December 6, 2007

Rating Information

Sector Rating	Market Weight
Target Price YE' 08 (DPWGN.DE)	€27.00

Trading Data

52-Wk Range	€20.00–25.60
Market Cap.	€27,890 MM
Shares Out.	1,205.0 MM
Dividend Yield	4.3%
Avg. Daily Vol.	7,177,000
Float	814.0 MM

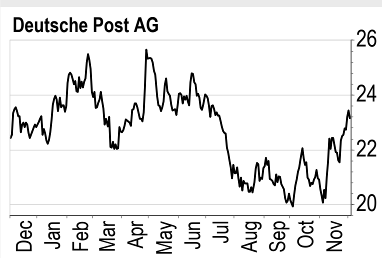
Source: BSIL Estimates

Fundamental Data

EV/EBITDA	6.9x
Enterprise Value	€41,097 MM
LT Debt to Total Cap.	18.5%
Book Value	€10.20
Long-Term Growth	10%

Source: BSIL Estimates

Price Performance



Source: FactSet

Securities in this report priced as of: December 4, 2007

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Deutsche Post

DPWGN.DE–€23.23–Outperform

Should It Say 'Goodbye' to America? Scenario Analysis

- Since the day Deutsche Post announced its acquisition of Airborne (March 25, 2003), the market has been counting the cost. The strategic rationale remains unproven almost five years later. Financially, the acquisition has been – and still is – a disaster.
- With the appointment of John Allan as group CFO on October 1, 2007, a more radical approach to the US business became possible. All solutions to the US woes are apparently on the table.
- In this note, we examine the potential impact of a partial shutdown scenario on the group's valuation. We conclude – unsurprisingly – that the most prudent strategy would be to back away from domestic US domestic express - a business that looks never able to produce a ROIC above its WACC. This note quantifies the effect of shutting down the US domestic express operations under three different scenarios.
- We have also refined our long-term domestic-mail margin assumptions, which leads to small EPS reductions. However, at the time of writing, we have not yet accounted for the evolution of the debate about instituting a minimum wage in Germany in our forecasts. We remain of the view that the eventual outcome is unclear. That said, we believe there is in this regard upside risk for Deutsche Post.
- Though we expect European freight-related markets to be relatively resilient into 2008, we also believe that our outlook for Deutsche Post's operations is cautious. However, we favour the shares because in it we see the potential for significant restructuring as the new CFO institutes some very basic measures to enhance capital controls and shareholder returns.
- And then there is the undemanding valuation (13.4x 2008E P/E) and decent dividend yield (4.3%). We are confident that our €27 price target is a reachable target for Deutsche Post shares.

Sector View: Long-term structural and cyclical growth in most segments. Mail volumes should decrease >3% pa.

IFRS EPS Estimates (All values in €)

		EPS	P/E
2006		1.18	19.7x
2007		1.33E	17.5x
2008		1.73E	13.4x
	Previous	1.75E	

† All EPS estimates are net of stock options unless otherwise stated.

Deutsche Post – Should It Exit the US Domestic Operations?

It would not be pretty if we were to tally up all of the costs associated with Deutsche Post's US express expansion, starting at the point of the March 2003 purchase of Airborne. That said, some perspective is warranted: since that acquisition, DHL Americas (which is bolstered by some non-US operations) has lost more than €2bn at the operating level. And on top of this you can add Airborne.

Looking forward, we believe Deutsche Post management must reconsider its strategy to become a global express operator offering international and domestic services in all the major markets under an integrated brand and service umbrella. Our analysis in this regard (see below) does not reveal any surprises - under all but the most optimistic assumptions, going forward the near-term losses are not likely to be compensated by longer-term gains.

Our previous forecast losses in the DHL Americas business were €600m for 2007, €512m in 2008 and €346m in 2009, with full-year breakeven in 2012. We now no longer have faith in this scenario, and this set of forecasts now comprises our 'blue sky' scenario. Our assessment of current market conditions, alongside management's outlook for its US business, is sufficiently pessimistic that we are recasting our forecasts in a more negative light. Accordingly, our new base case scenario assumes that:

1. DHL Americas never does better than lose €200m per year after the US domestic air and ground networks have been wound down (€200m approximates to the level of losses in the DHL Americas operation before the Airborne acquisition).
2. A partnership agreement with a competitor can be struck (for example with FedEx, UPS or USPS) that will help prevent Deutsche Post losing significant amounts of business indirectly (i.e. global contracts). Undoubtedly, DHL Americas' competitors would be happy to take the extra volume, but they would likely be less forthcoming in helping DHL Americas make an easy exit from its US domestic operations.
3. The cost of this restructuring will be roughly netted off by the planned disposal of at least €1bn of assets over the next two years from across the group's portfolio.

These assumptions underpin our new forecasts for the DHL Americas. The risk:reward trade-off is clear. If we assume that the chance of the best and worst outturns coming out is equal, the obvious conclusion is to back out of domestic US express because of the asymmetric outturns (half a chance of a €0.51/share profit, and half of a €3.53 loss). In other words, our blue sky scenario would have to be 7x 'bluer' to offer an even risk:reward trade – and in our view this is not feasible.

DHL Americas Scenarios (€m)

€m	2007E	2008F	2009F	2010F	2011F	2012F	2013F	2014F	TV
Blue-sky DHL Americas EBIT	-600	-512	-346	-173	-21	137	252	355	362
Normalised tax effect*	180	154	104	52	6	-41	-76	-107	-109
Proportion of WC and Capex**	-159	-140	-84	-92	-95	-100	-105	-110	-13
FCF	-579	-498	-326	-213	-110	-4	72	139	241
PV***	-579	-459	-277	-167	-79	-3	44	79	125
PV of cashflows	-1317								
PV of terminal cashflow****	1934								
Total PV	**618**								
per share	**0.51**								
	2007E	**2008F**	**2009F**	**2010F**	**2011F**	**2012F**	**2013F**	**2014F**	**TV**
Base-case DHL Americas EBIT	-600	-512	-346	-200	-200	-200	-200	-200	-200
Normalised tax effect****	180	154	104	60	60	60	60	60	60
Proportion of WC and Capex	-159	-140	-84	-92	-95	-100	-105	-110	-13
	-579	-498	-326	-232	-235	-240	-245	-250	-153
PV	-579	-459	-277	-182	-170	-159	-150	-141	-80
PV of cashflows	-2198								
PV of terminal cashflow	-1227								
Total PV	**-3425**								
per share	**-2.84**								
	2007E	**2008F**	**2009F**	**2010F**	**2011F**	**2012F**	**2013F**	**2014F**	**TV**
Black-sky DHL Americas EBIT	-600	-512	-346	-300	-300	-300	-300	-300	-300
Normalised tax effect	180	154	104	90	90	90	90	90	90
Proportion of WC and Capex	-159	-140	-84	-92	-95	-100	-105	-110	-13
	-579	-498	-326	-302	-305	-310	-315	-320	-223
PV	-579	-459	-277	-237	-220	-206	-193	-181	-116
PV of cashflows	-2469								
PV of terminal cashflow	-1790								
Total PV	**-4259**								
per share	**-3.53**								

*Assumes (very generously) that US tax losses can be used to offset profits generated in other parts of the business and therefore reduces cash tax paid
*Assumes that from 2009 onwards, proportion of WC and capex reflects DHL Americas excluding US domestic express ***Assumes 8.5% discount rate ****Assumes 2.0% terminal growth rate
Source: Company data; Bear, Stearns International Ltd. estimates

Changes to Forecasts – Domestic Mail

Beyond the changes pertaining to DHL Americas, we have also refined our view of Deutsche Post's domestic mail margin. Here we have attempted to capture the effects of (a) negative operational gearing due to volume losses, (b) cost savings by not replacing all employees who leave or retire, and (c) average annual wage increases.

The table below breaks down the constituent parts of our domestic mail margin forecast. Please note that we restate Deutsche Post's mail volumes and margins to show addressed mail separately from unaddressed. Underpinning these changes are the following assumptions:

- 45% of domestic mail costs are staff-related, with 2% average annual wage increases (hence 2% x 45% = 0.9%)
- 50% of the cost base is flexible, so for each 1% of volume lost, only half of the associated costs can be cut. This is why in 2008, for example, we forecast a 3.1% fall in addressed volumes, of which half drops straight through to the margin as negative operational gearing.

Should competition be significantly curtailed – which we see as unlikely – there would be considerable upside to our volume and margin assumptions.

Changes to Mail Forecasts

	2007F	2008F	2009F	2010F	2011F	2012F
Total addressed volume (m)	14,958	14,500	13,938	13,386	12,922	12,469
% chg YoY	*-1.5*	*-3.1*	*-3.9*	*-4.0*	*-3.5*	*-3.5*
Total addressed revenue (€m)	8,870	8,512	7,978	7,471	7,067	6,751
% chg YoY	*-2.7*	*-3.9*	*-6.1*	*-6.2*	*-5.2*	*-4.3*
Annual staff cost increase (%)	*-0.9*	*-0.9*	*-0.9*	*-0.9*	*-0.9*	*-0.9*
Negative operational gearing (%)	*-0.8*	*-1.5*	*-1.9*	*-2.0*	*-1.7*	*-1.8*
Contribution from ongoing cost-savings (%)	*0.5*	*1.5*	*1.9*	*2.0*	*1.7*	*1.8*
New EBIT margin forecast (%)	*19.0*	*18.1*	*17.2*	*16.3*	*15.4*	*14.5*
Previous EBIT margin forecast (%)	*19.0*	*18.6*	*18.3*	*17.9*	*17.5*	*17.2*
New Mail division EBIT forecast (€m)	1,993	1,886	1,781	1,649	1,542	1,452
Previous Mail division EBIT forecast (€m)	1,993	1,938	1,871	1,772	1,698	1,640
Δ (%)	*0.0*	*-2.7*	*-4.8*	*-6.9*	*-9.2*	*-11.5*
Value of cost-savings (€m)	45	133	158	151	126	121

Source: Bear, Stearns International Ltd. estimates

Earnings Revision

These changes to German domestic mail profitability lower our EPS forecast in 2008 by 1.8% and 2.4% in 2009, respectively.

Changes to EPS forecasts

	2007E	2008E	2009E
New adjusted EPS (€)	1.33	1.73	2.09
Previous adjusted EPS (€)	1.33	1.75	2.14
Δ (%)	-	*-1.1*	*-2.4*

Source: Bear, Stearns International Ltd. estimates

Valuation

We arrived at our unchanged €27 target price using a simplified version of our previous DCF/SOTP hybrid. Our DCF methodology remains basically unchanged, though the terminal value is lower as we now assume DHL Americas to remain unprofitable in perpetuity and because our terminal margin for domestic mail is now lower.

Our SOTP calculation has seen some changes, the most important of which pertains to our valuation of Financial Services. Here we now apply a 35% premium to our €63.5 valuation, which increases our implied Financial Services valuation per share from our previously estimated €3.5 to €5.8. This equates to around 2x book value. Also, we previously accounted for provisions (mainly pension-related) by applying a discount rate. Our new methodology nets off the pension charge that is allocated to the interest line in the profit and loss account with the pension credit allocated to the Logistics division. We then apply an average of the target P/Es used in the SOTP valuation (13.1x). Finally, instead using a DCF to value the 'Unallocated' division as we had done previously, we apply the same average target P/E to the 2008 charge.

Putting all these changes together results in an unchanged target price of €27, implying 16% upside from current levels. In the event that more radical restructuring is visited upon the group – say splitting Express/Logistics from Mail/Financial Services – we calculate upside beyond our €28 DCF valuation. And on top of this, more aggressive gearing could certainly be possible.

Deutsche Post Valuation (€)

Group DCF	**28**	8.5% WACC, terminal growth rate 1.4%
SOTP		
Mail	12.5	15% premium to P/E paid by CVC for stake in Danish Post (10.2x)
Express	13.0	FedEx's through-cycle P/E (16x)
Logistics	6.0	Discounted KNIN through-cycle P/E (13.1x)
Financial Services	5.8	35% premium to target price (€85.7/share)
Net unallocated pension charge	-5.1	Multiplied by average target P/Es (13.1x)
Unallocated	-6.6	Multiplied by average target P/Es (13.1x)
	26	
Target price	**27**	Average of two methods
Current share price	23.23	
Implied upside (%)	*16*	

Source: Bear, Stearns International Ltd. estimates

Deutsche Post P&L

Yr to Dec	2006	2007F	2008F	2009F
Revenue				
Mail	15,290	15,672	15,743	15,576
Express	13,463	13,716	14,401	13,329
Logistics	24,405	26,516	29,116	31,865
Financial Services	9,593	10,390	10,909	11,359
Services/consolidation	-2,206	-2,000	-2,117	-2,176
Total	**60,545**	**64,294**	**68,052**	**69,954**
%ch	*29.8*	*6.2*	*5.8*	*2.8*
Costs				
Cost of materials and banking transactions	-34,349	-34,940	-36,813	-38,713
Staff costs	-18,616	-18,936	-19,951	-20,981
Depreciation and amortisation ex goodwill	-1,771	-1,763	-1,891	-1,969
Other operating expenses	-4,758	-4,879	-5,106	-5,389
Total operating expenses	**-57,182**	**-60,632**	**-63,976**	**-65,324**
%ch	*28.4*	*6.0*	*5.5*	*2.1*
EBIT (pre-exceptionals)				
Mail	2,094	1,993	1,886	1,781
Express	288	428	604	860
Logistics	751	885	1,046	1,196
Financial Services	1,004	1,057	1,140	1,193
Unallocated/Services	-774	-700	-600	-400
Total	3,363	3,662	4,076	4,630
%ch	*15.5*	*8.9*	*11.3*	*13.6*
EBIT margin (%)	*5.6*	*5.7*	*6.0*	*6.6*
Exceptionals	509	161	-	-
EBIT post-exceptionals	**3,872**	**3,824**	**4,076**	**4,630**
Net finance expense	-1,030	-1,006	-1,002	-998
Adj PBT	**2,333**	**2,656**	**3,074**	**3,632**
Tax	-560	-318	-569	-672
Tax rate (%)	*20.0*	*19.5*	*18.5*	*18.5*
PAT	2,282	2,500	2,505	2,960
Minorities	-366	-538	-423	-442
Net income	**1,916**	**1,962**	**2,083**	**2,517**
Basic EPS (€)	1.60	1.63	1.73	2.09
%ch	*-19.5*	*1.4*	*6.1*	*20.9*
Adj EPS (pre-exceptionals) (€)	**1.18**	**1.33**	**1.73**	**2.09**
%ch	*-5.1*	*12.7*	*30.1*	*20.9*
DPS (€)	**0.75**	**0.90**	**0.99**	**1.14**
Dividend growth (%)	*14.0*	*20.0*	*10.0*	*15.0*
Number of shares (m)	1,194	1,205	1,205	1,205

Source: Company data; Bear, Stearns International Limited estimates.

ADDENDUM
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Andrew Beh

Companies Analyzed

Deutsche Post (DPWGN.DE) - €23.23 (as of December 4, 2007 market close) - Outperform
Price Target ('08): €27.00
Risk(s) to Price Target - Postal deregulation, global trade flows, failing internal controls
Valuation Methodology - DCF and SOTP

Deutsche Post (DPWGN.DE): The subject company is or during the past twelve (12) months has been a non-investment banking client (securities related services) of Bear Stearns & Co. Inc.

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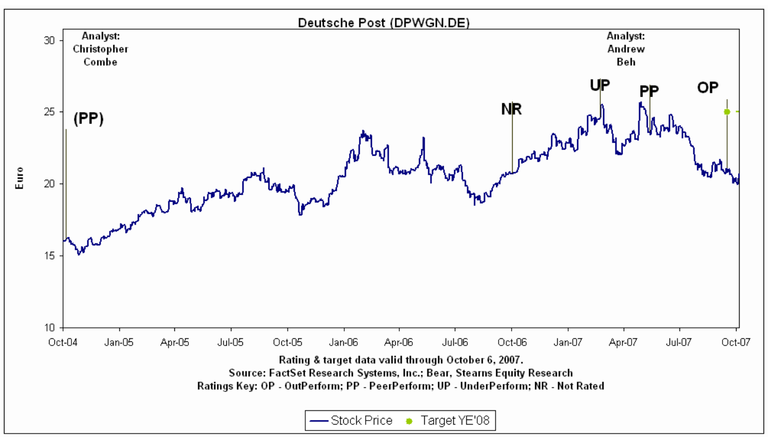

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Market Overweight (MO) - Expect the industry to perform better than the primary market index for the region (S&P 500 in the US) over the next 12 months.

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