

Report of the Executive Board on agenda item 9

The proposed authorization to issue bonds with nominal amount of up to EUR 50,000,000 and to create the associated Contingent Capital 2020 II in the amount of up to EUR 8,116,883.00 under agenda item 9 of the invitation to the virtual ordinary Annual General Meeting to be held on 25 September 2020 is intended to expand the opportunities, explained in greater detail below, available to KPS AG to finance its activities and to enable the Executive Board with the approval of the Supervisory Board to secure timely and flexible financing in the interest of the company particularly in the event of favorable capital market conditions. An appropriate capital structure is a key foundation for the development of the company. Issuing conversion and option bonds enables the company to make use of attractive financing possibilities according to the market situation in order to provide the company with capital at lower current interest rates. By issuing participation rights with conversion and/or option rights, the interest payable can also be based e.g. on a future dividend of the company. The conversion and option premiums achieved benefit the company in the event of an issue. Experience shows that some financing instruments can only be placed by granting option or conversion rights.

The shareholders are entitled to the statutory subscription right to bonds which are associated with option or conversion rights or option or conversion obligations or a substitution right of the company (Articles 221 Section 4, 186 Section 1 Stock Corporation Act (AktG)). Insofar as shareholders are not allowed to subscribe directly to bonds, the Executive Board can utilize the opportunity to issue bonds to a bank or to an equivalent company under statutory regulations and the resolution proposal, or to a group or a consortium of banks and/or companies with the obligation to offer the shareholders the bonds in accordance with the participation right (indirect subscription right).

However, the Executive Board is to be authorized to exclude the subscription right in certain cases.

1. Exclusion of subscription rights from fractional amounts

The exclusion of the subscription right for fractional amounts permits the utilization of the requested authorization through rounded amounts and facilitates definition of a practical and technical feasible subscription ratio. This makes it easier to process a bond issue. The value of the fractional amounts is generally minimal for each individual shareholder, and the potential dilution effect can therefore also be regarded as low. In view of the minimal dilution effects associated with the exclusion of subscription right for fractional amounts and after carefully considering all the circumstances, the Executive Board has come to the conclusion

that exclusion of the subscription right within the circumscribed limits is reasonable and in the interest of the company.

2. Exclusion of subscription right for purposes of protection against dilution

The Executive Board is further to be authorized to exclude the subscription right to the extent that it is necessary in order to grant the owners of option or conversion rights or option or conversion obligations arising from bonds, which were previously issued by the company or a group company or are still to be issued, a subscription right in the volume that would be attributable to them as a shareholder after exercising the option or conversion rights or fulfilling the option or conversion obligations.

Providing bonds with this kind of protection against dilution is in line with the standard market practice based on the expectations of the capital market. The exclusion of the subscription right in favor of the owners of these financial instruments has the advantage that the option or conversion price for bonds does not have to be reduced and this consequently permits a higher inflow of funds. A careful consideration of all the current circumstances indicates that the exclusion of subscription rights within the circumscribed limits is reasonable and in the interest of the company.

3. Simplified exclusion of subscription rights

The Executive Board with the approval of the Supervisory Board is furthermore authorized to exclude the subscription right of shareholders when the issue of the bonds against a cash consideration is carried out at a price which does not fall significantly short of the market value of these bonds. As a result, the company is able to make timely and flexible use of favorable market situations and by defining conditions close to the market achieve better conditions when establishing interest rate, option or conversion price, and issue price for bonds. Definition of conditions close to the market and smooth placement with third parties would not be possible if the subscription right were observed. Although Article 186 Section 2 Stock Corporation Act (AktG) permits publication of the subscription price (and hence the conditions of these bonds) up to the third-last day of the subscription period, the frequently observed volatility in stock markets means that there would be a market risk over a period of several days, which would lead to security discounts in determining the bond conditions and would consequently lead to conditions that were not close to the market. In addition, the existence of a subscription right could jeopardize the successful placement with third parties as a result of uncertainty surrounding the exercise of a granted subscription right

(subscription behavior) or be associated with additional expenses. Ultimately, the company is unable to respond rapidly to favorable or unfavorable market conditions when granting a subscription right owing to the length of the statutory subscription period of at least 14 days, but it is exposed to declining share prices during the subscription period which can lead to unfavorable equity financing for the company.

Pursuant to Article 221 Section 4 sentence 2 Stock Corporation Act (AktG), determination of Article 186 Section 3 sentence 4 Stock Corporation Act (AktG) applies mutatis mutandis for the exclusion of the subscription right. The limit of 10 % of the capital stock defined there for exclusions of subscription rights must be complied with in accordance with the content of the resolution. The maximum volume of the contingent capital which in this case may be made available for securing the option or conversion rights or fulfilling the option or conversion obligations, must not exceed 10 % of the capital stock at the time when the authorization for the exclusion of subscription rights comes into effect pursuant to Article 186 Section 3 sentence 4 Stock Corporation Act (AktG). An appropriate definition in the authorization resolution also ensures that if there is a decrease in the capital the 10 % limit is not exceeded because the authorization for the exclusion of subscription rights must explicitly not exceed 10 % of the capital stock, and specifically neither at the time of coming into force nor – if this value is less – at the time when this authorization is exercised. This includes own shares which are sold with exclusion of the subscription right pursuant to Article 186 Section 3 sentence 4 Stock Corporation Act (AktG), and those shares which are issued from authorized capital with exclusion of the subscription right pursuant to Article 186 Section 3 sentence 4 Stock Corporation Act (AktG) if the sale or issue is carried out during the period of authorization before a bond issue free of subscription rights pursuant to Article 186 Section 3 sentence 4 Stock Corporation Act (AktG), set off and thereby reduced correspondingly by this amount.

Article 186 Section 3 sentence 4 Stock Corporation Act (AktG) further stipulates that the issue amount must not fall significantly short of the stock market price. This is intended to ensure that there is no significant dilution of the financial value of the shares. Whether a dilution effect of this nature occurs when bonds are issued free of subscription rights can be determined by calculating the hypothetical market value of the bonds in accordance with acknowledged financial mathematical methods and compared with the bond issue amount. If in accordance with a mandatory audit this issue amount is not significantly below the hypothetical stock market price at the time when the bonds were issued, an exclusion of subscription right is permissible on account of the insignificant deduction pursuant to the intent and purpose of the regulation of Article 186 Section 3 sentence 4 Stock Corporation

Act (AktG). The resolution therefore states that prior to issue of the bonds and following careful consideration the Executive Board must be of the opinion that the issue amount earmarked for the bonds will not lead to any notable dilution in the value of the shares since the issue amount for the bonds is not significantly below their hypothetical market value determined in accordance with generally acknowledged financial mathematical methods. This means that the calculated market value of a subscription right would fall to almost zero such that the shareholders would not suffer any notable economic disadvantage as a result of the exclusion of subscription rights. This process ensures that a significant dilution of the value of the shares does not occur as a result of the exclusion of subscription rights.

Furthermore, the shareholders have the option of maintaining their share of the capital stock in the company even after exercising option or conversion rights or the occurrence of option or conversion obligations at any time by purchasing shares on the stock market. On the other hand, the authorization for the exclusion of subscription rights enables the company to define conditions close to the market and provides the greatest possible security in relation to placement with third parties and use of favorable market situations at short notice.

4. Participation rights and profit-participating bonds

Insofar as participation rights or profit-participating bonds are to be issued without option or conversion rights or option or conversion obligations, the Executive Board is authorized with the approval of the Supervisory Board to completely exclude the subscription right of shareholders if these participation rights or profit-participating bonds have obligatory characteristics, i.e. convey no membership rights in the company, do not grant participation in liquidation proceeds and the interest payable is not calculated on the basis of the level of the annual earnings after income taxes, the net profit or the dividend. Furthermore, it is necessary for the interest payable and the issue amount for the participation rights or the profit-participating bonds to correspond to the current market conditions on the date when the issue takes place. If these prerequisites are fulfilled, no disadvantages are incurred by the shareholders as a result of the exclusion of the subscription right since the participation rights or the profit-participating bonds are not based on any membership rights and do not grant any participation in liquidation proceeds or in the profit of the company.

After carefully considering all the circumstances, the Executive Board has come to the conclusion that exclusion of the subscription right in the cases referred to is appropriate, necessary, objectively justified and reasonable for the reasons presented, also taking into account the corresponding dilution effects to the detriment of shareholders.

When reaching its decision, the Executive Board will carefully consider in each case when it should make use of the authorization to issue bonds with exclusion of the subscription rights of shareholders. Only in this case will the measures be adopted if, in the opinion of the Executive Board and the Supervisory Board, this is in the interest of the company and hence also its shareholders.

The Executive Board will in each case report to the next Annual General Meeting about the issue of bonds and about the utilization of the Contingent Capital 2020 II.

Unterföhring, September 2020

Leonardo Musso
Sole Member of the Board of Management