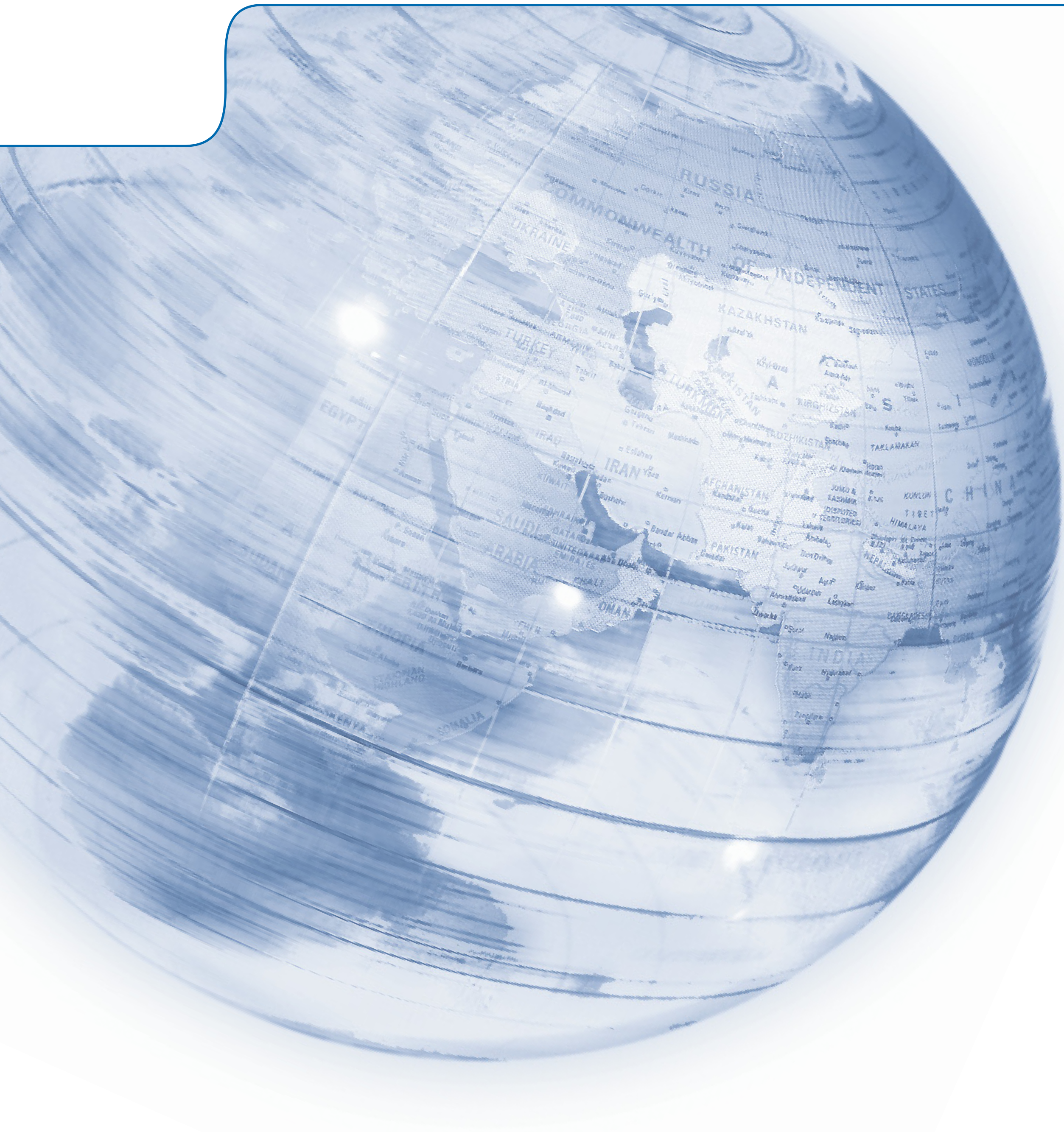
Second-quarter report 2004

Q2/04



software AG
THE XML COMPANY

Key figures IFRS, unaudited				
€ millions (unless stated)	**June 30, 2004**	**June 30, 2003**	**2Q 2004**	**2Q 2003**
Revenue	**202.0**	**206.3**	**106.3**	**103.1**
Products	143.5	141.2	76.2	72.0
of which licensing	52.6	45.8	29.4	24.0
of which maintenance	90.9	95.4	46.8	48.0
Professional services	57.6	64.3	29.6	30.7
Other	0.9	0.8	0.5	0.4
Adjusted EBIT	**39.4**	**25.4**	**24.2**	**17.4**
as % of revenue	20%	12%	23%	17%
Income from investments	24.5	0	24.5	0
Restructuring expenses	0	– 31.8	0	0
EBIT	**63.9**	**– 6.4**	**48.7**	**17.4**
Income before taxes	**65.4**	**– 4.8**	**49.6**	**18.2**
as % of revenue	32%	– 2%	47%	18%
Income after taxes	**49.2**	**– 3.6**	**39.4**	**11.2**
as % of revenue	24%	– 2%	37%	11%
Earnings per share (EUR)	**1.80**	**– 0.13**	**1.45**	**0.41**

	June 30, 2004	**June 30, 2003**
Employees	**2,467**	**2,896**
of which in Germany	815	1,211

€ millions (unless stated)	**30.06.2004**	**31.12.2003**
Total assets	**533.1**	**509.1**
Cash and cash equivalents	**110.5**	**74.2**
Shareholders´equity	**301.5**	**269.2**
as % of total assets	57%	53%

Profile

Software AG is an international provider of systems software and XML integration and data-management services. We offer integration solutions based on XML (eXtensible markup language), a key technology for the smooth exchange of data and documents, and a powerful means of introducing state-of-the-art applications into existing IT architectures. We are the European No. 1 and one of the world leaders in this area.

Karl-Heinz Streibich
Chief Executive Officer

Increased focus on core business generates added value

Software AG has achieved a great deal over the past months and this is clearly reflected in our results for the first half of 2004. Operational improvements are going hand in hand with financial success.

Our growth strategy consists of four consecutive stages: Rightsizing, greater focus, development of the organization's portfolio and expansion. The first two stages have been completed and we have reached the following important milestones:

- Increase profitability through the company right-sizing.
- A clear company focus on two business lines, representing our core competencies, as a result of restructuring.

Customer requirements are at the heart of everything we do

Our main goal during the first half of this year was to strategically refocus the company on Enterprise Transaction Systems and XML Business Integration. In line with our Customer First program, this helped us improve our performance in critical areas. For example, both business lines now benefit from highly effective, global product management. We have intensified international marketing efforts, leveraging successful strategies across regions. We have raised revenues by making our sales activities more customer-focused; and are fostering greater innovation by establishing new research and development centers.

Against this background, we have significantly strengthened our market position in both business lines: Enterprise Transaction Systems benefited almost immediately from increased growth and XML Business Integration is now enjoying improved conditions for business development.

A broader, solution-driven portfolio

We also started implementing the third stage of our strategy during the first six months:

- We optimized our product offerings and began the definition of a fuller portfolio based on market and customer requirements.

During the first quarter, we launched our new product packages for the modernization of enterprise transaction systems. The second quarter saw the international launch of XML Business Integration packages for systems integration with further packages to follow. Customer response to our optimized product portfolio has been very positive. The increased demand that this has generated will help both business lines to make further progress throughout the year.

Strong position in the integration solutions growth market

Over the coming months, we will continue to cement our new strategy based on our core competencies. This will entail assigning relevant R&D activities to the XML Business Integration or Enterprise Transaction Systems business lines. This will enable us to better address the specific characteristics and needs of both market segments.

The reorganization of R&D will accelerate innovation and expertise in our two business lines. Moreover, we will be able to recognize and respond more rapidly to changing requirements in the fast-moving XML market. This will clearly position Software AG as a pioneering and leading provider of integration solutions.

Geographical expansion offers exciting new opportunities

During the second half of 2004, we aim to activate additional drivers of business success.

- We will look to grow both organically and via strategic acquisitions and partnerships.

We intend to benefit from the considerable potential of promising growth markets through an increased presence. And we have already taken the first steps, for example in China, Russia, and South Africa.

Looking back at the first six months of this year, I truly believe that Software AG is heading in the right direction. We are well prepared to face the challenges of 2005.

Karl-Heinz Streibich
Chief Executive Officer

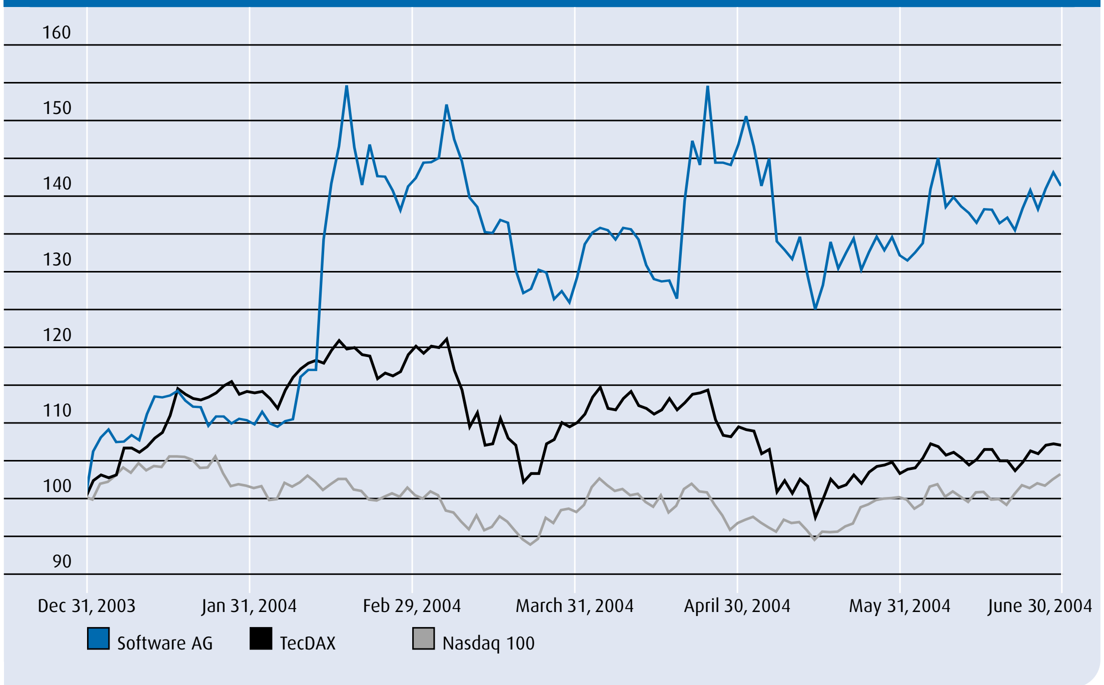
Software AG outperforms TecDAX

During the first six months of 2004 Software AG shares significantly outperformed the TecDAX. While the index of leading tech stocks rose approximately 7 percent over the period, Software AG shares gained 41 percent. Comparable US companies were also unable to match our impressive stock development: The NASDAQ 100 only increased by 3 percent between January and June.

Stock-market sentiment worsened during the second quarter. The high oil price and rising US interest rates had a negative impact on the global economy. Coupled with a troubled labor market in Germany, this had a negative impact on shares. In view of this poor climate, the development of Software AG stock is all the more impressive.

Having already significantly exceeded market expectations in both the fourth quarter of 2003 and the first three months of 2004, Software AG's Q2 2004 figures again outperformed projections. Two factors in particular led to a higher valuation for the Company, and a higher share price: The healthy positive development of license sales for products

Comparison of share development with leading indices



from our Enterprise Transaction Systems business line, and a further reduction in costs. The improved licensing situation in the Enterprise Transaction Systems business line helped to persuade investors and analysts that our decision to focus the Company on two business lines would succeed. This, in conjunction with successful moves to reduce costs, helped us to further improve profitability.

In the light of our six-month figures, we have again raised our full-year forecast for earnings per share (EPS). We now expect EPS to be between € 2.75 and € 2.85. This includes approximately € 0.88 attributable to the sale of shareholdings.

High resonance among investors

During the second quarter, we stepped up efforts to communicate our new strategic orientation. Software AG management met investors for group and one-on-one discussions on nine roadshows. We also presented our first-half results at an analyst and investor conference in London. This event was Webcast live, and a recording can be viewed online. JP Morgan is the latest major investment bank to provide coverage of Software AG shares. This is indicative of our higher profile, and will increase awareness of the Company among both private and institutional investors.

Shareholder's meeting passes all motions with overwhelming majority

The annual shareholders' meeting took place on April 30, 2004. CEO Karl-Heinz Streibich and CFO Arnd Zinnhardt introduced the Company's strategy and presented figures for full-year 2003 and first-quarter 2004. All agenda motions were adopted with overwhelming majorities. Dr. Andreas Bereczky was elected to the Supervisory Board to replace Dr. Peter Lex, whose mandate ended. The meeting also approved revised contingent capital and renewed the Executive Board’s share buyback authorization. The next annual shareholders' meeting will take place on May 13, 2005.

Table: Software AG shares

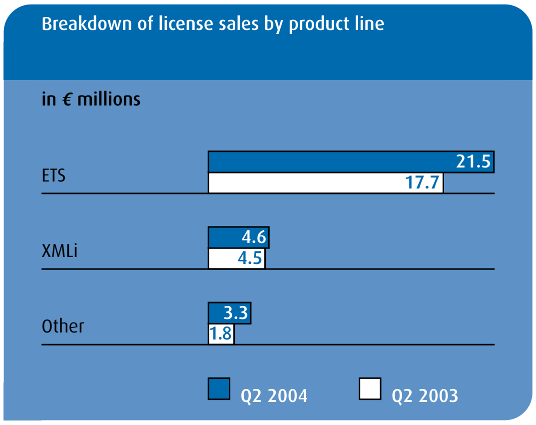
	June 30, 2004	June 30, 2003
XETRA closing price (in €)	23.00	11.90
Number of shares	27,266,752	27,266,752
Market capitalization (in € millions)	627	324
52-week high/low	25.16 / 11.81	

Frankfurt (Prime Standard/TecDAX), ISIN DE 0003304002, ticker symbol SOW

Positive business development borne out by rising revenues and earnings

In the second quarter of 2004, business continued to develop strongly at Software AG: Profits climbed sharply, license sales grew, and total revenues rose. We were able to build on a highly successful restructuring and strategy reorientation to exceed market expectations.

The Company posted a pre-tax profit of € 49.6 million, € 31.4 million higher than in the second three months of 2003. Net profit tripled to € 39.4 million. Software AG made further progress in terms of revenues too: Primarily as a result of growth in license business, consolidated revenues rose 3 percent in the second quarter to € 106.3 million (€ 103.1 million in Q2 2003.)



Development of revenues

License sales increase in both business lines

New software license sales increased by 23 percent to € 29.4 million (€ 24.0 million in Q2 2003). This was largely attributable to the Enterprise Transaction Systems business line, which after a strong first quarter, contributed € 21.5 million (€ 17.7 million in Q2 2003) between April and June. This line focuses on the modernization of mainframe systems. It profited from our Customer First program, which aims to intensify dialog between Software AG and its customers. Our new Enterprise Transaction Systems packages also spurred demand.

In spite of the general reluctance of companies to invest in new technologies, our XML Business Integration business line achieved a 2 percent gain in license sales to €4.6 million.

We generated € 46.8 million (€ 48.0 million) from maintenance during the period. Adjusted for currency translation effects, this figure is practically unchanged over the previous year. Combined revenues from licensing and maintenance rose to € 76.2 million (€ 72.0 million).

Increased demand for services

Project services also posted a notable increase in revenues during the second quarter, up 6 percent over the first quarter to € 29.6 million (€ 30.7 million). Three of our four regions increased sales in this area. Only in Central and Eastern Europe did the figure fall slightly. This was once again largely a result of price pressure and excess capacity on the German market.

Breakdown of revenues by region

in € millions	Q2 2004	Q2 2003
America	32.7	34.9
Southern and Western Europe	31.5	28.9
Central and Eastern Europe	22.1	22.8
Northern Europe, Asia/Pacific, South Africa	20.0	16.4

Strong licensing figures across the regions

License revenues increased in three of Software AG's business regions compared to Q2, 2003: Northern Europe / Asia posted a 57% increase, Central and Eastern Europe a 54% increase and Southern and Western Europe a 23% increase. These three regions all built on significant gains posted for the first three months of the year. The Americas region reported license revenues down by € 0.5 million at constant currency rates.

Profitability

Costs continue to fall

The restructuring program initiated in 2003 continued to generate significant cost reductions during the second quarter of the year. Compared to the second three months of 2003, for example, sales, marketing and distribution expenses fell by a further 9 percent and administrative costs by 12 percent. The most marked reduction was for research and development where, as a result of the consolidation of activities in this area, the Company saved € 4.9 million – around one third of all R&D costs.

Profits surge

Increased revenues and reduced costs combined to produce significant improvements in margins. Operating profit, for example, which excludes all exceptional income, rose 39 percent to € 24.2 million (€ 17.4 million). The sale of the Company's SAP SI stockholding raised € 24.5 million. As no restructuring costs were incurred during the period, EBIT totaled € 48.7 million (€ 17.4 million) – a 180 percent increase over the same period in 2003. The profit before tax rose from € 31.4 million to € 49.6 million.

Net profit of € 39.4 million (€ 11.2 million) led to increased earnings per share of € 1.45 (€ 0.41). Organic cash flow nearly tripled to € 11.7 million, 11 percent of total revenues.

Strategic progress

International launch of new XML Business Integration portfolio

We showcased our new XML Business Integration portfolio at Gartner Application Integration Summits in Los Angeles, Amsterdam and Sydney. Comprising of enhanced packages, it optimizes real-time access to business-critical information in existing IT systems. The highly innovative line of integration products exceeded market requirements. We therefore expect the launch of these products to provide extra momentum to XML Business Integration sales.

Commitment to promising growth markets

In line with the Company's growth strategy, we continued to develop both new and existing regional markets in the first half year. All regions played an active part in the process. Our new regional headquarters in Australia will strengthen our presence in Asia. And we intend to exploit the fast-growing Chinese market via a new strategic alliance with value-added reseller Shanghai 5A technology Development Co. Ltd. This agreement centers on XML Business Integration products.

Software AG is targeting significant two-digit annual growth in South Africa this year. In order to improve our position in this exciting market, we terminated our sales agreement with Dimension Data and established our own offices. Employees with relevant product expertise transferred from Dimension Data to Software AG.

A new world of opportunities in Eastern and Southern Europe

Software AG is now certified to provide mainframe products for the Russian government for high-security areas. In collaboration with Nicevt, Russia's leading hardware and software vendor, we have founded a competence center dedicated to the modernization and optimization of mainframes.

Newly formed SAG Systemhaus S.L. in Spain and Software AG Institute in Portugal will help to strengthen the Company's presence in Southern and Western Europe. Moreover, we recently signed a partnership agreement with Engineering Ingegneria Informatica, one of Italy's top-three systems integrators. We are also making a concerted effort to expand our technology partnerships in the USA.

Business development in first half year

Licensing contributes one quarter of consolidated revenues

The first half year at Software AG was characterized by rising license sales, up 15 percent over 2003 at € 52.6 million (€ 45.8 million). This represents an increase from 22 to 26 percent of total revenues. Including licenses and maintenance, and excluding currency effects, product sales gained 5 percent to € 143.5 million (€ 141.2 million). Total consolidated first-half revenues reached € 202.0 million (€ 206.3 million) – growth of 1 percent before currency effects.

Considerable cost reductions

Software AG continued to bring down expenses during the first half of the year. Compared to the first six months of 2003, costs for administration, sales, marketing and distribution, and R&D fell by a total € 19.3 million to € 90.9 million (€ 110.1 million). As a result, operating profit climbed by 55 percent to € 39.4 million.

Development of earnings		
in € millions	June 30, 2004	June 30, 2003
EBIT	63.9	– 6.4
Financial income	1.5	1.5
Pre-tax profit	65.4	– 4.8
Net profit	49.2	– 3.6

Significant improvement in cash flow
In spite of restructuring costs totaling € 19.3 million, net cash nearly doubled, rising to € 10.4 million (€ 5.3 million). Taking into account factoring, restructuring payments, and tax claims, organic cash flow rose to € 35.2 million, or 17.4 percent of total revenues.

Shareholders' equity rises by € 45.3 million
At June 30, 2004, cash and cash equivalents amounted to € 110.5 million, exceeding the 2003 figure by € 35.4 million. This was largely due to the sale of Software AG's stockholding in SAP SI. Shareholders' equity advanced to € 301.5 million, taking the equity-to-total-assets ratio to 57 percent. Total assets rose to € 533.1 million (€ 520.3 million). The reduction in fixed assets was due to the disposal of SAP SI shares.

Employee structure increasingly international
Restructuring of the Software AG workforce was completed sooner than expected: On June 30, 2004, the Group had 2,467 employees (2,896). This figure may rise slightly during the second half of the year. Approximately two thirds of the entire workforce are based outside Germany, which reflects the highly international structure and orientation of Software AG, and demonstrates the success of our efforts to create a lean holding company.

Positive business development set to continue

Since January, analysts have downgraded their full-year growth forecasts for the IT market as a whole. The 5 percent initially projected is no longer deemed realistic, as many companies are still consolidating capacity. At Software AG, we remain cautiously optimistic regarding the second half of the year.

Revenues will remain stable

Our decision to focus on two business lines, Enterprise Transaction Systems and XML Business Integration, will continue to have a positive impact during the second six months. In particular, this will encourage further growth in license sales. Enterprise Transaction Systems license volume will significantly exceed that of the previous year. And our XML Business Integration portfolio, which was launched during the second quarter, will promote growth in 2005. Adjusted for currency effects, we expect maintenance revenues to remain stable at the current high level. Sales of project services could stabilize further, but are expected to remain slightly below the previous year's figures. Adjusted for currency effects, we expect total revenues to remain at a similar level to 2003.

Cost reductions and more focused offering to drive profits

In 2003, Software AG posted an operating profit of € 59 million. In the current fiscal year, we expect to exceed this figure by around 40 percent – significantly higher than the previous forecast of 25 percent. Including the € 0.88 generated by the sale of SAP SI stock, we expect earnings per share to lie between € 2.75 and € 2.85.

Consolidated income statement for the six months ended June 30, 2004 (January 1 to June 30, 2004)

IFRS, unaudited

€ thousands	June 30, 2004	June 30, 2003	2Q 2004	2Q 2003
Revenue				
Products	143,510	141,170	76,121	71,958
of wich licencing	52,605	45,818	29,353	23,953
of which maintenance	90,905	95,352	46,768	48,005
Professional services	57,624	64,304	29,625	30,728
Other	841	802	510	450
Total revenue	**201,975**	**206,276**	**106,256**	**103,136**
Total costs of sales	– 68,997	– 76,681	– 35,692	– 37,247
Gross profit	**132,978**	**129,595**	**70,564**	**65,889**
Research and development	– 25,596	– 31,770	– 10,565	– 15,537
Sales, marketing and distribution	– 43,068	– 50,701	– 22,482	– 24,728
Administrative costs	– 22,166	– 27,667	– 11,060	– 12,583
Total operating expenses	**– 90,830**	**– 110,138**	**– 44,107**	**– 52,848**
Other income / expenses	– 2,798	5,991	– 2,237	4,383
Restructuring expenses	0	– 31,780	0	0
Income from sale of SAP-SI shares	24,539	0	24,539	0
Interest income / expenses	**1,499**	**1,521**	**848**	**817**
Profit before tax	**65,388**	**– 4,811**	**49,607**	**18,241**
Taxes	**– 16,229**	**1,250**	**– 10,205**	**– 7,031**
Net income	**49,159**	**– 3,561**	**39,402**	**11,210**
Earnings per share (EUR, basic)	1.80	– 0.13	1.45	0,41
Earnings per share (EUR, diluted)	1.80	– 0.13	1.45	0.41
Weighted average shares outstanding (basic)	27,266,752	27,266,752	27,266,752	27,266,752
Weighted average shares outstanding (diluted)	27,266,752	27,266,752	27,266,752	27,266,752

Consolidated balance sheets as of June 30, 2004

IFRS, unaudited

€ thousands	June 30, 2004	June 30, 2003	December 31, 2003
Assets			
A. Cash and cash equivalents			
1. Cash on hand and bank balances	72,619	46,762	53,083
2. Securities	37,847	28,300	21,076
	110,466	75,062	74,159
B. Current assets			
1. Inventories	388	392	387
2. Trade receivables	137,189	124,974	124,578
3. Other receivables and other assets	6,174	12,921	7,701
	143,751	138,287	132,666
C. Fixed assets			
1. Intangible assets	1,327	1,210	1,491
2. Goodwill	176,472	176,591	176,472
3. Property, plant and equipment	45,620	50,232	47,880
4. Financial assets	6,219	20,875	25,028
	229,638	248,908	250,871
D. Deferred taxes	41,008	49,860	44,959
E. Deferred expenses	8,213	8,208	6,476
Total assets	533,076	520,325	509,131
Equity and liabilities			
A. Current liabilities			
1. Current financial liabilities	4,981	4,820	6,546
2. Trade payables	20,421	21,882	26,770
3. Other current liabilities	23,632	28,262	25,294
4. Current provisions	57,704	73,152	77,791
	106,738	128,116	136,401
B. Non-current liabilities			
1. Non-current financial liabilities	4,088	5,947	4,356
2. Trade payables	6	0	22
3. Other non-current liabilities	3,639	3,533	3,641
4. Current provisions	20,786	19,001	19,666
5. Non-current provisions	4,769	4,248	5,596
	33,288	32,729	33,281
C. Deferred taxes	11,999	15,942	12,798
D. Deferres income	79,432	87,383	57,330
E. Minority interest	126	0	126
F. Equity			
1. Share capital	81,800	81,800	81,800
2. Capital reserve	132	132	132
3. Retained earnings	156,454	149,358	149,358
4. Consolidated income	49,159	– 3,561	7,096
5. Currency translation income	– 24,350	– 16,224	– 32,340
6. Other comprehensive income	38,298	44,650	63,149
	301,493	256,155	269,195
Total equity and liabilities	533,076	520,325	509,131

Cash flow statement for the six months ended June 30, 2004 (January 1 to June 30, 2004) IFRS, unaudited				
€ thousands	**June 30, 2004**	**June 30, 2003**	**2Q 2004**	**2Q 2003**
Income/loss after taxes	49,159	– 3,561	39,402	11,210
Depreciation	4,532	6,057	2,282	2,977
Income from sale of SAP-SI shares	– 24,539	0	– 24,539	0
Income from sale of other assets	– 6	363	– 8	352
Interest result	– 1,499	– 1,521	– 848	– 817
Income taxes	15,368	– 2,376	9,845	6,491
Cash generated from operations	43,015	– 1,038	26,134	20,213
Changes in inventories, receivables and other current assets	– 12,843	– 1,600	– 13,533	– 3,259
Changes in payables and other liabilities	– 11,695	27,073	– 8,264	– 12,697
Income taxes paid	– 6,776	– 16,771	– 2,778	– 7,934
Interest paid	– 519	– 632	– 319	– 249
Interest received	1,932	2,080	1,129	1,064
Net cash used in/provided by operating activities	**13,114**	**9,112**	**2,369**	**– 2,862**
Cash received from the sale of tangible/intangible assets	56	547	34	255
Investments in property, plant and equipment/ intangible assets	– 1,916	– 2,981	– 1,179	– 1,111
Cash received from the sale of financial assets	26,138	6	26,103	2
Investments in financial assets	– 748	– 838	– 191	– 373
Net cash used in/provided by investing activities	**23,530**	**– 3,266**	**24,767**	**– 1,227**
Repayment of loans from acquisitions and other finance liabilities	– 1,497	– 4,433	– 770	– 788
Net cash used in/provided by financing activities	**– 1,497**	**– 4,433**	**– 770**	**– 788**
Change in cash funds from cash relevant transactions	**35,147**	**1,413**	**26,366**	**– 4,877**
Currency translation adjustments	**1,160**	**– 1,774**	**1,002**	**– 946**
Net change in cash and cash equivalents	**36,307**	**– 361**	**27,368**	**– 5,823**
Cash and cash equivalents at the beginning of the period	74,159	75,423	83,098	80,885
Cash and cash equivalents at the end of the period	**110,466**	**75,062**	**110,466**	**75,062**

Segment report for the six months ended June 30, 2004 (January 1 to June 30, 2004)

IFRS, unaudited

€ thousands	Americas	Southern and Western Europe	Northern Europe, Asia/Pacific, South Africa	Central and Eastern Europe	Total	Central functions, R&D and Consolidation	Total Group
Licenses	13,620	12,090	15,642	11,254	52,606	– 1	52,605
Maintenance	38,692	13,686	18,612	19,939	90,929	– 24	90,905
Services	7,495	33,766	3,998	12,479	57,738	– 114	57,624
Other	274	215	66	43	598	243	841
Total revenue	**60,081**	**59,757**	**38,318**	**43,715**	**201,871**	**104**	**201,975**
EBITA	17,787	5,840	10,146	6,688	40,461	– 1,111	39,350
Amortization							0
Interest result							1,499
Income from SAP-SI sale							24,539
Profit before tax							65,388
Taxes							– 16,229
Net income							49,159
Total revenue proportion per region	29.8%	29.6%	19.0%	21.6%	100.0%		
Product revenue	52,312	25,776	34,254	31,193	143,535		
Proportion per region	36.4%	18.0%	23.9%	21.7%	100.0%		

Segment report for the six months ended June 30, 2003 (January 1 to June 30, 2003)

IFRS, unaudited

€ thousands	Americas	Southern and Western Europe	Northern Europe, Asia/Pacific, South Africa	Central and Eastern Europe	Total	Central functions, R&D and Consolidation	Total Group
Licenses	16,716	9,997	10,825	8,246	45,784	34	45,818
Maintenance	42,487	13,633	18,789	20,449	95,358	– 6	95,352
Services	9,041	34,450	3,441	17,936	64,867	– 563	64,304
Other	48	42	270	83	444	358	802
Total revenue	**68,292**	**58,122**	**33,325**	**46,715**	**206,453**	**– 177**	**206,276**
EBITA	19,257	6,150	7,916	2,685	36,008	– 10,560	25,448
Amortization							0
Interest result							1,521
Restructuring expense							– 31,780
Profit before tax							– 4,811
Taxes							1,250
Net loss							–3,561
Total revenue proportion per region	33.1%	28.2%	16.1%	22.6%	100.0%		
Product revenue	59,203	23,630	29,614	28,695	141,142		
Proportion per region	42.0%	16.7%	21.0%	20.3%	100.0%		

Segment report for Q2 2004 (April 1 to June 30, 2004) IFRS, unaudited							
€ thousands	Americas	Southern and Western Europe	Northern Europe, Asia/Pacific, South Africa	Central and Eastern Europe	Total	Central functions, R&D and Consolidation	Total Group
Licenses	8,455	6,767	8,233	5,899	29,354	– 1	29,353
Maintenance	19,766	7,197	9,759	10,055	46,778	– 10	46,768
Services	4,312	17,356	1,974	6,092	29,734	– 109	29,625
Other	175	166	31	21	393	117	510
Total revenue	**32,707**	**31,487**	**19,997**	**22,067**	**106,259**	**– 3**	**106,256**
EBITA	10,306	3,170	5,174	2,828	21,477	2,744	24,220
Amortization							0
Interest result							848
Income from SAP-SI sale							24,539
Profit before tax							49,607
Taxes							– 10,205
Net income							39,402
Total revenue proportion per region	30.8%	29.6%	18.8%	20.8%	100.0%		
Product revenue	28,221	13,965	17,992	15,955	76,132		
Proportion per region	37.1%	18.3%	23.6%	21.0%	100.0%		

Segment report for Q2 2003 (April 1 to June 30, 2003) IFRS, unaudited							
€ thousands	Americas	Southern and Western Europe	Northern Europe, Asia/Pacific, South Africa	Central and Eastern Europe	Total	Central functions, R&D and Consolidation	Total Group
Licenses	9,329	5,509	5,251	3,829	23,918	35	23,953
Maintenance	21,144	6,931	9,349	10,234	47,658	347	48,005
Services	4,394	16,456	1,606	8,742	31,198	– 470	30,728
Other	47	21	239	30	337	113	450
Total assets	**34,914**	**28,917**	**16,445**	**22,835**	**103,111**	**25**	**103,136**
EBITA	11,465	3,027	4,096	1,012	19,600	– 2,176	17,424
Amortization							0
Interest result							817
Restructuring result							0
Profit before tax							18,241
Taxes							– 7,031
Net income							11,210
Total revenue proportion per region	33.9%	28.0%	16.0%	22.1%	100.0%		
Product revenue	30,473	12,440	14,600	14,063	71,576		
Proportion per region	42.6%	17.4%	20.4%	19.6%	100.0%		

Statement of changes in equity for the six month ended June 30, 2004 (January 1 to June 30, 2004)

IFRS, unaudited

€ thousands	Shares		Capital reserve	Retained earnings	Consolidated income	Currency translation differences	Other comprehensive Income	Total
	Number	Share capital						
As of January 1, 2004	27,266,752	81,800	132	156,454	0	– 32,340	63,149	**269,195**
Consolidated income for the period					49,159			49,159
Currency translation differences						7,990		7,990
Measurement of financial assets							– 18,301	– 18,301
Currency translation							– 6,550	– 6,550
As of June 30, 2004	27,266,752	81,800	132	156,454	49,159	– 24,350	38,298	**301,493**

Statement of changes in equity for the six month ended June 30, 2003 (January 1 to June 30, 2003)

IFRS, unaudited

€ thousands	Shares		Capital reserve	Retained earnings	Consolidated income	Currency translation differences	Other comprehensive Income	Total
	Number	Share capital						
As of January 1, 2003	27,266,752	81,800	132	149,358	0	0	27,639	**258,929**
Consolidated income of the period					– 3,561			– 3,561
Currency translation differences						– 16,224		– 16,224
Measurement of financial assets Currency translation							17,011	17,011
As of June 30, 2003	27,266,752	81,800	132	149,358	– 3,561	– 16,224	44,650	**256,155**

Accounting principles

Basis

Since the beginning of 2004, the consolidated financial statements of Software AG have been prepared in accordance with the International Accounting Standards Board's (IASB) International Accounting Standards (IAS) and International Financial Reporting Standards (IFRS). Software AG complied with the IAS and IFRS, and IFRIC (International Financial Reporting Interpretations Committee, formerly SIC) interpretations applicable on December 31, 2003.

Figures in the consolidated financial statements are, unless otherwise stated, quoted in thousands of euros (€ thousands).

Principals of consolidation

The consolidated financial statements include Software AG and companies under its control. Control is generally taken to be proven where the Group holds, directly or indirectly, the majority of voting rights for authorized capital in a company, and/or can determine the fiscal or business policy of the company.

The financial statements of consolidated companies are compiled according to consistent accounting and valuation principles.

Subsidiaries established by Software AG are consolidated on the date they are formed. However, first-time consolidation occurred after the date of foundation for Softinterest Holding AG and its subsidiaries – which were consolidated for the first time in 1994 – as well as for Asian subsidiary SQL and for SAG-IRL.

The first-time consolidation of all companies was undertaken using the book value method. Subsequent consolidation is derived from the figures employed for first-time consolidation.

Debit balances arising from capital consolidation and relating solely to goodwill from acquisitions before January 31, 2001, were netted against capital reserves, pursuant to Section 309, Subsection 1, of the German Commercial Code (HGB). Goodwill from acquisitions after January 31, 2001, was capitalized and will be amortized over ten years. In accordance with the option granted by IFRS 1.14, the Company has not applied IAS 22 retrospectively, but has continued to use the figures for mergers and acquisitions posted according to HGB.

Revenue, expenses and income, receivables, liabilities, and provisions arising between consolidated companies have been eliminated. Intercompany earnings from services provided within the Group were also eliminated where these were not realized from services to third parties.

Consolidated companies

On May 13, 2004, SAG Systemhaus S.L., Madrid, Spain was founded with subscribed capital of € 60 thousand. As of this date, the new company was consolidated as part of the Software AG Group. This was the only change to the scope of consolidation in comparison with December 31, 2003.

Estimates and assumptions

In a few instances, estimates and assumptions were made which could impact the statement and amount of figures posted for balance-sheet assets, debt, income, expenses and contingent liabilities. True values may deviate from these estimates and assumptions.

Currency translation
The financial statements of foreign subsidiaries are translated using functional currencies: As these companies have organizational, financial, and commercial independence, the respective local currency is identical to the functional currency. Assets and liabilities are translated according to the exchange rate on the balance-sheet date, and expenses and income according to monthly averages. Currency translation differences are posted as such under equity, but not recognized in net profit or loss for the period.

In the individual financial statements for consolidated companies, foreign-currency items are translated on the balance-sheet date, and included in net profit or loss for the period. Translation differences from long-term intercompany cash items are excepted from this rule. These are posted as other comprehensive income under equity, but not recognized in net profit or loss for the period.

Cash on hand and bank balances
This item includes cash and short-term investments, plus short-term cash equivalents.

Cash equivalents are short-term, highly liquid financial investments which can be converted to cash at any time, and which are only subject to immaterial fluctuations in value.

Securities and financial assets
Financial assets are initially valued at the cost of acquisition, including transaction costs. The subsequent valuation depends on their classification.

Financial assets which are available for sale are valued according to their price on the balance-sheet date (i.e. the fair market value). Price gains or losses are posted as other comprehensive income under equity, but not recognized in net profit or loss for the period.

Software AG uses hedging instruments to protect against the risks posed by worldwide currency fluctuations. Company policy is to hedge against currency risks in their totality, and not take specific action for each individual transaction. Open positions in futures transactions are valued at the fair market price, and listed on the balance sheet under securities held for trading purposes. Price gains or losses are included in the net income figure for the relevant year.

Financial assets are recorded at their individual fair market values where this is possible to calculate and the assets have not been held until maturity. Loans and receivables included under this item which are not held for trading purposes, and assets with no publicly available price on an active market, where it is not possible to reliably calculate a fair market price, are valued at the adjusted cost of acquisition. All values are subject to regular, objective impairment testing, and value impairment, where it has occurred, is reflected in earnings for the period.

Inventories
Inventories are recorded at the lower of cost of acquisition / manufacture or net realizable value. Net realizable value is the estimated amount that would be raised from a sale during normal operations, less the estimated costs arising until manufacture is complete, and less sales costs.

Trade receivables
Trade receivables are posted at the fair value applicable when revenues are realized or services provided, and valued at the net book value, less any necessary value adjustments.

This item also includes unbilled services from projects for which a fixed price has been agreed, but for which the percentage of completion method is applied.

Other current assets

Other current assets are valued at cost of acquisition, which corresponds to fair market value.

Intangible assets

Concessions, industrial and similar rights and assets, and licenses to such rights are capitalized at cost of acquisition and amortized over their useful economic lives according to the straight-line method. These assets are regularly subject to impairment testing.

Goodwill

Debit balances arising from capital consolidation as defined by HGB are calculated according to book value, with no disclosure of hidden reserves. Before January 31, 2001, balances were offset against capital reserves, pursuant to Section 309, Subsection 1 of HGB. After this date, goodwill was capitalized and amortized over ten years according to the straight-line method. The term over which goodwill is amortized is established at the time of the acquisition, based on the useful economic life of the goodwill. Software AG makes use of IFRS 1.13, which allows the Company to retain HGB valuations of goodwill arising before the transition to IFRS accounting on January 1, 2003. In accordance with IFRS 3, the historical HGB valuation of goodwill was posted at € 176,591 thousand on this date. IFRS 3 requires that goodwill is no longer amortized, but subject to annual impairment testing and examination of its future useful economic life. The residual book value is written down to its fair value where the value has been impaired.

Property, plant and equipment

Property, plant and equipment are stated at cost of acquisition or manufacture less accumulated depreciation and impairment costs. Where items are sold or scrapped, the relevant cost of acquisition and accumulated write-downs are eliminated – any realized income / loss from the disposal of the asset is shown on the income statement.

Tangible assets acquired for € 410 or less are fully written down in the year they are first posted.

Cost of acquisition / manufacture comprises purchase price, including any customer payments and non-refundable income tax, and costs that are directly attributable to preparing the asset for its intended use. Expenditure such as maintenance incurred once the asset is in use is posted in the period during which it is incurred. Subsequent expenditure is only booked under assets where this improves the condition of the asset beyond its originally assessed standard of performance. Financing costs are not included under cost of acquisition / manufacture.

Property, plant and equipment are depreciated over their useful economic lives according to the straight-line method:

Buildings	50 years
Leasehold improvements	8 – 10 years
Office equipment	3 – 13 years
Computer hardware and accessories	1 – 4 years

Useful economic lives and methods of depreciation are periodically examined to ensure that theoretical values correspond with actual expected values.

Assets under construction are allocated to unfinished property, plant and equipment, and stated at cost of acquisition / manufacture. Depreciation only takes place once manufacture is complete and the asset is in use.

Impairment of the value of intangible assets and property, plant and equipment

Where there is evidence that the value of intangible assets, property, plant and equipment has been impaired, these are immediately written down to their recoverable values, i.e. the higher of net realizable value and value in use. Value in use is the cash value of forecast future cash flows from the continued use of an asset and from disposal at the end of its useful economic life.

Leasing

Fixed assets include assets provided under leasing contracts. Software AG leases property, plant, and equipment. According to IAS 17, leasing contracts are classified as capital leases (where the leased asset is allocated to the lessee) or operating leases (where the leased asset is allocated to the lessor).

Capital leases: Leased items are posted on the balance sheet under both assets and leasing liabilities (at the same amount). The fair market value of the leased item at the beginning of the contract is used, or, where less, the cash value of the total minimum leasing payments. Calculation of this cash value is based on the interest rate of the overall lease agreement, where this figure can be practically identified. Otherwise, the lessee's threshold borrowing interest rate is used. Capital leases are amortized over their scheduled useful economic lives according to the straight-line method. Future lease installments are posted as financial liabilities.

Operating leases: Operating lease payments are expensed throughout the life of the leasing agreement.

Deferred taxes

Tax assets and liabilities are deferred according to the balance-sheet liability method for temporary differences between figures stated for tax purposes and those on the consolidated balance sheets. Taxes are also deferred on loss carryforwards.

Deferred taxes are calculated according to the tax rate expected to apply in the year in which they will be realized. Dividends are only included once the annual shareholders' meeting has voted on the use of earnings.

Deferred tax assets and liabilities are not discounted.

The book values of deferred taxes are regularly examined and, where necessary, adjusted.

Prepaid expenses

This item includes prepayments made by Software AG within the scope of license and rental agreements. Amounts are reversed and booked as expense in the accounting period when the service is delivered to Software AG.

Liabilities

Short-term liabilities are stated at their repayment or fulfillment value.

Long-term liabilities are stated at adjusted cost of acquisition, calculated according to the effective interest method, i.e. by discounting expected future repayments.

Provisions

Provisions are formed where the Company has a de jure or de facto obligation to a third party arising from an event in the past, where it is likely that the Company will have to settle this obligation, and a reliable estimate can be made of the value of the liability. Estimates are subject to regular scrutiny and adjustment.

Where the effect of the time value of money is material, the amount of a provision is the present value of the expenditures expected to be required to settle the obligation.

Provisions for pensions

Software AG operates both defined-benefit and defined-contribution pension plans. The actuarial calculation of provisions for pensions follows the projected unit credit method described in IAS 19, whereby expected future increases in pensions and salaries are also included.

For the defined-contribution plan, Software AG has no obligations beyond its undertaking to pay all contributions to earmarked funds.

Deferred income

Deferred income includes prepayments from customers for maintenance services. Amounts are reversed and posted as revenue in the period Software AG delivers the service.

Other comprehensive income

Other comprehensive income comprises differences arising from the translation of the financial statements of commercially independent non-German subsidiaries, and effects from the valuation of financial instruments. Also included are translation differences from cash positions that are primarily part of a net investment in a commercially independent non-German subsidiary. Figures are quoted after tax.

Equity

Development of shareholders equity is shown on page 18.

In addition, contingent capital at June 30, 2004, comprised the following amounts:

1.) Up to € 3,357 thousand in up to 1,118,962 no-par value shares, reserved to cover subscription rights granted under the first share-option plan (Management Incentive Plan I, MIP I) for Executive Board members and senior executives of the Software AG Group. The terms and conditions of this plan, as well as the numbers of shares allocated / exercised, are given on page 32.
2.) Up to € 3,000 thousand in up to 1,000,000 no-par value shares, reserved to cover subscription rights granted under the second share-option plan (Management Incentive Plan II, MIP II) for Executive Board members and senior executives of the Software AG Group. The terms and conditions of this plan, as well as the numbers of shares allocated / exercised, are given on page 32.
3.) Up to € 13,515 thousand in up to 4,505,000 no-par value shares, reserved to grant option rights to holders of warrants from cum-warrant bonds, and to grant conversion options to holders of convertible bonds in accordance with the bonds' terms. The Executive Board is authorized to issue such bonds, with a term of up to 10 years, once or more than once in the period to April 27, 2006, up to a total nominal value of € 500,000 thousand. The Executive Board had not made use of this authorization by June 30, 2004. At the annual shareholders' meeting on April 30, 2004, the entitlement to draw on this capital was withdrawn and replaced by that detailed under section 4 below.
4.) Up to € 36,000 thousand in up to 12,000,000 bearer shares, each with a € 3 share of capital stock, reserved to grant option rights and to agree option obligations arising from option-bonds, and to grant conversion options and option obligations to holders of convertible bonds in accordance with the bonds' terms (agreed at the annual shareholders' meeting on April 30, 2004). Subject to the approval of the Supervisory Board, the Executive Board may authorize the exercise of these rights by Software AG or a (directly or indirectly) wholly owned subsidiary by April 29, 2009.

In this instance, shareholders are entitled to subscription rights, with the following exceptions:

- The Executive Board is authorized to exclude fractional amounts.
- Subject to the approval of the Supervisory Board, the Executive Board is authorized to totally exclude shareholders' subscription rights in the following instance: Where, upon due examination, the issue price of options or convertible bonds is not thought to be significantly less than its hypothetical market value (i.e. such value being calculated by accepted financial industry methods). However, this right to exclusion only applies to options and convertible bonds with rights or obligations for shares totaling no more than € 8,180 thousand, or, where lower, 10 percent of capital stock at the time the subscription rights are excluded.

The Executive Board had not made use of this authorization by June 30, 2004.

At the balance-sheet date, the Executive Board is further authorized, with the consent of the Supervisory Board, to increase the Company's subscribed capital by up to € 37,989 thousand once or more than once in the period to April 27, 2006, by issuing up to 12,663,036 registered shares against cash and/or non-cash contributions (authorized capital). With the exception of the cases detailed below, shareholders will be granted pre-emptive subscription rights:

- The Executive Board is authorized to deviate from shareholders' pre-emptive subscription rights with respect to fractional amounts.
- The Executive Board is further authorized, with the consent of the Supervisory Board, to deviate from shareholders' pre-emptive subscription rights with respect to capital increases against non-cash contributions effected for the purpose of acquiring participations, holdings, companies or business units.
- The Executive Board is also authorized, with the consent of the Supervisory Board, to deviate from shareholders' pre-emptive subscription rights provided that the capital increase against cash effected on the basis of this authorization does not exceed 10 percent of the subscribed capital at the time this authorization is first exercised, and provided that the issue price is not significantly lower than the market value.
- Finally, the Executive Board is authorized, with the consent of the Supervisory Board, to deviate from shareholders' pre-emptive subscription rights with respect to a nominal amount not exceeding € 6,503 thousand in order to offer new shares to employees of Software AG and its affiliated companies (in accordance with sections 15 ff. of the German Stock Corporation Act) under an employee share option plan. The new shares can also be transferred to a bank on condition that sale is restricted to entitled persons in accordance with the Company's instructions.

At June 30, 2004, the Executive Board had not exercised its power to increase subscribed capital.

Revenues

Software AG primarily generates revenues from software licenses (for unlimited periods of usage), maintenance, and other services. Incoming monies from software licenses are only posted as revenues once a contract has been signed with the customer, all possible rights of return have expired, the software has been supplied, and a price has been agreed or can be established, and there is sufficient probability that payment will be made.

Maintenance revenues are prorated over the period of service provision.

Revenues from contract work invoiced according to man-hours are recognized once the services have been provided by Software AG.

Pursuant to IAS 11 and IAS 18, revenues from fixed-price service contracts are recognized according to the percentage of completion method where the revenues can be reliably measured, there is sufficient probability that Software AG will receive the economic benefits of the transaction, and that all related costs expected until completion of the service can be reliably measured.

Revenues figures are net of all discounts and rebates.

Costs of manufacture

Costs of manufacture include all production-related costs on the basis of normal utilization levels. They include individual unit costs that can be directly allocated to projects, plus fixed and variable overheads. Borrowing costs are not capitalized in costs of acquisition / manufacture. No unscheduled write-downs on inventories were required during the reporting period.

Research and development costs

Research and development costs are expensed in the income statement as they are incurred.

The creation of and subsequent improvements to software involve closely linked, highly interwoven research and development phases. Accordingly, it is not possible to strictly separate expenses incurred for research from those incurred for development, and the criteria for separately reporting development costs laid out in IAS 38, Section 41, in conjunction with 42, cannot be met.

Sales, marketing and distribution

These include personnel and materials costs, write-downs, and advertising expenses.

Administrative costs

These include personnel and materials costs, and applicable depreciation and amortization.

Earnings per share

Earnings per share are calculated by dividing net income allocable to shareholders for the period by the weighted number of shares outstanding during the period. Software AG only has common stock.

Notes on the first-time application of IAS / IFRS

Accounting and valuation

Pursuant to IFRS 1, International Accounting Standards (IAS)/International Financial Reporting Standards (IFRS) are applied retrospectively upon their initial adoption. Figures from previous periods are adjusted accordingly to allow effective comparison.

New standards published as part of the International Accounting Standards Board Improvement Project in December 2003, whose application is not compulsory until January 1, 2005, have not been employed for these financial statements.

Of the new standards published during the previous quarter, whose application is not compulsory until January 1, 2005, or later, Software AG chose to apply the provisions of IFRS 3 relating to the impairment testing of goodwill to these financial statements.

Application of IAS/IFRS involves the following material deviations from the accounting and valuation principles set out in German law:

- Goodwill is no longer amortized, but subject to regular impairment testing
- Securities available for sale are valued at their fair market value, even where this exceeds the cost of acquisition. Gains and losses are included in other comprehensive income under equity, but are not recognized in net profit or loss.
- Derivative instruments are valued at their fair market value, even where this exceeds the cost of acquisition. Both gains and losses are recognized in net profit or loss for the period.
- Revenues are recognized according to the percentage-of-completion method.
- Property is depreciated according to its useful economic life, and not according to tax scales.
- Finance leases, according to the more restrictive IFRS provisions, are posted as assets and leasing liabilities.
- Provisions are only formed where obligations to third parties exist, and the probability that these obligations will be fulfilled is at least 50 percent. Medium and long-term provisions are stated at cash values. Provisions are not formed for failure to perform maintenance or for other expenses.
- Provisions for pensions are formed according to the projected unit credit method.
- Deferred taxes are calculated according to the balance-sheet liability method. Deferred taxes on loss carryforwards are formed where the Company expects to be able to make use of these loss carryforwards.
- Cash positions in foreign currencies are valued at the balance-sheet-date rate and recognized in net profit or loss for the period. However, translation differences from long-term intra-Group cash positions are posted in other comprehensive income under equity, but are not recognized in net profit or loss for the period.

Balance-sheet reconciliation on January 1, 2003 (HGB to IFRS)

€ thousands	Note	HGB Jan 1, 2003	Income Statement related changes	Reclassifications	IFRS Jan 1, 2003
Assets					
A. Cash and cash equivalents					
Cash in hand and bank balances		75,423	0	0	75,423
Securities		0	0	0	0
		75,423	**0**	**0**	**75,423**
B. Current assets					
Inventories	(1)	4,628	0	– 3,873	755
Trade receivables	(1)	122,160	616	3,873	126,649
Other receivables and other assets	(2)	10,395	1,048	0	11,443
		137,183	**1,664**	**0**	**138,847**
C. Fixed assets					
Intangible assets		1,551	0	0	1,551
Goodwill		176,591	0	0	176,591
Property, plant and equipment	(3)	37,000	15,776	0	52,776
Financial assets	(4)	5,937	9,909	0	15,846
		221,079	**25,685**	**0**	**246,764**
D. Deferred taxes	(5)	**188**	**38,060**	**0**	**38,248**
E. Deferred expenses		**6,947**	**0**	**0**	**6,947**
Total assets		**440,820**	**65,409**	**0**	**506,229**
Equity and liabilities					
A. Current liabilities					
Current financial liabilities	(6)	3,395	3,016	0	6,411
Trade payables	(7)	13,992	0	8,474	22,466
Other current liabilities	(7)	18,046	0	12,934	30,980
Current provisions	(8)	97,950	– 16,110	– 28,413	53,427
		133,383	**– 13,094**	**– 7,005**	**113,284**
B. Non-current liabilities					
Non-current financial liabilities	(6)	0	8,395	0	8,395
Trade payables		0	0	0	0
Other non-current liabilities	(7)	448	0	3,393	3,841
Provisions for pensions	(9)	8,781	10,653	0	19,434
Non-current provisions	(7)	0	0	3,612	3,612
		9,229	**19,048**	**7,005**	**35,282**
C. Deferred taxes	(5)	**2,012**	**14,994**	**0**	**17,006**
D. Deferred income		**81,728**	**0**	**0**	**81,728**
E. Equity					
Share capital		81,800	0	0	81,800
Capital reserves		132	0	0	132
Retained earnings		132,959	34,552	– 18,153	149,358
Consolidated income		0	0	0	0
Currency translation differences		– 423	0	423	0
Other comprehensive income	(10)	0	9,909	17,730	27,639
		214,468	**44,461**	**0**	**258,929**
Total equity and liabilities		**440,820**	**65,409**	**0**	**506,229**

Notes on the balance-sheet reconciliation from HGB to IFRS (January 1, 2003):

(1) Work in progress as defined by HGB was recognized and posted as non-invoiced receivables according to the percentage of completion method (including margin).

(2) Derivative instruments are valued at fair market value, even where this exceeds the cost of acquisition.

(3) Depreciation of property was adjusted to take account of expected useful economic lives. Assets from capital leases were capitalized.

(4) This change is a result of the fair-market valuation of securities. The change is included in other comprehensive income under equity, but not recognized in net profit or loss for the period.

(5) Deferred tax assets are primarily formed for loss carryforwards and provisions. Deferred tax liabilities are primarily formed for deferred expense and property, plant and equipment.

(6) Long and short-term financial liabilities include capitalized liabilities from capital leases.

(7) Certain provisions under HGB were reclassified as short or long-term liabilities to comply with IFRS.

(8) The adjustment of provisions (recognized in net profit or loss) primarily comprises dis-solved provisions for expenses (maintenance, guarantees) and provisions where the probability of the obligation having to be settled is less than 50 percent (legal costs, contingent losses, general risks). Reclassifications comprise provisions which, according to IFRS, are to be posted as liabilities. See also note (7).

(9) The increase in pension provisions is primarily a result of the requirement under IFRS to include indirect pension obligations at SAG UK. These were not previously included, in accordance with the option granted by Article 28 of the Introductory Act to the German Commercial Code (EGHGB).

(10) Other comprehensive income includes unrealized gains from the fair-market valuation of securities and differences from the translation of long-term intra-Group cash positions in foreign currencies (i.e. not in euros).

Reconciliation of equity on January 1, 2003 (HGB to IFRS)

€ thousands	Note	
Equity in accordance with HGB as at Jan 1, 2003		**214,468**
Revenue recognized according to percentage of completion	(1)	616
Depreciation of buildings	(3)	8,884
Finance leases	(3), (6)	– 4,519
Market value of securities and financial derivatives	(2), (4)	10,957
Deferred tax assets	(5)	38,060
Adjustments to other provisions	(8)	16,110
Adjustments to pension provisions	(9)	– 10,653
Deferred tax liabilities	(5)	– 14,994
Equity in accordance with IFRS as at Jan 1, 2003		**258,929**

Balance-sheet reconciliation on June 30, 2003 (HGB to IFRS)

€ thousands	Note	HGB Jan 1, 2003	Income Statement related changes	Reclassifications	IFRS Jan 1, 2003
Assets					
A. Cash and cash equivalents					
Cash in hand and bank balances		46,762	0	0	46,762
Securities		28,300	0	0	28,300
		75,062	**0**	**0**	**75,062**
B. Current assets					
Inventories	(1)	5,727	0	– 5,335	392
Trade receivables	(1)	119,242	397	5,335	124,974
Other receivables and other assets	(4)	12,270	651	0	12,921
		137,239	**1,048**	**0**	**138,287**
C. Fixed assets					
Intangible assets		1,210	0	0	1,210
Goodwill	(2)	165,665	10,926	0	176,591
Property, plant and equipment	(3)	35,391	14,841	0	50,232
Financial assets	(4)	6,769	14,106	0	20,875
		209,035	**39,873**	**0**	**248,908**
D. Deferred taxes	(5)	**28,192**	**21,668**	**0**	**49,860**
E. Deferred expenses		**8,208**	**0**	**0**	**8,208**
Total assets		457,736	62,589	0	520,325
Equity and liabilities					
A. Current liabilities					
Current financial liabilities	(6)	1,804	3,016	0	4,820
Trade payables	(7)	14,098	8	7,776	21,882
Other current liabilities	(7)	17,908	0	10,354	28,262
Current provisions	(8)	106,295	– 7,372	– 25,771	73,152
		140,105	**– 4,348**	**– 7,641**	**128,116**
B. Non-current liabilities					
Non-current financial liabilities	(6)	0	5,947	0	5,947
Trade payables		0	0	0	0
Other non-current liabilities	(7)	140	0	3,393	3,533
Provisions for pensions	(9)	8,348	10,653	0	19,001
Non-current provisions	(7)	0	0	4,248	4,248
		8,488	**16,600**	**7,641**	**32,729**
C. Deferred taxes	(5)	**2,012**	**13,930**	**0**	**15,942**
D. Deferred income		**87,383**	**0**	**0**	**87,383**
E. Equity					
Share capital		81,800	0	0	81,800
Capital reserves		132	0	0	132
Retained earnings		146,017	21,494	– 18,153	149,358
Consolidated income		– 7,378	806	3,011	– 3,561
Currency translation differences	(10)	– 823	0	– 15,401	– 16,224
Other comprehensive income	(11)	0	14,107	30,543	44,650
		219,748	**36,407**	**0**	**256,155**
Total equity and liabilities		457,736	62,589	0	520,325

Notes on the balance-sheet reconciliation from HGB to IFRS (June 30, 2003):

(1) Work in progress as defined by HGB was recognized and posted as non-invoiced receivables according to the percentage of completion method (including margin).

(2) Scheduled amortization of goodwill pursuant to HGB was reversed as, according to IFRS 1, where IFRS 3 is voluntarily applied to 2004, it should also be applied to 2003. Accordingly, 2003 goodwill was not amortized according to the straight-line method.

(3) Depreciation of property was adjusted to take account of expected useful economic lives. Assets from capital leases were capitalized.

(4) This change is a result of the fair-market valuation of securities. The change is included in other comprehensive income under equity, but not recognized in net profit or loss for the period. Derivative instruments are valued at fair market value, even where this exceeds the cost of acquisition.

(5) Deferred tax assets are primarily formed for loss carryforwards and provisions. Deferred tax liabilities are primarily formed for deferred expense and property, plant and equipment.

(6) Long and short-term financial liabilities include capitalized liabilities from capital leases.

(7) Certain provisions under HGB were reclassified as short or long-term liabilities to comply with IFRS.

(8) The adjustment of provisions (recognized in net profit or loss) primarily comprises dissolved provisions for expenses (maintenance, guarantees) and provisions where the probability of the obligation having to be settled is less than 50 percent (legal costs, contingent losses, general risks). Reclassifications comprise provisions which, according to IFRS, are to be posted as liabilities. See also note (7).

(9) The increase in pension provisions is primarily a result of the requirement under IFRS to include indirect pension obligations at SAG UK. These were not previously included, in accordance with the option granted by Article 28 of the Introductory Act to the German Commercial Code (EGHGB).

(10) The change in currency translation differences arose primarily from the fact that, as permitted by IFRS 1.22, the HGB figure was reset to zero for the IFRS statements on January 1, 2003. From this date, only IFRS currency translation adjustments were recorded.

(11) Other comprehensive income includes unrealized gains from the fair-market valuation of securities and differences from the translation of long-term intra-Group cash positions in foreign currencies (i.e. not in euros).

Reconciliation of equity on June 30, 2003 (HGB to IFRS)		
€ thousands	**Note**	
Equity in accordance with HGB as at June 30, 2003		**219,748**
Revenue recognized according to percentage of completion	(1)	397
Adjustment to goodwill amortization	(2)	10,926
Depreciation of buildings	(3)	8,902
Finance leases	(3), (6)	– 3,024
Fair market valuation	(2), (4)	14,757
Deferred tax assets	(5)	21,668
Adjustments to other accruals	(8)	7,372
Adjustments to pension accrual	(9)	– 10,653
Deferred tax liabilities	(5)	– 13,930
Other		– 8
Equity in accordance with IFRS as of June 30, 2003		**256,155**

Reconciliation of net income on June 30, 2003 (HGB to IFRS)		
€ thousands	**Note**	
Net loss in accordance with HGB at June 30, 2003		**– 7,378**
Revenue recognized according to percentage of completion	(1)	– 219
Adjustment to goodwill amortization	(2)	10,926
Depreciation of buildings	(3)	18
Finance leases	(3), (6)	1,495
Fair market valuation	(4)	– 398
Deferred tax assets	(5)	– 3,334
Adjustments to other accruals	(8)	– 8,738
Adjustments to pension accrual	(9)	0
Deferred tax liabilities	(5)	1,064
Other		3,003
Net loss in accordance with IFRS as of June 30, 2003		**– 3,561**

Seasonal effects

The following table shows a breakdown of revenues and pre-tax profits (adjusted for restructuring costs) over the four quarters of 2003:

€ thousands	Q1 2003	Q2 2003	Q3 2003	Q4 2003	2003
Revenues	103,140	103,136	98,680	115,086	420,042
% of revenues at year-end	24.6 %	24.5 %	23.5 %	27.4 %	100.0 %
Pre-tax profit	8,728	18,241	16,426	18,420	61,815
% of net income at year-end	14.1 %	29.5 %	26.6 %	29.8 %	100.0 %

Revenues developed similarly to previous years – largely in line with the sales cycle. Against this background, Software AG expects a similar pattern for fiscal 2004. Restructuring activities in the second half of 2003 produced significant cost reductions, which contributed to an increase in pre-tax profit.

Contingent liabilities

At June 30, 2004, no provisions had been formed for the following contingent liabilities (stated at face values), for which it was deemed improbable that the Company would have to fulfill obligations:

€ thousands	
Bank guarantees	5,333
Other	1,144
	6,477

Share-option plans

The Software AG Group runs various share-option plans for Executive Board members, senior executives, and other employees which are not expensed in the consolidated financial statements.

First share-option plan: At June 30, 2004, Executive Board members held 145,846 subscription rights to shares in the Company, and senior executives 69,069 – unchanged over June 30, 2003. These rights cannot be exercised before June 30, 2004. Options have a term of seven years from the date on which they are granted, and may only be exercised, after an initial vesting period of 24 months as of the Software AG IPO, on four occasions during each fiscal year: after the publication of quarterly, biannual, and annual earnings figures.

The subscription price per share is the issue price less a 20 percent mark-down, but no less than € 28.12. As Company stock was floated at € 30, this minimum applied.

- Holders of subscription rights must fulfill the following three conditions before they may exercise their conversion rights:Consolidated earnings from ordinary activities (according to HGB) must have increased by 30 percent between 1997 and 1999.

This condition was fulfilled between 1997 and 1999.

- Consolidated earnings from ordinary activities (according to HGB) must total at least 10 percent of revenues for the fiscal year prior to conversion.
- The share price must exceed the minimum conversion price.

Second share-option plan: At June 30, 2004, Executive Board members held 142,250 subscription rights to shares in the Company, and senior executives 434,750. These rights cannot be exercised before June 30, 2004. During the second quarter, 90,000 of the options held by Executive Board members were withdrawn, and 125,400 new options were issued to senior executives. No rights could be exercised during the period.

The subscription price is the average XETRA closing price over the previous five trading days on the Frankfurt Stock Exchange before the date of conversion.

Holders of subscription rights must fulfill the following two conditions before they may exercise their conversion rights:

- Consolidated revenues must have increased for the fiscal year prior to conversion by at least 10 percent in comparison to the previous year.
- Consolidated earnings from ordinary activities (according to HGB) must total at least 10 percent of revenues for the year prior to conversion.

The terms, blocking period, and conversion dates correspond to those of the first share-option plan.

Other financial obligations

Software AG has entered into rental and leasing contracts for buildings, real estate, IT and PBX systems, and vehicles. Obligations from these contracts (where the contracts are still within their minimum durations) until the end of fiscal 2004 total € 8,829 thousand. Obligations until the end of fiscal 2008 total € 38,535. The leasing contracts are operating leases as defined by IAS 17.

Employees

The Software AG workforce averaged 2,435 during the second quarter of 2004, and totaled 2,467 on June 30, 2004.

Executive Board and Supervisory Board

On June 30, 2003, the composition of the Supervisory Board had changed as follows in comparison to December 31, 2003:

By resolution of the annual shareholders' meeting on April 30, 2004, Dr. Andreas Bereczky, Director of Production at German public-service TV broadcaster ZDF, Mainz, was elected to succeed Dr. Peter Lex on the Software AG Supervisory Board.

Karl-Heinz Hageni (employee representative) left the Supervisory Board on April 30, 2004. On June 25, 2004, employees elected Monika Neumann, chair of the General Works' Council, Schliersee, as Mr. Hageni's replacement.

The composition of the Executive Board at June 30, 2004, was unchanged in comparison to December 31, 2003.

Events subsequent to the balance-sheet date

Restructuring for international growth

August 2004: Software AG streamlined its international structure as part of a drive to encourage growth across both new and established markets. The Company's activities will now be organized into three regions, previously four, represented on the Executive Board by a Regional Manager.

- North America/Northern Europe includes the USA, Canada, and the United Kingdom. This region is led by Mark Edwards, and also covers activities in Scandinavia and South Africa.

- The South region spans southern Europe, south and central America, and is the responsibility of Christian Barrios Marchant.

- Central/Asia is managed by Andreas Zeitler, and incorporates the German-speaking countries, Eastern Europe, the Mid-east, Asia, and Australia. This will enable the company to service high growth markets more efficiently.

This strategic reorganization will enhance integration across the Software AG Group by mirroring the cultural and language links between countries in the company's regional structure. This will allow us to better exploit traditional economic ties, leverage resources and skills, improve cooperation, and form valuable new partnerships.

New R&D structure

July 2004: Software AG reorganized its research and development activities. The Research and Development integration team has joined the XML Business Integration business line, and the Enterprise Transaction Systems development team is now part of the Enterprise Transaction Systems business line. This means that, as with product management and marketing, all R&D activities now take place within the framework of the two strategic business lines. This move is intended to ensure all Software AG development work is focused on market requirements, taking account of the specific characteristics of the Enterprise Transaction Systems and XML Business Integration segments. In this way, we can rapidly recognize and respond to changing needs, establishing the basis for practical innovation. This will strengthen skills and flexibility at both business lines. It also reinforces Software AG's place as a first mover in the fast-paced XML market.

Changes to Software AG management

The managers of the two new R&D areas report directly to the CEO. Chief Technology Officer Dr. Peter Mossack has left the Company. Gary Voight, Executive Board member responsible for the Americas region, has also departed to join a US software house as CEO. The Software AG Executive Board now has five members. Haskell Mayo, previously Senior Vice President, Marketing and Sales, in the USA, has been appointed President, North American Operations.

Financial Calendar

September 30, 2004	HVB German Investment Conference, München
October 28, 2004	Q3 earnings figures
November 23/24, 2004	German Equity Forum, Deutsche Börse AG, Frankfurt
May 13, 2005	Annual Shareholders' Meeting

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