also presented deskBase, its new model for the workplace. Based on the principle of cloud computing, this workplace model enables employees to access applications and data stored in the data centre at any time and from anywhere. deskBase is currently being introduced in the Lufthansa Group and is also on offer on the external market.

In addition, Lufthansa Technik and Lufthansa Systems have signed a long-term service agreement for their IT workspaces. This enables Lufthansa Systems to strengthen its long-term position as the main provider of infrastructure services at Lufthansa Technik.

In the field of logistics, Lufthansa Systems ramped up its collaboration with Hamburg Süd, Schenker Deutschland and the Hamburg Port Authority. As a general contractor, Lufthansa Systems is renewing the IT systems that manage all rail traffic at the Port of Hamburg.

The publishers Lippische Zeitungsverlag and Donaukurier Verlagsgesellschaft are using additional functions of the publishing solution VI&VA. Volkswagen also commissioned the introduction of a new company portal. Gesundheit Nord gGmbH has appointed Lufthansa Systems to merge all the SAP systems in the four hospitals that form the Bremen clinic group. Viking River Cruises is the first customer from the river cruise sector.

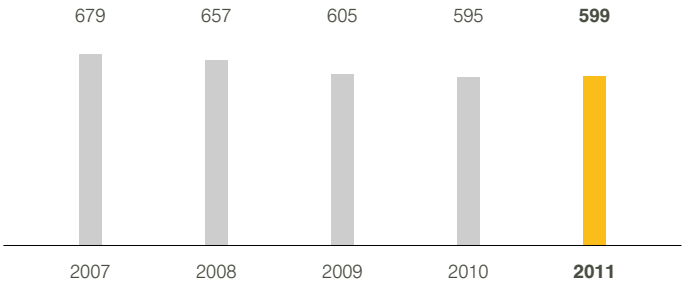
Lufthansa Systems won the innovation prize from German industry for a system that supports the rapid and secure recovery of IT passwords by means of biometric identification.

Revenue and earnings development

Revenue trend stabilises

Business at Lufthansa Systems became increasingly stable over the reporting period. Revenue of EUR 599m was marginally higher than the previous year's figure of EUR 595m. Revenue with Lufthansa Group companies rose by 1.7 per cent to EUR 369m thanks to higher volumes. Pruning the sector portfolio trimmed revenue from external customers by 0.9 per cent to EUR 230m. Revenue from external customers was, however, an important component of Lufthansa Systems' business success, accounting for 38 per cent of total revenue.

Revenue IT Services in €m



Other operating income declined year on year by 43.8 per cent to EUR 18m. This is largely due to lower investment in product software.

Total operating income fell to EUR 617m (–1.6 per cent).

Operating expenses reduced by 3.1 per cent

Increased project activity in the area of infrastructure services drove the cost of materials and services up by 12.0 per cent to EUR 84m.

Operating expenses IT Services

	2011 in €m	2010 in €m	Change in %
Cost of materials and services	84	75	12.0
Staff costs	229	247	–7.3
Depreciation and amortisation	34	34	0.0
Other operating expenses	251	261	–3.8
of which external staff	59	59	0.0
of which rent/maintenance of IT	104	106	–1.9
Total operating expenses	**598**	**617**	**–3.1**

In connection with the Jetzt! programme the average number of employees was reduced to 2,855 in the reporting period (previous year: 2,974). Staff costs were 7.3 per cent lower than in the previous year at EUR 229m. This includes one-off effects in connection with restructuring measures initiated the year before.

Depreciation and amortisation came to EUR 34m, exactly the same as last year.

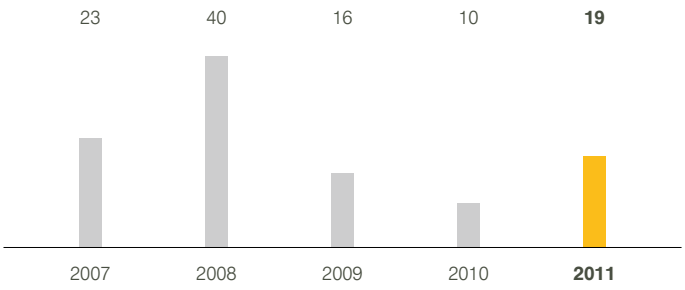
Other operating expenses fell by 3.8 per cent to EUR 251m.

Total operating expenses declined accordingly to EUR 598m (–3.1 per cent).

Distinct improvement in operating result
The stabilisation of sales and the sustainably lower costs are reflected in a tangible improvement to the operating result. Lufthansa Systems increased its operating profit to EUR 19m (previous year: EUR 10m).

The segment result was a profit of EUR 21m. This came after a segment loss of EUR 6m the year before. The loss was the result of write-downs made in connection with new priorities being set for development projects.

Operating result IT Services in €m



Capital expenditure up on the year
Lufthansa Systems made segment investments of EUR 55m in 2011. The considerable increase compared with the previous year's figure of EUR 36m stems from the transfer of assets from the subsidiary Lufthansa Systems FlightNav to Lufthansa Systems AG. Adjusted for this effect, capital expenditure was roughly the same as the previous year and served mainly to maintain existing business.

Long-term overview confirms the effects of Jetzt!
In mid 2010 Lufthansa Systems started the programme Jetzt! to boost the company's profitability.

It was intended to make up for dwindling sales prices and weak demand in a market environment plagued by margin pressure by cutting costs and generating additional income at short notice. These activities had an effect right in the first year. They enabled revenue, which had been sliding since 2007, to be stabilised. At the same time, Lufthansa Systems took its operating result past its 2009 and 2010 levels for the first time in the 2011 financial year. The adjusted operating margin improved as well as a consequence.

Forecast

Cost-cutting measures to be continued
Irrespective of the customer's sector, IT plays a central role in the optimisation of business process with the goal of reducing costs and increasing flexibility. In an economic environment that is volatile overall, it remains essential for companies to keep their costs down permanently and yet still be able to respond quickly to market changes. New technologies such as cloud computing and mobilisation open up a wide range of new possibilities in this area. By developing new products and solutions Lufthansa Systems creates the conditions for companies to benefit from these developments.

The restructuring in 2011 laid the foundation for Lufthansa Systems to return to profitable growth again in 2012. Targeted measures will also save further costs in the years ahead.

Although business with Lufthansa Passenger Airlines will initially continue to decrease as a result of the switch to new and cheaper technologies, the greater customer orientation and faster response times should lead to more new business in external markets.

After an in-depth review of strategic partnership opportunities a focused approach has been chosen, by which wherever it makes sense for the company and its customers, Lufthansa Systems will work with selected partners on a project basis or in specific areas. The discussions did not produce any convincing options for a global partnership.

For the years 2012 and 2013 Lufthansa Systems is expecting its business to develop positively and revenue to increase thanks to more new orders from airlines, especially in the regions Asia/Pacific and America, and greater income from existing customers in other industries. The improved cost base will also be reflected in further improvements in the operating result during this period.