

Management report of the Deutsche Telekom group and Deutsche Telekom AG.

In 1997, Deutsche Telekom had a successful year in its core business activities, reporting growth in both net revenue and net income. As previously announced, a dividend payment of DM 1.20 per share will be recommended to the shareholders' meeting. Shareholders' equity will not be increased by retaining earnings.

Deutsche Telekom (group) key figures

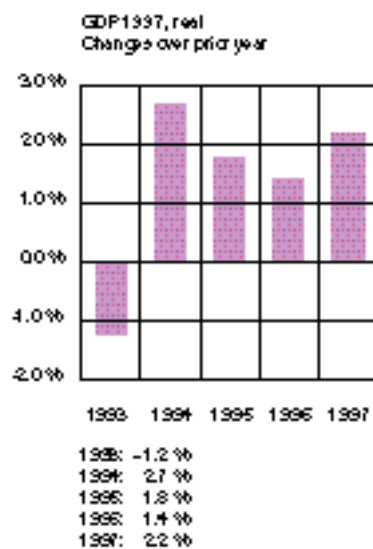
billions of DM	1997	1996	1995
Net revenue *	67.6	63.1	59.6
Net income	3.3	1.8	5.3
Balance sheet total	162.8	174.3	160.2
Investments	15.5	22.6	17.7

Employees at year-end **	216,006	229,590	225,185
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*1995 figure adjusted for value-added tax

**from 1996 includes approx. 20,000 MATAV employees

The management report for Deutsche Telekom AG has been combined with the management report for the Deutsche Telekom group.



General economic situation Restrained economic development in Germany

The vast majority of Deutsche Telekom's business activities take place in Germany.

The general economic situation in Germany improved somewhat during 1997, with gross domestic product (GDP) increasing by 2.2 percent in real terms, while capital expenditure on plant and equipment grew 3.9 percent. At the same time, demand for German goods abroad increased by 10.7 percent.

GDP 1997, real

(unadjusted figures)

Changes over prior-year period

1st quarter	2nd quarter	3rd quarter	4th quarter
1.0%	3.0%	2.4%	2.4%

Year as a whole	2.2%
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The domestic labor market remains a cause for concern, with the number of people employed falling by 487,000 in 1997. Unemployment reached a level of 4.82 million people in December, the highest figure ever recorded.

Labor productivity across the economy as a whole (GDP per employee) rose 3.7 percent in 1997, while at the same time unit labor costs (defined as the ratio of gross income from dependent employment to labor productivity) fell 1.8 percent.

At the present time, inflation does not appear to present a danger to the German economy. The Bundesbank does not expect any inflationary or deflationary pressures in the foreseeable future.

With the economy expanding at a relatively slow rate, the telecommunications market in Germany failed to expand beyond expected levels, with no real signs of any special stimulus for growth at Deutsche Telekom.

Deutsche Telekom feels aftershocks from Asian crisis

Developments on the global currency markets have been affected by the financial crisis in Southeast Asia.

The adjustment process under way throughout East Asia since late 1997 has been accompanied by massive devaluations of the respective local currencies. The International Monetary Fund (IMF) has agreed on assistance packages and related economic and structural reforms with South Korea, Thailand, Malaysia, Indonesia and the Philippines, with implementation of the individual packages at different stages in the various countries involved. Developments in Southeast Asia have a strong impact on Deutsche Telekom's strategic interests in the expanding telecommunications markets in Malaysia, Indonesia and the Philippines.

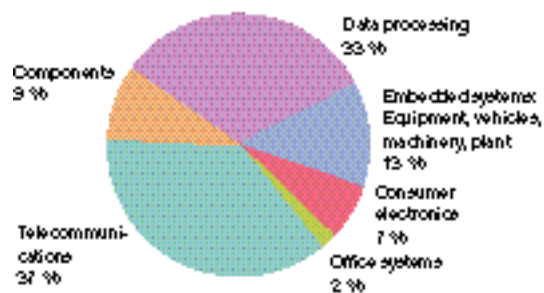
Compact news: T-Online also offers online research through a wide variety of publishing houses and databases. The publishing group Handelsblatt makes information available at "wirtschaft#" from media such as Handelsblatt, Wirtschaftswoche, DM, vwd, Karriere direkt, Genios and the Hoppenstedt publishing house. The Spiegel publishing house can also be accessed in T-Online.



"The ICE-press is transmitted via the T-D1 network from the Spiegel publishing company to the trains where it is printed out. Hot off the press."

Ferdinand Rätching, Head of Administration, Spiegel publishing company, Hamburg

Total market for information and communication technologies 1997
Total volume DM 253 billion



Source: Diebold

Development of the telecommunications industry

Growth and liberalization
The telecommunications industry is characterized by increasing globalization and a worldwide opening of markets. For Deutsche Telekom, these changes mean not only tougher competition in its home market, but also opportunities for growth in expanding international markets, which the Company takes advantage of.

Diebold, a market-research organization, has estimated the total volume of the German market for information and telecommunications technology to be DM 253 bn for 1997, with telecommunications making up DM 93 bn (37 percent) of this market.

The opening of the German market on January 1, 1998, created the most liberalized telecommunications market in the world. 1997 was characterized by preparations for unrestricted competition. By year-end, 112 licenses had been granted, of which 67 involved class 3 licenses for transmission lines, while the remaining 45 were for class 4 licenses for voice telephony.

Deutsche Telekom is the market leader in Europe and the third largest telecommunications company in the world. Over the next few years, the Company is likely to lose market share within Germany as a result of more competition and regulatory requirements. However, by focusing on new technologies, enhanced service and customer orientation, and increased efficiency, Deutsche Telekom is well prepared for the new market conditions.

New providers take position

During 1997, most carriers and resellers concentrated their efforts on developing an entry strategy for the German market, dealing with market segmentation and defining their product portfolios. Business customers represented the main group initially targeted by competitors; residential customers will not become the focus of attention of these alternative providers until some time later in 1998.

The number of providers – nationwide, regional and local carriers and resellers – preparing to enter the competitive marketplace in 1997 is expected to drop over the coming years as consolidation occurs through takeovers and alliances. The alternative network operators continued to expand their own infrastructures during 1997, while many of the Company's competitors also leased lines from Deutsche Telekom to transmit their voice and data traffic.

The regulatory framework Telecommunications Act comes into effect

The statutory framework regulating the telecommunications sector in Germany was completely redefined by the German Telecommunications Act (TKG), which came into force on August 1, 1996. The new legislation called for the German telecommunications market to be fully liberalized as of January 1, 1998.

The Act is supplemented by numerous ordinances governing important issues such as rates regulation, network access and network interconnection, and universal service details. In December 1997, the Telecommunications Customer Protection Ordinance was also revised and modified to keep pace with the rapidly changing market environment.

New regulatory authority replaces BMPT

On January 1, 1998, the Federal Ministry of Posts and Telecommunications (BMPT) was replaced by the new Regulatory Authority for Telecommunications and Posts, which assumed responsibility for supervising the telecommunications market in Germany.

Consistent with the existing regulatory provisions, important rates-related decisions and significant offers made by Deutsche Telekom to its competitors were subject to regulatory approval. For example, Deutsche Telekom concluded network interconnection agreements with a number of network operators in 1997. These agreements, in accordance with the new legal framework, were submitted for approval to the BMPT, which still functioned as the regulatory authority in 1997. In contrast to Deutsche Telekom's proposals, the BMPT set interconnection rates of between 1.24 and 5.14 pfennigs per minute, with the average rate across all tariff zones being 2.7 pfennigs per minute. With this decision, the BMPT rejected Deutsche Telekom's move to

offset the access deficit calculated into the price of providing access lines. To protect its legal position, Deutsche Telekom has appealed the decision made by the BMPT, although no final decision has yet been reached.

Development of business in 1997

During the 1997 financial year, Deutsche Telekom generated consolidated net revenue totaling DM 67.6 bn. Results from ordinary business activities amounted to DM 7.2 bn, while the Company reported net income of DM 3.3 bn. Earnings per share totaled DM 1.20.

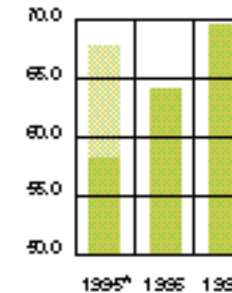
Considerable revenue growth

Deutsche Telekom was able to benefit from the steady growth of the telecommunications market, ending the financial year with a considerable increase in revenues.

Deutsche Telekom (group) revenue			
billions of DM	1997	1996	Change
Fixed-network communications	50.5	47.4	6.6%
Mobile-network communications	5.0	4.2	19.0%
Network communications	55.5	51.6	7.6%
Cable TV/broadcasting	3.1	3.0	3.3%
Terminal equipment	3.2	3.4	-5.9%
Special value-added services	2.3	2.3	0.0%
Other services	1.1	0.9	22.2%
International activities	2.4	1.9	26.3%
	12.1	11.5	5.2%
Total revenues	67.6	63.1	7.1%

Revenue from fixed-network communications rose 6.6 percent to reach DM 50.5 bn. The key factor for this was the telephone network service, where the number of ISDN access lines increased considerably and traffic volume also showed strong growth. The number of ISDN channels grew 41.1 percent to 7.3 million by year-end 1997. With revenues rising 8.7 percent, activities involving data communications and systems solutions experienced a healthy rate of growth. Thanks to active marketing of the Telekom Designed Networks/Solutions concept, it again proved possible to increase revenues in this sector.

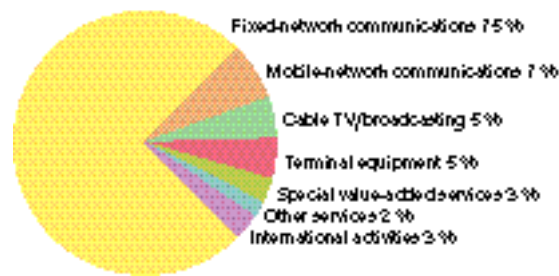
Development of revenues
billions of DM



1995: 53.6
1996: 63.1
1997: 67.6

*1995 figure adjusted for VAT

Revenue by business area



In 1997, mobile-network communications recorded year-on-year income growth of 19.0 percent. The T-D1 service experienced a sharp rise in revenues as the result of the dynamic development in the number of customers, which grew 51.9 percent to reach 3.3 million. At the same time, the revenues reported for T-C-Tel fell as the number of customers dropped and the lower tariffs introduced at the beginning of the period under review took effect.

The success of T-Online, the largest on-line service in the German market, was maintained throughout 1997, with revenue rising 90.7 percent. In excess of 1.9 million T-Online customers were registered by year-end.

In international activities, revenue amounting to DM 2.4 bn was primarily generated by the telecommunications operator MATAV. This represents a rise of 22.4 percent in 1997 that can be attributed to an increase in the number of lines operated by this Hungarian company in its fixed and mobile network.

Net income up

During the year under review, Deutsche Telekom generated net income totaling DM 3.3 bn, representing a year-on-year increase of 88 percent. Results from ordinary business activities in 1997 amounted to DM 7.2 bn (1996: DM 6.6 bn).

This change can be attributed to a number of offsetting factors. The 7 percent growth in net revenue was offset by a disappointing 19 percent increase in the expenses for goods and services purchased, which reached

Hidden computers: These days, modern chip technology is indispensable for telecommunications, too. Digital switching computers with high storage capacities allow intelligent network management and applications such as T-Online, ISDN or mobile data communications. Information technology and telecommunications are converging to become a single sector - telematics.



DM 12.1 bn (1996: DM 10.2 bn). This increase can for the most part be attributed to the higher level of purchases of terminal equipment coupled with an increase in the number of interconnections with networks run by other operators, primarily in the field of mobile communications.

Personnel costs fell 2.3 percent to DM 18.3 bn (1996: DM 18.8 bn), generally tracking the 5 percent reduction in the workforce.

As expected, depreciation and amortization rose 5 percent to DM 18.6 bn (1996: DM 17.7 bn) following the complete digitization of Deutsche Telekom's networks.

Other operating expenses rose by a total of DM 0.7 bn to DM 10.2 bn, with cost savings being offset by the increased cost of risk provisions.

At DM 7.8 bn (1996: DM 7.7 bn), net financial expense remained fairly constant. Of this total, net interest expense decreased DM 0.9 bn to DM 6.4 bn, as expected, due to the scheduled reduction of debt. At the same time, losses related to subsidiary, associated and related companies grew sharply, reaching DM 1.4 bn (1996: DM 0.4 bn),

mostly as a result of considerable losses in investments in Southeast Asia as well as additional start-up losses at Atlas/Global One. By year-end, local currencies in the Asian countries affected had lost more than one third of their value against the dollar compared with prior-year levels. As the capital investments made by the companies concerned were financed to a large extent in US dollars, this resulted in considerable losses; in addition, revenue predictions have had to be lowered to take into account the general economic situation in the region. These difficulties are reflected in amortization of goodwill totaling DM 0.5 bn in addition to proportionate losses of DM 0.4 bn.

While the transfer of shares in MagyarCom Grand Cayman, Cayman Islands, to MagyarCom Holding GmbH, Bonn, contributed DM 1.0 bn to the income reported by Deutsche Telekom AG, the transaction had no impact on income within the Group due to the effects of consolidation.

With the initial public offering now over and the costs of the personnel restructuring measures being fully accounted for in previous years, there were no extraordinary losses to be reported in the year under review. The DM 1.4 bn rise in tax expenses to DM 3.6 bn reflects the increase in income before taxes.

Group/DVFA earnings per share billions of DM	1997	1996
Consolidated net income	3.303	1.758
Amortization of goodwill	0.617	0.284
Other additions*	0.0	1.064
Other deductions	0.0	0.0
DVFA/SG earnings	3.920	3.106

Number of common shares	2,743,240,100
DVFA/SG earnings per share (DM)	1.43

* Extraordinary losses for personnel restructuring measures and share offering costs, net of tax effects

"Everyone needs modern telecommunications these days. I communicate with my customers via ISDN, mobile phone and T-Online."

Robert Muslan, Hutkönig,
The hat-maker at the cathedral,
Regensburg



Summary of the annual financial statements of Deutsche Telekom AG

Statement of income		
billions of DM	1997	1996
Net revenue	60.4	57.5
Increase in inventories and other own capitalized costs	2.0	2.0
Other operating income	8.4	7.7
Goods and services purchased	(11.6)	(9.6)
Personnel costs	(15.9)	(16.6)
Depreciation and amortization	(16.9)	(16.0)
Other operating expenses	(13.2)	(12.6)
Financial income (expense), net	(6.4)	(6.3)
Extraordinary income (losses)	-	(2.5)
Income before taxes	6.8	3.6
Taxes	(3.5)	(2.1)
Net income	3.3	1.5

Balance sheet		
billions of DM	Dec. 31, 1997	Dec. 31, 1996
Property, plant and equipment, and intangible assets	118.0	125.1
Financial assets	16.6	14.8
Noncurrent assets	134.6	139.9
Inventories, materials and supplies	0.8	1.0
Receivables	8.2	7.6
Liquid assets	12.4	17.6
Current assets	21.4	26.2
Deferred tax receivables	0.8	0.7
Prepaid expenses	1.2	1.0
Special loss account arising from creation of accruals	-	0.1
Total assets	158.0	167.9
Shareholders' equity	49.4	47.7
- of which: net income	3.3	1.6
Accruals	13.0	14.1
Liabilities	94.9	105.7
Deferred income	0.7	0.4
Total shareholders' equity and liabilities	158.0	167.9

The annual financial statements of Deutsche Telekom AG which have an unqualified audit opinion from C&L Deutsche Revision Aktiengesellschaft Wirtschaftsprüfungsgesellschaft are published in the Federal Gazette (Bundesanzeiger) and filed with the Commercial Registry of the Bonn District Court. The annual financial statements are available upon request from Deutsche Telekom, Investor Relations, Postfach 20 00, D-53105 Bonn, Germany, fax +49 228 181-8405.

Annual financial statements of Deutsche Telekom AG

Reporting of corporate groups with international activities is increasingly focusing on the consolidated financial statements. However, the key factor behind the dividend payable to the shareholders is the net income generated by Deutsche Telekom AG. For this reason, the annual financial statements of Deutsche Telekom AG are presented in summarized form below.

The balance sheet total for Deutsche Telekom AG decreased by DM 9.9 bn due to the reduction in debt, while the increase in net income caused shareholders' equity to increase to DM 49.4 bn. The equity ratio climbed 1.7 percent to 29.2 percent. Deutsche Telekom AG recorded a 5 percent increase in net revenue, taking the total to DM 60.4 bn. With income before taxes totaling DM 6.8 bn, Deutsche Telekom AG succeeded in exceeding the equivalent figure for 1996 by 88 percent. The currency crisis in Southeast Asia resulted in an unexpectedly high level of financial expense. Net income amounted to DM 3.3 bn after deduction of taxes totaling DM 3.5 bn. The proposal for the appropriation of net income calls for almost 100 percent of this amount to be distributed to the shareholders.

DM 1.20 dividend per share

The Supervisory Board and the Board of Management propose, subject to approval at the shareholders' meeting, to use the unappropriated net income of DM 3.3 bn to pay a dividend of DM 1.20 per share with nominal value of DM 5, on the dividend-bearing capital stock of DM 13.7 bn. In addition, shareholders who are fully subject to domestic taxes will receive a tax credit of DM 0.47 per share with nominal value of DM 5.

Balance sheet structure: Equity ratio enhanced

The balance sheet total for Deutsche Telekom declined DM 11.5 bn to DM 162.8 bn during the 1997 financial year. On the assets side, the reduction can be attributed mainly to the fall in noncurrent assets of more than DM 7 bn, with depreciation and disposals of property, plant and equipment being only partially offset by a lower level of capital investment. Current assets declined by DM 4.6 bn, primarily due to the use of liquid assets to reduce debt and to invest in securities. At December 31, 1997, shareholders' equity amounted to DM 48.1 bn (1996: DM 46.6 bn), with the equity ratio rising to 27.5 percent compared with 25.8 percent at the prior balance sheet date, excluding proposed dividend payments, which, for purposes of this calculation, were treated as short-term debt.

Further reduction in debt

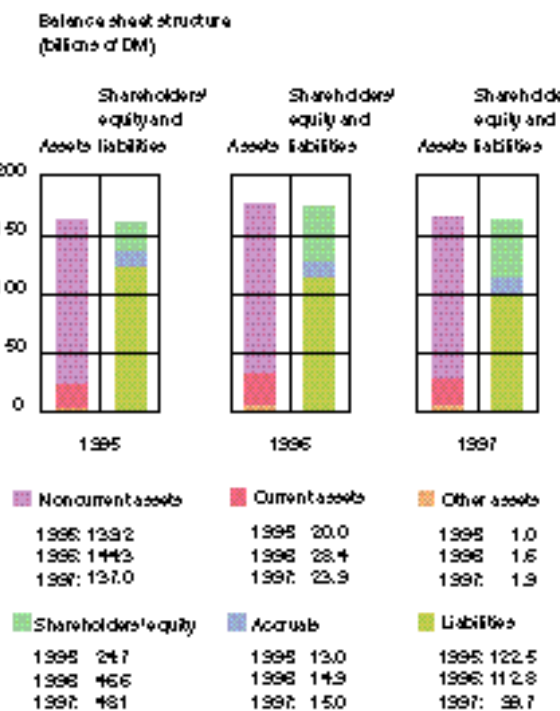
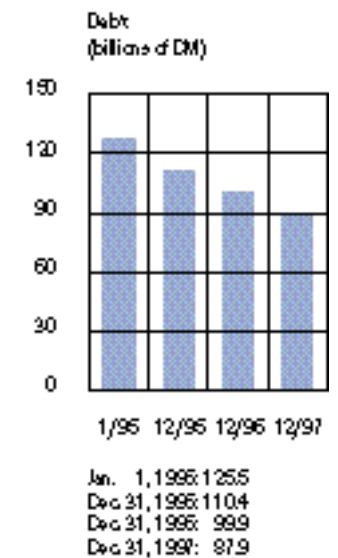
Deutsche Telekom has enhanced its financial structure by systematically reducing its debt by a further DM 1.2 bn (12 percent) to DM 87.9 bn. As a result, of the amount originally scheduled for repayment (around DM 60 bn in the old consolidated group), a total of DM 39 bn in debt has already been repaid since 1995; the reduction of debt to DM 65 bn by the year 2000 will continue to be a goal vigorously pursued in the future.

During the year under review, Deutsche Telekom set up a debt issuance program for a maximum of ecu 3 bn (just under DM 6 bn) with a view to further optimizing its financing costs at the same time as enhancing the maturity pattern of its debt. This program represents a framework agreement under which the company can raise funds on the international financial markets outside the United States in the future. Among other benefits, it also allows Deutsche Telekom to issue commercial paper in the form of publicly issued bonds and to make private placements in all major offering currencies and maturities.

High level of investments

During the 1997 financial year, investments at Deutsche Telekom totaled DM 15.5 bn (1996: DM 22.6 bn), of which DM 13.9 bn (1996: DM 17.0 bn) was invested in property, plant and equipment, and intangible assets, and a further DM 1.6 bn (1996: DM 5.6 bn) in financial assets. Investments in property, plant and equipment focused primarily on switching equipment, the telecommunications line network and transmission equipment. These investments in 1997 meant that work on digitizing the network could be completed. A total of DM 1.4 bn was spent on other plant and office equipment.

Of the DM 1.6 bn invested in financial assets, DM 0.9 bn was placed in fixed-income security issues (bond funds), mixed funds and equity funds launched by Deutsche Telekom AG with a view to optimizing returns on excess liquidity available for the medium and long-term. A further DM 0.3 bn was invested in associated companies; this mainly relates to payments of the second tranche of the investment to the Philippine companies, Isla Communications Company Inc. and Asiacom Philippines Inc., both in Manila.



Statement of cash flows (summarized)

billions of DM	1997	1996
Net cash provided		
by operating activities	22.6	22.3
Net cash used for		
investing activities	(10.5)	(25.3)
Net cash provided by (used for)		
financing activities	(13.8)	6.8
Net increase (decrease) in cash and cash equivalents	(1.7)	3.8
Liquid assets		
(short-term and long-term)	9.3	17.9

Cash generated from operations remains strong

Net cash provided by operating activities rose to DM 22.6 bn, while net cash used for investing activities declined to DM 10.5 bn during the year under review, mainly reflecting the lower level of investments in property, plant and equipment, and financial assets. The decrease in cash provided by (used for) financing activities of DM 20.6 bn to DM (13.8) bn in 1997 is primarily attributable to the comparison effects of the proceeds from Deutsche Telekom AG's global offering in 1996.

Financial derivatives hedge exposure

Derivative financial instruments are used to hedge exposure to interest rate and currency risk. These contracts are used solely for hedging purposes and not for speculation.

The notional amount of derivative interest rate contracts outstanding at December 31, 1997, was DM 9.8 bn, while forward exchange contracts outstanding totaled DM 0.4 bn. The derivative financial instruments were used to hedge and, to a minor extent, to optimize interest income.

The clear separation of duties in the organizational structure and the functional organization ensures that different people are responsible for trading and monitoring activities. To determine and control the risks associated with trading in derivatives, the transactions, once concluded, are immediately entered in a central treasury system, thus ensuring that the current transaction status can be monitored at all times.



“Coca-Cola now quenches thirst even faster. With mobile communications, such as Modacom and T-D1.“

Stefan Krenkel, Sales Advisor,
Coca-Cola, Berlin

Efficient purchasing

Investments in digitization completed

The total volume of goods and services purchased by the Group amounted to around DM 23 bn in 1997. This high volume was marked by the accelerated completion of network digitization. Nevertheless, the investment in property, plant and equipment was reduced considerably. This decrease related largely to prices, primarily reflecting developments in the market and advances in procurement logistics, with further price reductions being achieved in certain major areas of purchasing.

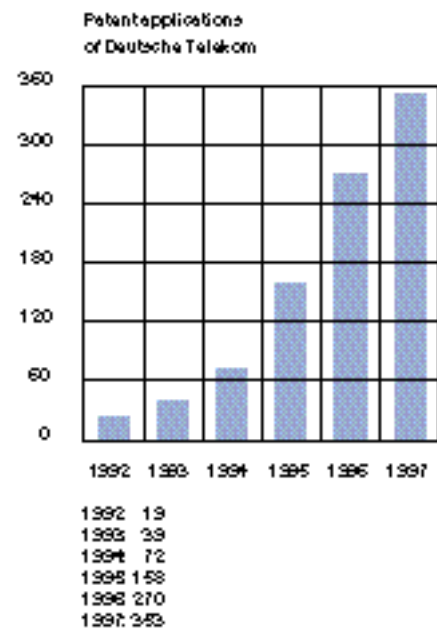
During the year under review, purchasing related principally to capital expenditure for telecommunications equipment and computer hardware and software (including related consultancy services).

Purchasing and logistics improved

By merging the purchasing and logistics functions to create the Purchasing and Logistics Group Service Center and forming the Logistics Center, Deutsche Telekom has succeeded in strengthening its supply management.

Over the last two years, the purchasing function has consistently worked towards more intensive collaboration with selected suppliers, with the main objective of reducing time-to-market by involving suppliers early on to utilize their expertise, signing Group-wide general contracts and cutting process costs. In this regard, Deutsche Telekom introduced purchasing by means of electronic data interchange in some areas during 1997 with a view to expanding the system in the future.

The policy of putting purchasing on a more international basis is being consistently expanded by using Deutsche Telekom's offices abroad. The aim of this strategy is to be able to react quickly in the significant technology markets in North America and South-east Asia.



Research and development

Customer-oriented and innovative
As an innovative enterprise on its way to becoming a telematics full-service provider, Deutsche Telekom views the development of new, customer-oriented products and services as one of our primary tasks. It's our goal to offer customers attractive, innovative and user-friendly products.

More than 4,000 trained staff members were involved in research and development as at the end of 1997, a little more than half of them at our software development centers and Multimedia Software GmbH in Dresden. Research and development work on new Deutsche Telekom products and services and on ways to raise efficiency and quality levels in our network infrastructure is conducted at our Darmstadt Technology Center and at T-Berkom in Berlin. Our development efforts focus on a variety of areas including telesecurity, user-friendly interfaces, voice processing, intelligent networks based on object-oriented architecture and applications such as teleworking, teleoffices and telelearning.

Together with leading international software houses, we have developed products that will open the door to the multimedia age for our customers.

Deutsche Telekom Advanced Solutions was established in Silicon Valley on June 1, 1997 to enable the early identification of international trends in the Internet and multimedia growth markets. This group pursues research, development and market monitoring tasks.

Venture capital enterprise established

In September 1997, we founded T-Venture (T-Telematik Venture Holding GmbH), a corporate venture capital enterprise that acquires stakes in young, innovative technology firms in the telematics field – that is, the field resulting from the convergence of telecommunications and information technology. T-Venture provides capital and entrepreneurial know-how to these companies. By doing so, we want to help translate innovation into marketable and profitable products.

Deutsche Telekom's innovative strength is evidenced by the marked increase in patent applications, which totaled 343 for the entire Group in 1997. No single patent is material for US securities law reporting purposes.

Many developments completed

The development of T-Intra, a multimedia value-added service, the T-Net-Box, a network digital answering machine, and the new service features in the digital T-Net network were among the projects completed in 1997. After carrying out extensive pilot projects, we launched an ATM (Asynchronous Transfer Mode) service that is being marketed throughout Germany. Our T-View 100 ISDN videophone is another example of a product brought to market in the year under review.

Together with the Berlin-based Heinrich Hertz Institute and the Technical University of Berlin, our Darmstadt research division succeeded in setting a "world record in transmission speed" last spring. For the first time ever, 40 Gbit/s were transmitted via conventional monomode optical fibers – like those used in our T-Net – over a 150-kilometer distance without the help of an intermediate repeater.

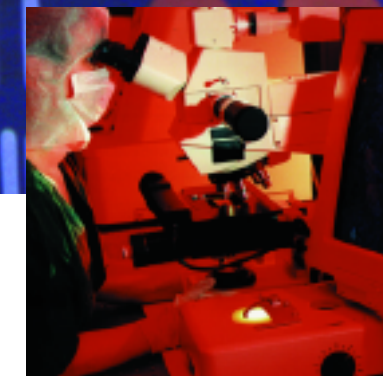
Access network enables broadband applications

In 1997, extensive tests were completed successfully so that a "broadband services" pilot project in North-Rhine/Westphalia will be conducted in the first half of 1998.



"To the benefit of my patients, I cooperate with other hospitals and doctor's offices to make use of the possibilities telemedicine has to offer."

Dr. Thomas Bäuml, Surgeon, Sport medicine



Telemedicine via ISDN: Here a pathologist is in his laboratory analyzing recordings of a tissue sample he has received during an operation by ISDN. It therefore takes him only a few minutes to decide how the operating team should continue. No more time-consuming transportation to an external laboratory. The patient is thus anesthetized no longer than absolutely necessary.

ADSL technology (Asymmetric Digital Subscriber Line) makes high-speed applications possible using copper cable in the local loop.

Deutsche Telekom's direct expenditures on research and development in 1997 totaled some DM 1.2 billion, 40 percent of which was spent on software development. By further improving our processes, we want to improve the quality and time-to-market of our products, services and networks in the coming years using the same resources.

Employees as of balance sheet date ¹	Dec. 31, 1997	Dec. 31, 1996	Dec. 31, 1995
Civil servants	91,542	105,419	114,430
Salaried employees	51,681	44,235	43,672
Wage earners	47,811	51,406	55,365
Deutsche Telekom group²	191,034	201,060	213,467

Changes in the composition of the Deutsche Telekom group of prior years (in particular MATAV)			
Trainees/student interns	18,261	19,607	-
	6,711	8,923	11,718

Total Deutsche Telekom group	216,006	229,590	225,185
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¹ adjusted to reflect full-time jobs

² before changes in the composition of the Deutsche Telekom group of prior years

Employees

Staff level down to 191,000

With approximately 191,000 employees at the end of 1997 – 47.9 % of them civil servants and 52.1 % non-civil servants – Deutsche Telekom is one of Germany's largest employers. These figures are based on the make-up of the 1995 consolidated group. Based on the consolidated group as at year-end 1997 – i. e. including the Hungarian company MATAV – the Company has approximately 209,000 employees.

More than one third of our employees are women. One of Deutsche Telekom's declared aims is to promote equal opportunities for women in all areas, including at the management level. In June 1997, Deutsche Telekom was awarded the "Total E-Quality" certificate for its comprehensive and successful efforts to promote equal opportunities.

Staff downsizing successful

In order to ensure Deutsche Telekom's ability to compete – and thus protect jobs in the long term – the Group's workforce is to be reduced, by socially acceptable measures, to approximately 170,000 employees by the year 2000. This goal corresponds to a workforce reduction of approximately 60,000 employees from the 1994 level, and does not include the employees of companies that were consolidated after 1995 (in particular MATAV). The staff reductions are being accomplished largely through natural attrition, early retirement programs and severance packages. Pursuant to a collective bargaining agreement with the unions, there will be no dismissals due to rationalization before the end of the year 2000. In turn, the same collective bargaining agreement provides for measures that will enhance flexibility and mobility of the workforce in terms of work areas and locations.

Workforce productivity considerably improved

As in the two previous years, the personnel reductions proceeded faster than planned: 10,000 positions were eliminated in 1997, meaning that the workforce decreased 5 % in comparison with the previous year. By the end

of the year, Deutsche Telekom had about 191,000 employees – as adjusted to reflect full-time jobs (comparative figure, thus it does not include MATAV). Previous accruals for the costs of the staff downsizing were recognized in the financial statements from 1994 to 1996 and did not affect the results of the year under review. Staff productivity increased by 12.5 percent in 1997, to DM 331,000 of revenue per employee (based on the composition of the 1995 consolidated group; the 1996 figure was DM 294,000).

Performance-based salaries

In response to the changed market conditions, Deutsche Telekom is gradually introducing a uniform compensation plan based on the individual employee's performance, which also takes into account the company's financial results. Similar performance-based and results-oriented compensation plans have already been introduced in the collective bargaining agreements for the employees of Deutsche Telekom's subsidiaries T-Mobil, DeTeCSM and DeTeSystem. Such a model for all other employees is currently being negotiated.

Pension plan restructured

During the year under review, Deutsche Telekom completely restructured its company pension plan. For each of its active employees, the Company makes annual payments into a capital account; when an employee becomes eligible for retirement, the account balance is either paid out as a lump sum or converted into an annuity.

In the past, payment obligations resulting from pension claims of former employees of Deutsche Bundespost were divided, in accordance with a set formula, among its successor companies. In the year under review, each beneficiary of a pension claim was assigned to a specific successor company. This arrangement contributes to the reduction of our pension expenses.

The pensions for civil servants continue to comply with the provisions laid down in the Second Posts and Telecommunications Reform.



"Life is easier with telecommunications – at home and at the office."

The Menzel family from Recklinghausen

Market-oriented career development

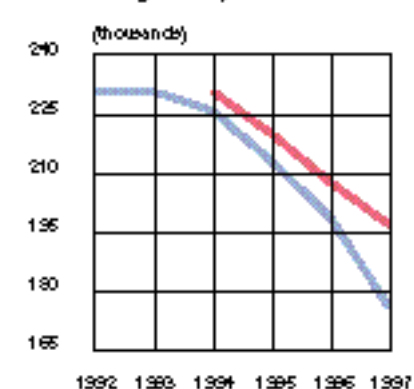
The commitment, motivation and know-how of our employees play a substantial role in the Group's success. Consequently, developing the skills and qualifications of the Group's employees is one of the primary tasks of our market- and performance-oriented personnel policy. Within the framework of the strategic plan for personnel, measures to promote career development such as annual discussions with employees, coaching and counseling groups, and the "High Potential" project for junior managers have been introduced. Comprehensive continuing education programs for employees help develop their qualifications – especially for the new demands that arise from the Company's evolution into a customer-oriented services company operating within an environment of open competition. Training expenditures for the 1997 financial year amounted to about DM 0.7 million.

New job profiles

In the year under review, the number of trainees in the Group averaged 6,200. A total of 400 trainees received open-end contracts upon completing their training, and 2,400 received fixed-term contracts.

To be able to continue offering young men and women training geared towards the future, the Group has defined new job profiles in the information and telecommunications technology sectors. These programs were started in the summer of 1997. In 1998, Deutsche Telekom will provide training for a total of 2,070 trainees – again, an increase over the previous year.

Number of Deutsche Telekom employees, average for the year (thousands)



■ Deutsche Telekom AG ■ Deutsche Telekom group

1992:	231,000	-
1993:	231,000	-
1994:	226,000	231,000
1995:	213,000	220,000
1996:	199,000	208,000
1997:	176,000	197,000

Number of employees, average for the year, adjusted to reflect full-time jobs (before changes in the composition of the Group of prior years, without trainees)

Broad sales coverage

Deutsche Telekom has 118 branch offices in Germany. It also maintains branch offices and representative offices at selected sites abroad.

Deutsche Telekom does not maintain any branches within the meaning of § 13 of the German Commercial Code (HGB).

Dependent company report

Due to the majority shareholding, Deutsche Telekom AG is a dependent company of the Federal Republic of Germany. No controlling agreement or profit-and-loss transfer agreement exists. Pursuant to § 312 of the German Stock Corporation Law (AktG), the Board of Management of Deutsche Telekom AG has therefore prepared a Dependent Company Report describing relations between the controlling body and affiliated companies. The Board of Management has included the following statement at the end of this report: "The Board of Management hereby states that, under the circumstances known to the Board of Management at the time of performing the business transactions, the Company received appropriate remuneration for such transactions. The Company did not perform or omit any actions on behalf of or on the instructions of the controlling company or any other affiliated companies."

Key events after December 31, 1997

Since the new German Telecommunications Act came into effect, Deutsche Telekom has submitted a large number of proposed tariff changes for approval by the Regulatory Authority. Of particular note at the beginning of 1998 are the new rates for voice telephony services at March 1, 1998, which were revised as part of the price-cap procedure prescribed by the Federal Ministry of Posts and Telecommunications pursuant to § 27 paragraph 1 (2) of the Telecommunications Act. The price changes, as approved in a letter dated January 30, 1998, are projected to result in savings for Deutsche Telekom customers amounting to around DM 2 bn.

An application made by Deutsche Telekom regarding the rates for providing subscriber access lines for competitors' services was not approved. In a letter dated March 9, 1998, the Regulatory Authority set the tariff for this service at DM 20.65 for a simple twin copper wire, while at the same time requiring a revised tariff proposal with lower rates to be submitted by May 22, 1998.

Outlook

Telecommunications – the market of the future

According to figures released by the OECD, the German economy is set to expand further in 1998, with above-average growth predicted for the telecommunications sector. Much is expected of the telecommunications market, but the potential is simultaneously accompanied by risks. Experts are predicting that telecommunications might well displace the automotive sector from its position as the key market over the next five years.

Consequently, potential for considerable growth is seen in mobile and data communications. Classical voice telephony, on the other hand, is expected to play more of a background role in revenue growth.

The volume of mobile communications services is said to expand in the wake of expected price cuts and the implementation of new technologies. A whole host of innovations are driving the growth of cable TV and Internet-based multimedia applications. As a result of the variety of services offered and the absence of applicable regulation, Internet service providers (ISPs) will increasingly compete directly with phone companies. It is estimated that 16 million people will use the Internet in the year 2000 compared with five million in 1997.

The future course of business at Deutsche Telekom

As the former monopoly supplier, Deutsche Telekom will lose market share in the parts of the market that were recently liberalized. The switch of traffic volume from the Company's own telephone network service to interconnection services will have an adverse impact on gross profits due to the level of interconnection rates.

Thanks to our customer orientation coupled with our comprehensive range of services and our state-of-the-art T-Net, we consider ourselves to be well prepared to take up the challenge of competition in the fully liberalized German telecommunications market. On the international front as well, the Company will systematically exploit the chances offered by the opening of the markets around the world.

Deutsche Telekom has set itself the following goals for the coming years:

- to increase its shareholder value and to offer its shareholders attractive returns,
- to expand its position as the leading supplier of complete telecommunications services in Germany,
- to offer its customers one-stop shopping worldwide, and
- to stimulate the demand for telecommunications services in the markets it serves, thus increasing revenues, cash flow and earnings strength, and improving its balance sheet structure.

Deutsche Telekom intends to use the following means to achieve these objectives.

Increasing customer satisfaction and strengthening customer loyalty

Deutsche Telekom has completed the process of turning itself into a customer- and earnings-oriented enterprise. In this respect, the range of products, services and tariffs offered by the Company is directed towards the various needs of its customers. To ensure that its products and services are always accessible and readily available, the Company maintains a dense network of sales and service outlets for the various customer groups it serves. Deutsche Telekom is convinced that the high quality of its services will play a decisive role in increasing customer satisfaction and strengthening customer loyalty, and therefore intends to pay close attention to further enhancing its sales and service activities.

New products and services based on the digital T-Net

Deutsche Telekom possesses one of the most modern networks in the world, which permits it to develop and market new products, services and customized solutions quickly. Moreover, the Company possesses the technology platforms and the know-how needed to meet the rising demand for more complex services and new applications like telematics and multimedia. One of the Company's objectives is to increase network utilization by offering open platforms and relocating intelligence from applications into the network.

Main investments in 1998

With the completion of the digitization of the network and the development program for eastern Germany in 1997, the Company expects the volume of investments and purchasing

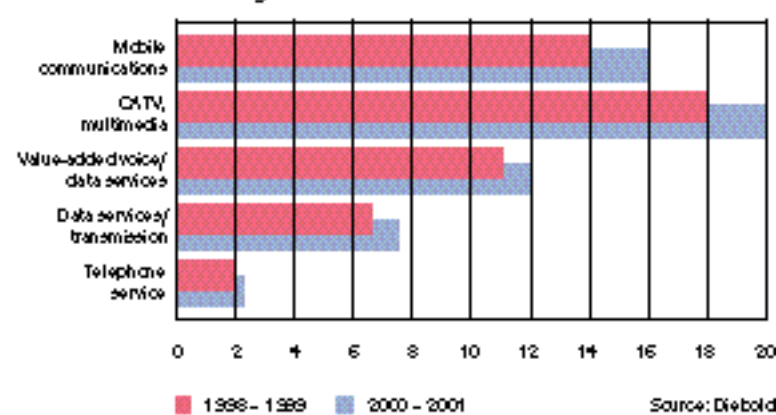
to drop sharply in 1998. Despite this, Deutsche Telekom plans to invest more than DM 9 bn in property, plant and equipment during the year.

Over DM 4 bn will be spent on further expanding the T-Net in 1998.

One major focus is the long-distance network, where a total well in excess of DM 2 bn is slated for investment. Major projects include new features in the telephone network service and the acquisition of worldwide submarine cable transmission rights, notably to cope with the rapid growth in Internet traffic. Being able to provide bandwidth is the decisive factor at the long-distance level: investments in an ATM platform and a new Internet platform will give Deutsche Telekom a strong position in these cutting-edge markets.

A second area highlighted for special attention is the access network, where more than DM 1 bn is to be invested during 1998, mostly on the installment of new lines to connect newly built-up areas and to make extensions to the existing network. In addition, investments in the access network give Deutsche Telekom's customers broadband access for multimedia applications and reflect the heavy demand for ISDN products.

Telecommunications: a growth market
German market
% annual growth rate



Further spending is planned to achieve the targeted savings in personnel costs by improving organizational flows and optimizing or installing new computer systems.

Medium-term investments

Through massive forward-looking spending, Deutsche Telekom is fostering the integration of the fixed network and the mobile communications network.

Almost DM 1 bn will be invested in the new product "broadband lines" in the medium term. Building on ADSL technology, these lines inexpensively provide high speeds for videotransmissions and Internet usage, thus helping to turn multimedia applications into a mass market.

Worldwide service for the customer

In its international operations, Deutsche Telekom is pursuing the strategy outlined below. On the one hand, the Company's customers increasingly expect to obtain their international telecommunications services in the fields of voice, video and data communications from a single source. With this in mind, Deutsche Telekom formed the Atlas/Global One joint venture with Sprint and France Telecom and further developed this Alliance. A strategic reorientation of Atlas/Global One is intended to sharply reduce the start-up losses run up by the venture.

At the same time, Deutsche Telekom is becoming involved in rapidly expanding national telecommunications markets. Besides committing capital, the Company is making full use of the technical know-how and management experience gained in the successful modernization of the telecommunications networks in eastern Germany and, in connection with the Company's stake in MATAV, in Hungary. Deutsche Telekom is continuing to pursue this strategy, planning to make selected

international commitments with a view to safeguarding its position in strategic markets and increasing shareholder value. Despite the current risks relating to the uncertain economic and political climate, Deutsche Telekom considers the markets in Southeast Asia to hold tremendous potential for the future and therefore does not intend to divest its local holdings in the region.

Increasing productivity and cutting costs

Reducing costs and improving productivity are of vital significance for Deutsche Telekom. The main factors involved here are personnel reduction measures without layoffs and the reduction of debt and the related interest expense. Further measures aimed at optimizing business processes and increasing productivity and efficiency have also been initiated.

Now that all the analog switching and transmission equipment has been fully depreciated, certain charges will not be incurred in the future, meaning that the level of depreciation and amortization will fall overall in the 1998 financial year.

Restructurings and selective price adjustments, such as those in the cable business and for directory services, will similarly help to improve the financial situation, while the locations of public telephones will be optimized.

A critical study will take a close look at the sale of terminal equipment with the aim of reaching a profitable solution in the near future.

Financing the future

The high level of cash generated from operations coupled with the potential for raising funds efficiently through the debt issuance program and the possibility of increasing the Company's equity capital nominally by up to an additional DM 1.4 bn by January 2, 2000, create the solid foundation necessary to finance the investments needed to secure the Company's future flexibly and inexpensively.



"DeTeSystem is developing a JAVA application for our worldwide information network which will enable us to accelerate the maintenance of our aircraft."

Dr. Rudolf Tewes, Head of Aircraft Maintenance, Lufthansa Technik AG

Revenue expected to continue growing

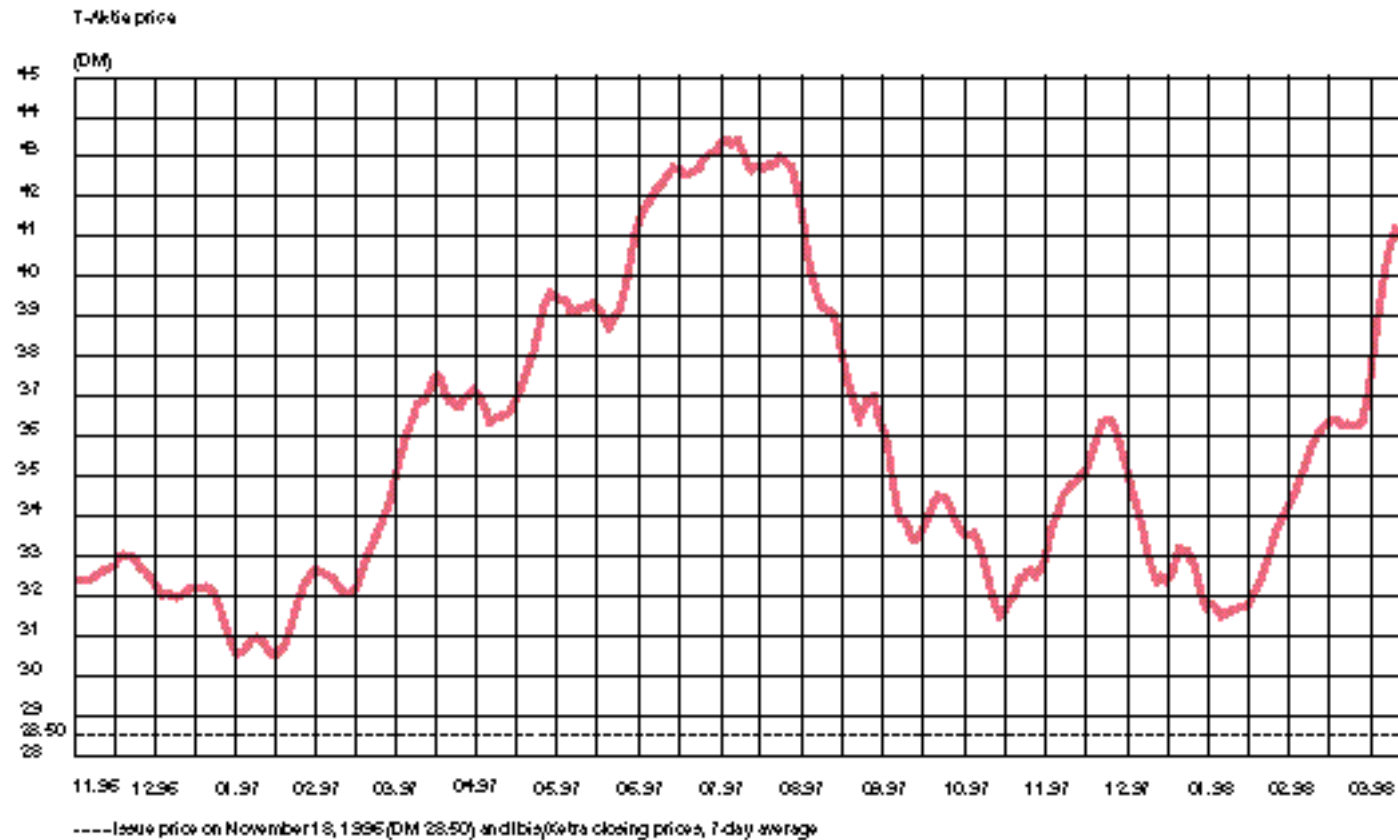
Despite tougher competition, Deutsche Telekom expects to gain from the continued expansion of the telecommunications market, and aims to pass on an appropriate share of the Company's profits to its shareholders.

Preparations for the Euro and the new millennium

To prepare the way for the introduction of the single European currency and the date change, Deutsche Telekom has initiated projects aimed at ensuring that its computer systems and applications are compatible with both.

With the introduction of the Euro in mind, Deutsche Telekom will propose to the shareholders' meeting the conversion of the common bearer shares currently with a nominal value of DM 5 each to no par shares at a ratio of one-to-one.

One of the major shares worldwide.



Highest and lowest prices of T-Aktie 1997
(Ibis/Xetra closing prices)

	High	Low
4th quarter 1996	DM 33.49	DM 31.44
1st quarter 1997	DM 38.41	DM 29.86
2nd quarter 1997	DM 43.11	DM 35.70
3rd quarter 1997	DM 44.20	DM 32.95
4th quarter 1997	DM 36.95	DM 30.30
1st quarter 1998	DM 41.65	DM 31.19

1997 was the first full year that the T-Aktie – the Deutsche Telekom share – was traded on the stock exchanges in Germany, the United States and Japan. The stock market in Germany displayed a marked upward trend in the first half of the year. After starting the year at 2,850 points, the German stock index – the DAX – reached its highest level in 1997 at the end of July with a high of 4,459 points (as measured at the close of trading on the IBIS computerized trading system). In the third quarter of 1997, however, the collapses of the stock markets and currency values in a number of Southeast Asian countries resulted in severe declines in share prices on practically all of the world's stock exchanges. Prices quickly recovered and the DAX ended the year at 4,224 points in the Xetra system which replaced the Ibis trading system on November 28, 1997.

Share price in 1997

Compared to the DAX, the performance of the T-Aktie was unsatisfactory. The T-Aktie reached its lowest value for the year of DM 29.86 on January 13, 1997. Beginning with a closing price of DM 31.98 on the first trading day in 1997, the share participated in the general buoyancy experienced by the German stock market during the first six months of the year. In mid-May, the German government announced that it would transfer part of its approximately 74 percent stake in Deutsche Telekom in two tranches to the federally owned Reconstruction Loan Corporation (Kreditanstalt für Wiederaufbau). This led to short-term uncertainty in the market and a drop in the price of the T-Aktie. However, in compliance with the provisions of the Second Posts and Telecommunications Reform, no shares held by the Federal Government may be sold on the stock exchange before the year 2000.

The share price experienced no noticeable pressure from sales upon sales of T-Aktie becoming free from German capital gains tax in May 1997, six months after our initial public offering in November 1996. On July 16, the T-Aktie reached its high for the year of DM 44.20.

Starting in August, the T-Aktie could not escape the general decline in prices on the German stock market and the share price fell. The T-Aktie came under additional pressure as a result of the decision by the Federal Ministry of Posts and Telecommunications regarding the prices for interconnection services. On the day the decision was announced, the T-Aktie suffered a loss of around 8 percent in price. It finished the year with a closing price of DM 33.28.

The T-Aktie's total trading volume on all German stock exchanges in 1997 was valued at more than DM 100 bn, the 11th highest volume amongst German shares. Trading volume on the New York and Tokyo stock exchanges were valued at approximately US\$ 1.1 bn and approximately yen 27 bn respectively. The price of the T-Aktie rose in the first quarter of 1998 and was thus part of the general rise in share prices.

Deutsche Telekom has 2,743.7 million shares outstanding, resulting in a market capitalization at year end of approximately DM 91 bn based on the year end closing share price. This figure positions Deutsche Telekom amongst the five largest companies in Germany by market value. Since Deutsche Telekom's initial public offering in 1996, about 26 percent of the T-Aktie are owned by private investors and institutional investors such as banks, insurance companies and investment companies. The remaining shares are held by the German government, with approximately 61 percent of the share capital held directly and, since the transfer of the first tranche of government shares on December 19, 1997 to the "Kreditanstalt für Wiederaufbau" about 13 percent indirectly. Pursuant to the Second Posts and Telecommunications Reform, the company may further increase its capital by issuing a total of 286.3 million shares; however, no decision has yet been made in this respect.

Announced dividend to be proposed at the annual shareholders' meeting

The consolidated earnings per share for the year ended December 31, 1997 was DM 1.20. As previously announced, a dividend of DM 1.20 per share will be proposed at the annual shareholders' meeting.

Earnings per share for 1997 – calculated in accordance with DVFA (German Society of Equity Research) – was DM 1.43. Our DVFA figure differs from net income per share mainly in the different treatment of goodwill amortization. Earnings per share for 1997 – calculated in accordance with U.S. GAAP – was DM 0.90. This discrepancy is due in particular to the different income tax effects. The method for calculating earnings per share according to U.S. GAAP is described in the notes to the financial statements included in this report.

Detailed information for our shareholders

We place great importance on the need to provide our shareholders with information. During 1997, the Investor Relations department began reporting directly to the Chief Financial Officer's office. Also during 1997, we hosted two analysts' meetings (to which invitations were also sent via DVFA), as well as two roadshows for financial analysts and institutional investors. More than 60 financial analysts currently monitor the progress of the company and evaluate its shares.

As early as January 16, 1998, Deutsche Telekom disclosed its results for the previous year, in accordance with the demands of the capital market for faster, more comprehensive information. Deutsche Telekom plans to continue this practice of promptly informing its shareholders of business developments.

1997 T-Aktie figures

Consolidated net income	DM 1.20 per share
Net cash provided by operating activities	DM 8.25 per share
DVFA/SG earnings	DM 1.43 per share
Earnings per share (U.S. GAAP)	DM 0.90 per share
Dividend proposal	DM 1.20 per share
Shareholders' equity	DM 17.02 per share

No. of T-Aktie shares issued (millions)	2,743
Market value (year-end)	DM 91.3 bn

Financial dates 1998

Press conference on the financial statements	April 28, 1998
Analysts' meeting (DVFA)	April 28, 1998
Shareholders' meeting (Hanover)	June 4, 1998
1998 Group half-year report	late August 1998

Press conference on the 1998 financial statements	April 1999
Shareholders' meeting	May 27, 1999

Stock exchange trading T-Aktie shares

Germany (all stock exchanges)	
New York (NYSE)	
Tokyo (TSE)	

Deutsche Telekom AG is a member of the "Deutscher Investor Relations Kreis e.V." (DIRK).

Regulation and competition:

German telecom market fully liberalized.

The legal framework for the regulation of the telecommunications sector in Germany was completely transformed by the Telecommunications Act (TKG), which took effect on August 1, 1996. This Act required the full liberalization of the German telecommunications market by January 1, 1998. It represented the final step in the liberalization of the telecommunications sector that started in 1989.

Liberalization began in 1989

Before 1989, the operation of telecommunications networks and the provision of telecommunications services were subject to a state monopoly exercised by the Deutsche Bundespost. In the initial phase of the liberalization process, text and data transmission services, and the entire terminal equipment sector, were opened up to competition. The mobile communications market became fully competitive in 1992, when digital mobile communications services were introduced. The provision of voice services for corporate networks and closed user groups via Deutsche Telekom's leased lines was liberalized in 1993. When the Telecommunications Act took effect in August 1996, the operation of transmission lines for all telecommunications services, with the exception of public voice telephony in the fixed network, was fully opened to competition.

Deutsche Telekom's broadband cable service has also faced competition from satellite television services and operators of broadband distribution and small master antenna television systems for some time. In recent years, Deutsche Telekom has also had to compete in the provision of international voice telephony with providers of bypass and call-back services and with resellers in general. With the removal of Deutsche Telekom's last exclusive right – namely, the right to provide public, domestic and international voice telephony to the public by means of a fixed network in Germany the liberalization of the German telecommunications market was completed.

The regulatory framework

In passing the TKG, Germany created the basis for virtually unrestricted market access by qualified entrants. The principal objectives of the Act are to promote a functioning, equal-opportunity competitive marketplace in the telecommunications sector through regulatory measures, to guarantee adequate telecommunications services throughout Germany and to provide for an efficient utilization of the frequency spectrum. Pursuant to the Act, licenses are required for the conduct of certain telecommunications activities. Furthermore, the Act creates a special regulatory framework for the allocation of frequencies, securing universal service and the regulation of companies with dominant market positions.

The Act is supplemented by numerous ordinances that govern important matters such as rates regulation, network access and network interconnection and the specifics of universal service. In December 1997, the Telecommunications Customer Protection Ordinance was revised and adapted to the new regulatory framework.

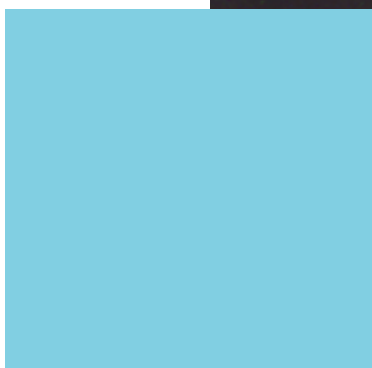
A new Regulatory Authority for Telecommunications and Posts was established on January 1, 1998 to succeed the former Federal Ministry of Posts and Telecommunications in the regulation of Germany's telecommunications sector.

Numerous licenses issued

The Telecommunications Act establishes licensing requirements for the provision of voice telephone services to the public and the operation of transmission lines that cross property boundaries and are used to provide public telecommunications services. Until the end of 1997, licenses were issued by the Federal Ministry of Posts and Telecommunications. On January 1, 1998, the new regulatory authority became responsible for issuing licenses. At the end of 1997, 67 class-3 licenses for the provision of transmission lines and 45 class-4 licenses for the provision of voice telephony services had been issued. At December 1997, over 60 additional applications for licenses had been submitted to the regulatory authority.

A number of other telecommunications services, such as text and data transmission services via leased lines and voice services for corporate networks and closed user groups are not subject to licensing requirements. At the end of 1997, approximately 1,000 providers of telecommunications services not subject to licensing requirements were registered with the Federal Ministry of Posts and Telecommunications.

With the full liberalization of the market as of January 1, 1998, Germany has complied with European Commission regulations stipulating the liberalization of the telecommunications markets of most EU member states by that date. Market liberalization has made Germany one of the most liberal and most competitive telecommunications markets in the world.



"See you later": The "T-View" videophone is an example of how residential customers can also benefit from ISDN: They can not only speak to each other, but see each other, too – with excellent picture quality. T-View also offers a broad spectrum of up-to-date information such as sports news, cinema schedules or travel tips.



"Talking to each other, understanding each other. A quick phone call can do wonders."

The Benkhoff family from Herten