Lufthansa Annual General Meeting 2020

Report of the Executive Board to the AGM on agenda item 7, pursuant to Section 221(4), sentence 2 AktG in conjunction with Section 186(4), sentence 2 AktG

The issuing of convertible bonds, option bonds, profit participation rights and/or participating bonds (or combinations of these instruments) (hereinafter referred to as "Debt Instruments") provides the Company with the opportunity, in addition to the traditional options of raising debt and equity, to use attractive financing alternatives on the capital market, depending on the market situation. 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 for strengthening its financial position by issuing such financing instruments and thereby ensuring the conditions for future business development. For this reason, the creation of a new authorisation to issue Debt Instruments is proposed to the Annual General Meeting. In total, bonds should be issued with a total nominal value of up to EUR 1,500,000,000.00, which entitle the company to purchase up to 47,819,425 no-par value shares in the name of the Company.

The issue of Debt Instruments enables the acquisition of debt capital on favourable terms, which can be classified as equity or equity capital equivalent depending on the respective conditions both for rating purposes and for balance sheet purposes. The conversion or option premiums achieved and the equity classification benefit the Company's capital base and thus enable it to use attractive financing options. The other options provided for, in addition to the granting of conversion and/or option rights, of establishing conversion or option obligations and the right of the Company to supply shares or to provide for combinations of these instruments, extend the design scope for these financing instruments. The authorisation also gives the Company the necessary flexibility to place the Debt Instruments itself or via Group companies. In addition to EUR, Debt Instruments can also be issued in other legal currencies of OECD countries, with or without a maturity limit.

In principle, the shareholders are to be granted a subscription right. In order to facilitate settlement, it should also be possible to make use of the option to issue Debt Instruments to credit institutions or companies within the meaning of Section 186(5), sentence 1 AktG with the obligation to offer them to shareholders for subscription in accordance with their subscription right. However, under the following conditions, it shall be possible to exclude the subscription right.

Initially, the Executive Board shall be authorised, with the approval of the Supervisory Board, to exclude the subscription right of the shareholders if the issue of the bonds is made in cash at a price that does not significantly fall below the market value of these bonds. This gives the Company the opportunity to take advantage of favourable market situations very quickly and at short notice, and to achieve better conditions for the determination of interest rate, option or conversion price and issue price of the bonds by setting the conditions close to the market. Market-oriented condition determination and seamless placement would not be possible if the subscription right was respected. Section 186(2) AktG permits publication of the reference price (and thus of the conditions of the Debt Instruments) until the third-last day of the subscription period. However, given the volatility of the stock markets which can often be observed, there is a market risk over several days, leading to safety discounts in the setting of bond conditions and thus leading to non-market conditions. In addition, if a subscription right exists, successful placement with third parties is at risk or additional expenses are incurred due to the uncertainty about its exercise. Finally, if a subscription right is granted, the Company cannot react to favourable or unfavourable market conditions in the short term due to the length of the subscription period, but is exposed to declining share prices during the subscription period, which can lead to an unfavourable acquisition of equity for the Company.

In this case, a complete exclusion of the subscription right applies in accordance with Section 221(4), sentence 2 AktG and the provisions of Section 186(3), sentence 4 AktG. The content of the resolution must comply with the subscription right exclusion limit specified within these provisions, which is 10% of share capital. The volume of the conditional capital, which in this case is to be made available at most to secure the option rights or conversion rights or obligations, may not exceed 10% of the share capital existing when the authorisation to exclude subscription rights becomes effective in accordance with Section 186(3), sentence 4 AktG. A corresponding requirement in the authorisation decision also ensures that the 10% limit is not exceeded even in the event of a capital reduction, since according to the authorisation to exclude subscription rights, 10% of the share capital must fundamentally not be exceeded, either on the effective date or – if this value is lower – at the time of the exercise of this authorisation. Own shares, which are sold under the appropriate application of Section 186(3), sentence 4 AktG, as well as those shares which are issued out of authorised capital, excluding the subscription right in accordance with Section 186(3), sentence 4 AktG, shall be credited and the amount reduced as appropriate if the sale or issue takes place during the term of this authorisation until the issue of the Debt Instruments with option and/or conversion rights or obligations and free of subscription rights pursuant to Section 186(3), sentence 4 AktG.

Furthermore, it follows from Section 186(3), sentence 4 AktG that the issue price must not fall significantly below the stock market price. This is to ensure that significant economic dilution of the value of the shares does not occur. Whether such a dilution effect occurs in the issue of convertible bonds, option bonds, participating bonds or combinations of these instruments without a subscription right can be determined by calculating the hypothetical market value of these bonds in accordance with recognised, in particular financial mathematical, methods and comparing them with the issue price. If, after due consideration, this issue price is only marginally lower than the hypothetical stock market price at the time of issue of the convertible, option or participating bonds or combinations of these instruments, a subscription right exclusion is permitted according to the sense and purpose of Section 186(3), sentence 4 AktG since the difference is insignificant. The decision therefore provides that, before issuing the bonds, the Executive Board must conclude that the planned issue price does not lead to a significant dilution of the value of the shares. This would reduce the calculated market value of a subscription right to almost zero, so that the exclusion of subscription rights does not create a significant economic disadvantage for shareholders.

All of this ensures that the exclusion of subscription rights does not significantly dilute the value of the shares. In addition, shareholders have the option of maintaining their share of the company's share capital at any time, even after exercising conversion or option rights, by buying in shares via the stock exchange. On the other hand, the Company's authorisation to exclude subscription rights enables market-related conditions to be determined, maximum security with regard to placement with third parties and the short-notice exploitation of favourable market situations.

Furthermore, the subscription right of the shareholders may be excluded by the Executive Board with the approval of the Supervisory Board if Debt Instruments are issued against benefits or contributions in kind, in particular in the context of company mergers or of (also indirect) acquisition of companies, businesses, parts of companies, holdings or other assets or claims to the acquisition of assets, including claims against the Company or its Group companies, and this is in the interest of the Company. Provided, that the value of the benefit in kind is a fair value compared to the value of the bond. Thus the theoretical market value according to recognised methods is relevant.

The issue of Debt Instruments against benefits in kind without subscription rights enables the Executive Board, inter alia, to use the Debt Instruments as an acquisition currency in appropriate individual cases to acquire such benefits in the context of company mergers or of (also indirect) acquisition of companies, businesses, parts of companies, holdings or other assets or claims to the acquisition of assets, including claims against the Company or its Group companies. Business expansion through acquisition of a business or equity typically requires rapid decisions. With this authorisation the Executive Board can react quickly and flexibly to advantageous offers or other opportunities on the national or international market and exploit opportunities for expansion by acquiring companies or holdings against issuing Debt Instruments in the interests of the Company and its shareholders.

The Executive Board is also authorised, with the consent of the Supervisory Board, to exclude fractional amounts from subscription rights. Such fractional amounts may result from the amount of the respective issue volume and the practical representation of the subscription ratio. In such cases, the exclusion of the subscription right facilitates the settlement of the issue. The free fractions excluded from shareholders' subscription rights are either sold via the stock exchange or realised in the best-possible manner for the Company.

Insofar as profit participation rights or participating bonds are to be issued without conversion right, option right or conversion or option obligation, the Executive Board is authorised, with the approval of the Supervisory Board to exclude the shareholders' right of subscription if these rights of participation or participating bonds have bond-like features, i.e. no membership rights in the company, no participation in the liquidation proceeds and the amount of the interest is not calculated on the basis of the amount of the net profit, balance net profit or dividend. It is also necessary that the interest rate and the amount of the profit participation rights or participating bonds issued correspond to the current market conditions for comparable exposures at the time of issue. If the above conditions are met, the exclusion of the subscription right does not result in any disadvantages for the shareholders, since the profit participation rights and/or participating bonds do not constitute membership rights and do not grant any share of the liquidation proceeds or the profits of the Company. Although it is permissible that the interest rate will depend on a net profit, a net profit or a dividend, a provision whereby a higher net profit, a higher net profit or a higher dividend would lead to a higher interest rate is inadmissible. Accordingly, the issue of the profit participation rights and/or participating bonds does not alter or dilute the voting rights or the participation of the shareholders in the company and their profits. Furthermore, no significant subscription right results due to the fair market conditions of issue, which are mandatory in this case of subscription right exclusion.

Finally, the Executive Board shall be given the opportunity, with the approval of the Supervisory Board, to exclude the subscription right of the shareholders in order to grant the holders of conversion or option rights to no-par value shares of the company or to the creditors of corresponding conversion or option obligation a subscription right to compensate for dilutions such as they would be entitled to after exercising the conversion or option rights or after fulfilling the conversion or option obligations or the right to tender of the company. This offers the possibility of preventing the option or conversion price for the holders of existing conversion or option rights from being reduced in the event of the authorisation being used in accordance with the respective conditions.

In order to increase flexibility, the respective terms of the bond may provide that the Company does not grant shares of the Company to a person entitled to the conversion or to an option, but pays the equivalent in cash. It should also be permissible to provide for a combination of these forms of fulfilment. The terms of the bond may also provide that the Debt Instruments, which are linked to option rights or conversion rights or obligations, are converted at the option of the Company into existing shares of the Company instead of into new shares of conditional capital, or that the option right can be fulfilled by the supply of such shares. The terms of the bond may also provide for the right of the Company to grant to the holders or creditors, in whole or in part, no-par value shares of the Company in lieu of the amount due in cash upon the maturity of the bond associated with option rights or conversion rights or obligations (including maturity due to termination).

The conversion or option price to be determined in each case may not be less than 80% of the price of the Company's share in Xetra trading system on the Frankfurt Stock Exchange (or a comparable successor system). For this purpose, the average closing price on the ten trading days before the date of the decision by the Executive Board shall be decisive regarding the issue of the respective bonds, unless subscription rights trading takes place, in which case the days of subscription rights trading are to be decisive, with the exception of the two last trading days of stock exchange of subscription rights trading. Where Debt Instruments include a conversion/option obligation or the right of the company to supply shares, the conversion/option price must be at least equal to the minimum price specified above or equal to the average volume-weighted price of the Company's share on at least three trading days in Xetra trading system on the Frankfurt Stock Exchange (or a comparable successor system) immediately prior to the determination of the conversion/option price in accordance with the respective conditions. This also applies if this average price is below the above-mentioned minimum price (80%).

Under the authorisation, the total number of shares issued under exclusion of the subscription right may not exceed 10% of the share capital, neither on the effective date nor, if this value is lower, at the time of the exercise of this authorisation. Shares will be counted against this limit which (i) are issued or sold during the term of this authorisation under another authorisation excluding the subscription right, or (ii) which are to be issued on the basis of convertible bonds or option bonds issued during the term of this authorisation on the basis of the use of another authorisation excluding the subscription right.

In order to ensure the Company's operating licences under air traffic law in accordance with the German Aviation Compliance Documentation Act (LuftNaSiG), the respective conditions shall provide for the possibility that when the conversion or option right is exercised, the convertible bond or the option certificate must be transferred to a domestic credit institution and the holder or creditor of the convertible bond or option certificate must receive a cash payment based on the stock exchange price instead of shares of the Company. This regulation is necessary to enable the Company to comply with air traffic regulations. The air traffic agreements concluded by the Federal Republic of Germany typically provide, in various terms, that on request of other contractual party it must be proven that substantial holdings (normally understood as a majority interest) and actual control of a company designated by a contracting state are in the hands of nationals from that contractual party. In order to avoid the situation where conversion or exercise of options poses a risk to the Company's operation licences, it is necessary that when the conversion or option rights are exercised, the Company can pay cash instead of shares or require that the new shares acquired by a third party by exercising the conversion or option rights be resold at a price not significantly lower than the stock exchange price.

Frankfurt, March 2020

The Executive Board

Translation for convenience only;
In case of any discrepancy or ambiguity the German version shall prevail.