Lufthansa Annual General Meeting 2016

Report of the Executive Board to the AGM on agenda item 7 pursuant to secs. 221(4), 186(3) sent. 4, 186(4) sent. 2 *AktG*

The issuing of conversion bonds, warrant bonds, profit participation rights and/or participating bonds (or combinations of these instruments) (collectively "Debt Instruments") provides the company with financing options on the capital market in addition to the traditional options of borrowing third-party capital and raising equity capital. In particular the authorisation to issue profit-related or profit-oriented instruments such as profit participation rights and participating bonds extends the Company's existing options, strengthens its financial basis through the issue of such financing instruments and safeguards the conditions for future business development. For this reason we are proposing to the Annual General Meeting the creation of a new authorisation to issue convertible bonds, warrant bonds, profit participation rights and/or participating bonds (or combinations of these instruments). The proposed new version is intended to provide an adjustment to the current market practice and to create greater flexibility. In total, Debt Instruments up to a total par value of EUR 1,500,000,000 may be issued with an entitlement to receive up to 92,907,750 no-par value registered shares in the Company.

The issuing of convertible bonds, warrant bonds, profit participation rights and/or participating bonds (or combinations of these instruments) enable the acquisition of third-party capital on attractive terms, which can be categorised, depending on the design of the relevant terms, as equity or equity-equivalent for both rating and reporting purposes. The conversion or option premiums achieved and the equity rating benefit the Company's capital base and thus enable it to use more attractive financing options. The additional options envisaged of establishing conversion or options obligations and tender options for the Company to provide shares in addition to granting conversion and/or option rights give additional leeway in the design of these financing instruments. The authorisation also gives the Company the necessary flexibility of either placing the Debt Instruments itself or via Group companies. Debt Instruments may be issued in the legal tender of other OECD countries as well as in EUR, with or without a limited term.

Shareholders are generally granted a subscription right. In order to make processing easier, the Company also intends to issue the Debt Instruments to banks or enterprises within the meaning of sec. 186(5) sent. 1 *AktG* with obligation to offer them to shareholders for subcription in accordance with their subscription rights. However, an exclusion of the subscription right is possible under the following conditions.

If convertible and/or warrant bonds (or profit participation rights or participating bonds with conversion rights, option rights or a conversion obligation or a tender option on the part of the Company) are issued, the Executive Board should be entitled, with the agreement of the Supervisory Board, to exclude subscription rights if the convertible or warrant bonds (or profit participation rights or participating bonds with conversion rights, option rights or a conversion obligation or tender option on the part of the Company) were issued for a cash consideration and the issue price is not significantly below the theoretical market value of the convertible or warrant bonds (or the profit participation rights or participating bonds with conversion rights, option rights or a conversion obligation or tender option on the part of the company) calculated using recognised financial mathematics methods. The calculated portion of the share capital apportioned to the shares that are to be issued on the basis of the Debt Instruments issued under this authorisation may not exceed 10% of the share capital at the time this authorisation comes into force or – if the value is lower – at the time of exercising this authorisation. This restriction recognises shares which were issued or sold during the term of this authorisation up to the point in time of their being exercised in direct or analogous application of sec. 186(3) sent. 4 *AktG*. It will also recognise shares which are to be issued or granted on the basis of the exercising of another authorisation with the exclusion of the subscription right in accordance with this provision;

This method of recognition ensures that no convertible and/or warrant bonds (or profit participation rights or participating bonds with warrant or conversion rights, conversion obligations or tender options) are issued if this would result in the subscription rights of shareholders being excluded in total for more than 10% of the share capital in direct or analogous application of sec, 186(3) sent. 4 *AktG* without a particular factual reason. This further restriction is in the interest of shareholders who aim at maintaining their participation level in the case of capital measures. In case of an exclusion of subscription rights, there is a requirement under the analogous application of sec. 186(3) sent. 4 *AktG* to set an issue price of the Debt Instruments that is not significantly below the market value. This is intended to ensure shareholder protection in respect of a dilution of their shareholding. Due to the requirement of this authorisation to set an issue price not substantially below the calculated market value, the value of the subscription right would in practise be zero. In order to secure this requirement for the issuance of the bonds, the issue price may not be substantially lower than the theoretical market value for the convertible or warrant bonds (or the participation rights or adjustment rights with option or conversion rights, conversion obligations or tendering rights) based on financial mathematical methods. In this case the protection of shareholders against a dilution of their shareholdings is ensured and the shareholder shall not incur any economic disadvantage through a subscription right exclusion. Shareholders who aim at maintaining their participation level with respect to the share capital in the Company or acquiring Debt Instruments in relation to their participation level may do so through purchase on the market.

Where participation rights or bonds without conversion rights, option rights or conversion or option obligations are to be issued, the Executive Board is authorised, with approval of the Supervisory Board, to exclude the shareholder subscription right, if such participation rights or participating bonds are issued with bond-like features, i.e. no membership rights in the Company, no participation in the liquidation proceedings and the level of interest not based on the levels of the annual net income, the net profit or dividends. In this case the interest and the issuance amount of the participation rights or the adjustment bonds must correspond to the market condition for similar financial borrowing. If the requirements named above are met, the exclusion of the subscription right shall not generate any disadvantage for shareholders, as the participation right or the bonds do not generate rights of membership and also no share of the liquidation proceeds or a share of the gains in the company. Stipulations may be made for interest payments contingent on an annual surplus, net income or a dividend. Such a rule would not be permitted, however, where greater annual surpluses, higher net annual income or higher dividends generate greater interest payments. The issue of participations rights or adjustment bonds shall also not dilute or alter neither the voting rights nor the participation of the shareholders in the company. In addition the marketable issue conditions, which are binding for the subscription, right exclusion in this case, no significant subscription right valuation.

The possibilities for excluding subscription rights described above give the Company the flexibility, to exploit beneficial capital market situations and grant the Company the opportunity to exploit low interest levels or beneficial demand windows flexibly and immediately for the issue of the financial instruments described above. The most important factor is that, in contrast to a bond issue with subscription rights, the issue price may be set shortly before the placement, whereby increased price change risk for the subscription period can be avoided and the issue proceeds can be maximized in the interest of all shareholders. Further advantages of the exclusion of subscription rights are the omission of preparation time in terms of costs for the issue and the placement. With an offer without subscription rights, the safety margin otherwise required as well as the placement risk can be reduced, leading to a more cost efficient company financing to the benefit of the company and its shareholders.

The Executive Board is also authorised to exclude the fractional amounts for the subscription rights with approval of the Supervisory Board. Such fractional amount may result from the issue volume and the presentation of a practical subscription ratio. An exclusion of the subscription rights eases the processing of the issues. The free fractions resulting from the exclusion of subscription rights shall be commercialised either by sale on the stock market or otherwise as best possible for the company.

In addition, the Executive Board with the approval of the Supervisory Board has the opportunity to exclude shareholder subscription rights, in order to grant the holder or creditor of convertible and/or warrant bonds or also the bonds with conversion or option obligations or a tendering right for the company from the supply of shares to compensate for dilution a subscription right in the scope as they would claim in the exercises of the conversion or option rights or be due after the fulfilment of the conversion or option obligations or the tendering rights of the Company. This offers the opportunity to prevent restrictions being required in the event of an exercise of the authorisation of the option or conversion price for the bearers due existing conversion or option rights in accordance with the relevant conditions.

In order to increase flexibility, the relevant conditions can have the company pay the conversion right holders or the warrant holder not in shares in the company but the market value in cash. A combination of these fulfilment forms is also possible. The relevant conditions may also allow changes to the number of conversion or option rights or subsequent to fulfilment of the shares to be issued under the conversion obligations or option price within a bandwidth set by the Executive Board regardless of the development of the share price or as the result of the dilution protection conditions during the period.

The fixed conversion or warrant price may not fall below 80% of the Company share price traded on the XETRA market (or an equivalent successor system). The average closing price on the ten trading day prior to the day of the resolution by the Executive Board governing the issue of the bonds is decisive unless subscription right trading takes place, which case the day of the subscription right trading with the exception of the two final stock exchange trading days of the subscription right trading is decisive. In as far as bonds with a conversion/option obligation or a tendering right for the Company require the supply of shares, the conversion/option price can be either at least the minimum price named above or the average volume-weighted price for the Company shares for at least three trading day in

XETRA trading (or an equivalent successor system) immediately prior to the determination of the conversion/option price (in keeping with relevant conditions). This shall also apply if the median price is below the minimum price named above (80%).

Lastly, the shareholders' subscription rights to the Debt Instruments may be excluded by the Executive Board, with approval of the Supervisory Board, if the issue of the Debt Instruments in exchange for a non-cash contribution or a benefit in kind, particularly in the context of mergers or for the (also indirect) acquisition of companies, operations, parts of companies, investments or other assets or entitlements to purchase assets including claims against the Company or its Group companies. The requirement is that the value of the contribution in kind is appropriate in relation to the value of the Debt Instrument. In the case of convertible and/or warrant bonds (or profit participation right or participating bonds with conversion rights, option rights or a conversion or option obligation or a tender option on the part of the Company) the price is the theoretical market value calculated using recognised methods. The issue of Debt Instruments against non-cash contributions opens up the possibility of using the Debt Instruments in appropriate cases as acquisition currency in association with the acquisition of companies, parts of companies or investments in companies. As a supplement to authorised capital, this creates the leeway to take advantage of the opportunities that arise to acquire companies, parts of companies or investments in companies in a manner which protects liquidity. Even when taking into consideration an optimum financing structure, such a procedure may be beneficial under individual circumstances.

According to the authorisation, the total shares issued with an exclusion of the subscription right may not exceed 20% of the share capital. This limit applies both at the date when it comes into force and – if this value is lower – at the time this authorisation is exercised. This limit includes (i) shares that were were issued or sold during the term of this authorisation on the basis of another authorisation excluding the subscription right, or (ii) that are to be issued on the basis of conversion or warrant bonds issued during the term of this authorisation on the basis of exercising another authorisation excluding the subscription right. As, under the current authorisation, the possibility of excluding the subscription right is very limited, this additional limitation, extending beyond the statutory limitations, will severely limit damage to the shareholders.

The purpose of the intended contingent capital is to settle the conversion or option rights associated with the conversion and/or warrant bonds issued against cash consideration (or profit participation rights or participating bonds with conversion or option rights, a conversion or option obligation or a tender option on the part of the issuer) or to perform conversion or option obligations or the tender option right on the part of the Company to provide shares, provided that neither treasury shares nor other forms of performance are used in this regard. The purpose of the intended contingent capital is not to settle conversion or option rights on conversion and/or warrant bonds issued against a non-cash consideration (or profit participation rights or participating bonds with conversion or option rights, a conversion or option obligation or a tender option on the part of the issuer) to settle the company's or conversion or option rights or to meet the tender option on the part of the Company to provide shares.

In order to safeguard the Company's powers in compliance with Germany's Aviation Compliance Documentation Act (*LuftNaSiG*), the relevant terms and conditions provide that, when exercising the conversion or option right, or upon the occurrence of the conversion or option obligation, or a tender option on the part of the Company to provide shares, the conversion bond or the warrant must be transferred to a domestic bank and the bearer or debtholder of the conversion bond or of the option right respectively will receive a cash payment related to the stock market price instead of shares in the Company. This rule is required so the Company can comply with aviation law. The air transportation agreements concluded by the Federal Republic of Germany typically include various clauses that it must be shown, on request, to the other contracting party, that significant investments (normally majority shareholdings) and the company designated by a contracting state is controlled by citizens of this contracting party. In order to avoid any risks arising in respect of the Company's powers under aviation law as a result of the exercise of conversions or options, the Company needs to be able to pay cash instead of shares exercising the conversion or option rights or that the new shares are acquired by a third party through exercising the conversion or option rights with the requirement that they sell them at a price that is not significantly lower than the stock market price.

Frankfurt, 7 March 2016
The Executive Board