RISK REPORT

GENERAL PRINCIPLES

KUKA Group conducts business around the globe, which exposes the company to numerous potential risks. The goal of entrepreneurial management is to minimize risks and take advantage of opportunities, in order to systematically and sustainably improve shareholder value and achieve the target objectives.

Risk management

KUKA continuously and systematically identifies external and internal risks in all business units and subsidiaries and evaluates them consistently throughout the Group with respect to their potential level of damage and likelihood of the events occurring. The precise risks are categorized into worst-, medium- and best-case scenarios and appropriate accruals or revaluations are formed on the balance sheet. Once per quarter, a steering committee analyzes the identified risks. The responsible persons evaluate the plausibility and define possible management alternatives. A risk summary is subsequently generated, which includes identification of the top ten risks and a summary of the overall risk situation. The Robotics and Systems divisions' top ten risks, and Group risks derived from them, are updated monthly and are a fixed agenda item of the monthly reporting process. In addition, the risk report is on the agenda during Executive Board meetings, and also especially during Supervisory Board Audit Committee Meetings.

The managers of the divisions and subsidiaries are directly responsible for the early identification, control and communication of risks. Risk coordinators in the central and decentralized business units ensure that the reporting process is uniform and consistent with the defined reporting channels and reporting thresholds and are in line with the size of the company. Companies are always obligated to provide internal ad hoc reports for risks that exceed certain reporting thresholds. KUKA Aktiengesellschaft's risk management system is coordinated by a head-office administrator and is an integral part of the overall budgeting, control and reporting process.

The Group's risk management system makes it possible for executive management to identify material risks at an early stage and take appropriate steps to counter them as well as monitor the mitigating measures. Regular audits of the risk management process by the internal audit department ensure efficiency and continuous improvement. In addition, the external auditors check that the early risk identification procedure is suitable for identifying risks at an early stage that could threaten the existence of the company.

MARKET AND BUSINESS RISKS

KUKA is exposed to the cyclic investment behaviour of its regular customers in the various market subsectors, particularly the automotive sector with its oligopolistic structures and ongoing price pressure. The industry represents a major share of the Systems and Robotics divisions' business volumes. It is further exposed to country risks, such as patent and brand protection in Asia, exchange rate fluctuations, financial and technical risks and the risk of substantial price increases of key raw materials.

In 2009, KUKA was particularly hard hit by the effects of the international financial crisis and the worldwide sales slump in the automotive industry, as well as the mechanical and plant engineering sector. Orders received dropped 29.4 percent and sales 28.7 percent compared to 2008. As a result of these developments, the company was unable to comply with certain financial covenants in fiscal 2009. Please refer also to the discussion on fiscal risks.

Furthermore, most carmakers' financial situation deteriorated significantly in 2009, particularly that of the major American carmakers. As a result, Chrysler and GM were forced to file for Chapter 11 bankruptcy protection. Thanks to systematic management of the risks associated with these companies, Chrysler's and GM's bankruptcy proceedings did not have a negative impact. After Chrysler and GM successfully completed their Chapter 11 bankruptcy proceedings, all original contracts, including KUKA Toledo Production Operations' (KTPO) pay-on-production contract, were reinstated.

Economic risks that could also affect business performance after 2009 include:

- tightened credit by banks
- euro appreciation and thus a further negative impact on exports in the euro zone
- expiry of the government incentive programs
- further increase in the number of Asian competitors resulting in increased cost pressure
- continuation of the financial crisis

PERFORMANCE RISKS

KUKA Robotics

The key challenges for the product portfolio are the continuing cost sensitivity of customers around the world and their demands for continuous product innovation. This applies particularly to the automotive industry and its subsuppliers. The result is permanent price pressure and potentially longer life cycles for the robots used in the currently served markets.

KUKA Robotics counters such trends by continually developing new products and applications that offer customers in existing markets quantifiable financial advantages driven by very short paybacks. In addition, the division targets and penetrates new markets; for example, new applications in the health care sector and other consumer related areas. In fiscal 2009, KUKA Group invested € 35.6 million in research and development, the majority of which was for robotics.

A key component of the corporate strategy is to develop new markets outside the automotive industry by expanding the customer base into general industry. In fiscal 2009, total orders from such customers accounted for over 40 percent of the Robotics division's orders received. In addition, the company continues to press ahead with efforts to expand its business in the United States and Asia.

Exchange-rate advantages benefit KUKA competitors' business in some areas. Increased distribution of value added across various local currencies will make the profitability of the company less susceptible to exchange-rate fluctuations.

KUKA Systems

In 2009, KUKA felt the effects of the international financial market crisis on orders received, as well as on customers' capital spending and payment behavior. For example, projects planned for 2009 were postponed. In addition, carmakers' cost reduction programs have a positive impact on the business on the one hand because of greater demands for better efficiency and more flexible production lines. On the other hand, they impact negatively because of the reduced capital spending overall. The long duration of the project management phase and the infrequency of the orders received, as well as price and competitive pressures, can expose the company to sales and profit risks. Exposure of our American subsidiaries in particular to the risk associated with the major US carmakers is reduced through a strict project and receivables management program. Due to the project nature of the business, there are also the additional risks of cost estimation errors and contractual penalties as well as postponements. These are continuously monitored and accrued for.

We further mitigate risk by diversifying regionally, spreading our business activities across Europe, North America and increasingly Asia. Asia in particular is seen as an area of further potential, since the automotive industry wants to participate in Asia's economic growth and is therefore building and expanding local manufacturing facilities. The increasing model variety in the automotive industry has a positive effect on orders received, since it results in rising demand for flexible production lines. This enables systems integrators and subsuppliers to participate in new business opportunities. US carmakers in particular will have to spend money to further adjust their manufacturing systems in order to remain competitive by catering to the demand for smaller, more fuel-efficient cars.

Pay-on-production contracts such as the one entered into by KUKA Toledo Productions Operations (KTPO) offer additional opportunities and risks. Compared to all other American cars, the Jeep Wrangler brand is demonstrating above-average growth opportunities, in which KUKA participated again in 2009. There are risks associated with the stronger dependencies on car sales and production volumes in the American car market.

After conducting a fundamental general industry market analysis, KUKA Systems is now to exploit long-term business potential also outside the automotive industry. Current examples are the aircraft and solar industry, as well as the rail vehicle manufacturing sector, where the first orders have been received.

CORPORATE STRATEGY RISKS

The goal of KUKA's divisions is to be among the technology and market leaders in their target markets. Consistently enhancing their technologies through coordinated innovation programs is therefore of primary importance. A key task is to identify the opportunities and risks of technical innovations in a timely manner and evaluate them with respect to feasibility. The company mitigates the impact of incorrect market assessment by conducting regular market and competitor analyses, some of which are decentralized. This is supported by application-oriented developments, partnerships with systems integrators and alliances; for example, the cooperative research being done with the German Aerospace Center (DLR) in Wessling near Munich, with RWTH Aachen and with the university clinic in Aachen.

Using effective quality assurance systems in combination with regular certification programs helps convince purchasers that we offer customer-oriented products and solutions and strengthens KUKA's companies' positions in their target markets.

The corporate strategy is managed by a central KUKA AG department and is regularly reviewed and coordinated with the divisions. Crossover technologies and concepts are developed at the joint Innovation Center. Uniform procedures and processes generate synergies that help the company meet the demands of the market for innovative products and solutions.

Centralized generic, administrative and support functions such as accounting and payroll strengthen cooperation within the Group, lead to uniform processes that meet compliance requirements, create synergies and therefore optimize costs.

PERSONNEL RISKS

KUKA relies on qualified specialists and managers to achieve its goals. In today's very competitive marketplace, it is therefore a constant challenge to attract these human resources to the Group and ensure they identify with the company over the long term. There is an increasing demand for well educated and motivated workers, especially in the world's growth markets. In Germany, there is also evidence of an increasing shortage of qualified personnel, particularly in the technical area. This requires that the company have appropriate in-house training programs and permanently stay in tune with the job market and job seekers. KUKA works closely with local and national universities and research institutes, such as the University of Augsburg, RWTH Aachen and the German Aerospace Center (DLR). The topic is made more acute by the recognizable demographic shift. Already now, the number of candidates and the quality of the applicants in some areas, such as future apprentices, is steadily declining.

Centralized and decentralized training and continuing education programs for employees at all levels ensure that the Group's people have the indispensable expert skills they require. The in-house and international trainee program offers recruits the opportunity to get to know various business areas and foreign companies. The 193 apprentices to be trained by KUKA Group by year-end will be quickly integrated into the company and subsequently offered a permanent position if possible.

A key task is to prepare KUKA Group for the future with regard to the demographic shift. Entrepreneurial thinking and management styles are also encouraged by offering managers attractive remuneration packages. This is supported by an employee share program.

INFORMATION SYSTEMS RISKS

IT is a strategic tool used to achieve cost-related business goals. Standardization and integration are key prerequisites for generating a strategic competitive advantage based on IT. Over the course of 2009, considerable progress was made in harmonizing the accounting IT systems and aligning them with the general strategic direction of the Group. The IT systems used also align with KUKA Group's security and uptime requirements.

By regularly reviewing and optimizing the IT systems in use, as well as the relative guidelines and organizational structures associated with effective IT security and IT service continuity management, the company ensures that the risks posed by the increasing potential threats from external sources and the dependencies resulting from the increased digitization of business processes are minimized. IT is also permanently integrated into KUKA Group's risk management process. An annual IT audit and spot checks regarding adherence to legal requirements are conducted by external auditors.

FINANCIAL RISKS

One of KUKA AG's primary tasks is to coordinate and control the Group's financing requirements and ensure that KUKA remains financially independent. With this goal in mind, KUKA Group optimizes the Group's financing and limits its financial risks. The standardized, group-wide treasury reporting system implemented in 2007 was further enhanced for this purpose. In addition, the Group's overall liquidity risk is reduced by closely monitoring the Group's companies and their control of payment flows.

Due to the difficult economic situation in fiscal 2009, the company was unable to comply with all clauses stipulated in the syndicated loan agreement (debt ratio). As a result, KUKA Group had to renegotiate its financing. Agreement on extending the Syndicated Senior Facilities Agreement totaling € 336 million (of which € 146 million is a cash credit line and € 190 million a credit line for LCs) was reached in March 2010, after the December 31, 2009 closing date. It includes various constraints and conditions, such as successfully implementing KUKA Group's restructuring, which also comprises further increasing equity via share issues or subordinated debts, refinancing the existing convertible bond and honoring various financial and non-financial covenants. Accordingly, no dividends will be paid to shareholders during the term of the Syndicated Senior Facilities Agreement.

Systematic implementation of the restructuring measures according to plan is thus decisive for the company's future solvency and securing the continuation of its business activities. Key covenants relate to minimum earnings before interest, taxes and depreciation (EBITDA), the degree of indebtedness and equity. As part of this agreement with the consortium banking partners, KUKA AG is obligated to ensure that it adds € 23 million either as equity or subordinated loan by the end of June 2010. Concerning this, the company has a guarantee in the amount of € 15 million. A provision of the credit line agreements with the banks, is that these will only be available in full in future if the corresponding cash injection has taken place. The agreed contractual term of the Syndicated Senior Facilities Agreement and the ABS program (regular sale of receivables) totaling up to € 25 million extends to March 31, 2012. Bilateral credit line agreements with banks and credit insurance companies supplement the Group's financing portfolio.

The € 69 million convertible bond issued on May 9, 2006 is due to be repaid on November 9, 2011. At the present time, the Executive Board expects the necessary refinancing to be successful. Successful refinancing of the convertible bond by August 2011 is also a key covenant of the new Syndicated Senior Facilities Agreement. KUKA Group will thus be exposed to a refinancing risk, if the operational situation of the company or the capacity of financial markets to absorb the placement is inadequate.

Interest rates are analyzed regularly to control these risks and the results are an important part of our risk management system. A change in the interest rate of 1 percent referred to the period end would alter KUKA Group's interest income by € 0.2 million.

Transaction-related currency exchange risks are hedged using forward foreign exchange contracts. The goal is to hedge the currency exchange risk to approximately 60 percent per financial year on a rolling basis. Details of the central currency management process are provided under Financial instruments on pages 108 to 110 of the Group notes. As a basic principle, all KUKA Group companies must secure their foreign currency positions as soon as they arise. Translation risks; that is, valuation risks associated with balance sheet items whose value has been converted from a foreign currency, are not hedged, but are continuously monitored. The risk associated with the volatility of leading currencies and the resulting economic exchange risk (competitive risk) is mitigated by having production facilities in several countries (natural hedging). Internal guidelines are used to control the trading and use of derivatives. Associated risks are continuously monitored internally.

The impact of the international financial market crisis has sent the global real economy into a slump, which also had a negative impact on the Group's cash flow from operating activities. The developments in the real economy have generally hampered access to the money and capital markets and there is a risk that refinancing costs could increase further.

COMPLIANCE RISKS

The risks associated with compliance can lead to fines, sanctions, legal directives regarding future business conduct, forfeiture of profits, exclusion from certain businesses, loss of union concessions or other restrictions. Furthermore, involvement in potential corruption proceedings could harm the overall reputation of KUKA Group and could have a negative impact on efforts to compete for business in both the public and private sectors. Such proceedings could also have a negative impact on the relationship KUKA Group has with business partners upon which it depends, as well as its ability to find new business partners. It could also have a negative impact on the company's ability to pursue strategic projects and transactions that may be important for the business; e. g., joint ventures or other forms of cooperation. Ongoing or future proceedings could lead to the suspension of some existing contracts and third parties, including competitors, could initiate legal proceedings against KUKA Group for substantial sums of money.

In order to make these risks transparent and controllable, a Corporate Compliance Program was introduced in early 2008. All managers around the globe have been trained. The initiative did not uncover any substantial risks, since the company is actively countering any exposure by mitigating risks an early stage and striving to eliminate risk sources; e. g., by aligning its business processes.

OTHER RISKS

KUKA Group continuously monitors other risks and mitigates these as far as possible. There is no evidence of environmental risks from operational activities, since the company does not use hazardous materials. Where possible, legal risks are limited by using standardized general contracts. The Group's legal departments support the business operations and thereby help limit risks. A Group-wide Directors' and Officers' (D&O) liability insurance policy is in place that covers, among others, the business management bodies (Executive Board and managers) and supervisory bodies (Supervisory, administrative and advisory boards) of the German and foreign Group subsidiaries. Existing insurance policies are reviewed annually in order to weigh the relationship between the insurance protection and deductible amount versus the risk premium. The Executive Board subsequently makes the final decision.

The shareholder structure is regularly analyzed to assess a possible takeover of the company. Because it has operations around the world, KUKA Group is required to observe numerous international and country-specific regulations, mostly related to the laws of the particular country, as well as financial administration rules. There is a risk that countries could implement duties should the company fail to properly observe laws and other regulations. Tax audits in particular could have a negative impact on the Group. Should the auditors find compliance issues, the company could be liable for payment of interest charges, penalties and tax back payments. Appropriate precautions based on experience are taken for such tax risks.

SUMMARY

Considering the risks from an overall perspective, it is clear that KUKA Group is primarily exposed to business performance and financial risks. This includes in particular the effects of the international financial market crisis, which have worsened the economic downturn. There is also the issue of dependency on major customers in the automotive sector, particularly in the case of our American subsidiaries.

As outlined under financial risks, the agreement on extension of the financing could threaten the existence of the company. However, overall we consider KUKA Group's risks to be manageable and transparent.