

REPORT OF THE SUPERVISORY BOARD

DEAR SHAREHOLDERS,

2019 was a financial year with particular challenges. The economic environment became increasingly difficult, while fire damage in the surface technologies segment and write-downs in the engineered products segment impacted the development of our Group. Together with the Management Board, in light of this we introduced extensive measures to create the basis for sustainable and successful corporate development.

For 2020, we expect a persistently difficult environment for the KAP Group. In particular, the potential and still unforeseeable impact of the spread of the coronavirus pandemic will have a negative effect on business development. Initial countermeasures and mitigation measures have already been introduced.

COLLABORATION WITH THE MANAGEMENT BOARD

The Supervisory Board performed the tasks incumbent on it pursuant to the law, the Articles of Association and the rules of procedure with great care in the 2019 financial year. We regularly advised the Management Board on the management of the Company and monitored its work. This was based on detailed written and oral reports by the Management Board, which were provided in and outside of the meetings of the Supervisory Board. Between the meetings, regular dialogue also took place between the chairman of the Supervisory Board and the Management Board and between the members of the audit committee and the Management Board. The Supervisory Board was directly involved in all decisions of fundamental importance for the Group. We were always comprehensively informed about the Group's business development, intended business policies, the Group's situation, the risk situation and risk management, compliance, corporate planning (including financial, investment, sales and personnel planning) and current topics. Where the Supervisory Board's consent was needed for decisions or measures of the Management Board on the grounds of the law, the Articles of Association or the rules of procedure, we comprehensively reviewed and thoroughly discussed the draft resolutions and adopted a resolution.

SUPERVISORY BOARD MEETINGS AND COMMITTEE MEETINGS

In the year under review, there were a total of five regular meetings of the Supervisory Board and two meetings of the audit committee, which was newly created in July 2019. The members of the Management Board took part in the meetings of the Supervisory Board - unless consultation without participation of the Management Board was considered appropriate on individual topics such as personnel matters of the Management Board - and reported in detail about the progress of business affairs, the current revenue and earnings development, the opportunities and risks of business development, the significant planned or ongoing investments and disinvestments, and the Group's situation overall. All the members took part in the regular Supervisory Board meetings in the 2019 financial year, with the exception of the meeting held on 19 February 2019, which Pavlin Kumchev, who left on 29 February 2019, did not attend. No member of the Supervisory Board took part in less than 50% of all meetings. The meetings had the following focuses:

In the meeting of 6 February 2019, we dealt intensively with the preliminary figures for the 2018 financial year. In addition, the possibility of a sale and leaseback transaction for an industrial property of the KAP Group was discussed.

With the auditor present, we dealt extensively with the 2018 annual financial statements and consolidated financial statements, the management report and the Group management report, the Group's separate non-financial report and the proposal on the appropriation of profits at the meeting of 25 March 2019. The auditor explained the audit reports including the focuses of the audit. In addition, adopted the Declaration of Conformity and voted on the selection of the new auditor. Moreover, the Management Board reported on current M&A opportunities and financing topics.

In the meeting on 25 June 2019, the focus was on the presentation of business development in the first half of the year and the 2019 corporate planning. The Management Board reported in detail about current topics and projects from the individual segments. Furthermore, it presented concrete approaches for possible strengthening of the existing compliance system and for optimisation of the Group-wide IT landscape. The preparation of the Annual General Meeting, the expansion of investor relations activities in connection with the higher requirements of the Prime Standard segment of the stock exchange and remuneration topics were further agenda items.

At the meeting on 26 September 2019, the focus was on detailed reporting on business development and on current projects in every segment of the KAP Group and the KAP Group's strategic direction. This also included possibilities for improving the operating performance in the individual segments. The Management Board also reported on the current corporate planning for the full year.

On 5 December 2019 we met for another Supervisory Board meeting. The focus at this meeting was not only current business development and the planning for the 2020 financial year but also the status quo of possible restructuring measures in the engineered products and precision components segments against the background of significantly worsened market conditions in the automotive sector. We also approved current investment plans in the surface technologies segment.

In addition, there were ten extraordinary meetings of the Supervisory Board, five of which by way of circulation of written resolutions. In these meetings, among other things, investment and disinvestment plans, personnel and remuneration matters, the Group's separate non-financial report, the Supervisory Board's report and the rules of procedure for the audit committee were discussed or adopted.

The Supervisory Board has had a committee in the form of the audit committee since July 2019. It is entrusted with all the tasks specified in section 107 (3) sentence 2 of the German Stock Corporation Act (AktG) and in 5.3.2. of the German Corporate Governance Code in the version of 7 February 2017. In the 2019 financial year, the audit committee particularly dealt with the

consolidated half-year report and the interim statement on the third quarter of 2019. At that point, it began reviewing the existing risk-management and internal control systems of the Company. Corporate planning for 2020 and compliance were further topics. The auditor reported on its audit findings in one of two meetings of the audit committee. The committee chairman reported on the meetings and the work of the audit committee at each Supervisory Board meeting.

CORPORATE GOVERNANCE

The principles of good corporate governance are very important to KAP AG and the Supervisory Board. The further development of corporate governance in our Group, not least in light of the substantially revised German Corporate Governance Code draft by the Government Commission, and compliance with the recommendations of the German Corporate Governance Code were a key focus of our auditing and consultancy work in the 2019 financial year. No conflicts of interests for individual members of the Supervisory Board came to light in the past financial year. The Corporate Governance Report contains additional information on corporate governance on page 20.

AUDIT OF THE ANNUAL FINANCIAL STATEMENTS AND THE CONSOLIDATED FINANCIAL STATEMENTS

Mazars GmbH & Co. KG Wirtschaftsprüfungsgesellschaft Steuerberatungsgesellschaft, Frankfurt am Main, which was appointed as auditor by the Annual General meeting, audited the annual financial statements and consolidated financial statements including the management reports for the 2019 financial year, which were prepared by the Management Board, taking into account the accounting records. The findings showed that the Company complied with the rules of the German Commercial Code (HGB) and International Financial Reporting Standards as adopted by the EU. The auditor did not raise any objections and issued unqualified audit opinions. The Supervisory Board satisfied itself of the independence of the auditor and the persons acting on the auditor's behalf.

The annual financial statements and consolidated financial statements including the management report and Group management report, the proposal for the appropriation of profit, the Group's separate non-financial report and the audit reports of the auditor were audited at meetings of the Supervisory Board on 2 and 22 April 2020 and discussed in detail with the Management Board and auditor. The financial statement documents and the audit reports were available to all members of the Supervisory Board on time and were dealt with in detail at the accounts meeting of the Supervisory Board on 2 April 2020. The auditor reported on the findings of the audit during its deliberations and was available to us for additional questions and information. The key audit matters were a focus. Based on the final result of our own review, we concurred with the findings of the audit conducted by the auditor and did not raise to any objections.

The Supervisory Board approved the annual financial statements of KAP AG prepared by the Management Board and the consolidated financial statements of the KAP Group at the meeting held to adopt the financial statements on 2 April 2020. KAP AG's 2019 annual financial statements are thus adopted. We agree with the Management Board's proposal on the appropriation of retained earnings, which recommends suspension of dividend distribution and carrying forward retained earnings.

CHANGES IN THE SUPERVISORY BOARD AND MANAGEMENT BOARD

Pavlin Kumchev resigned from the Supervisory Board with effect as of 29 February 2019 for reasons of a career change. His successor is Joachim Coers, who was elected to the Supervisory Board as a new member by shareholders at the Annual General Meeting on 3 July 2019. Joachim Coers is a proven industry expert with experience including as chairman of the executive board of Tognum AG and chairman of the management board of MTU Friedrichshafen GmbH. His term in office runs until the end of the Annual General Meeting that passes the resolution on the formal approval of the Supervisory Board's actions for the 2022 financial year.

With effect as of 1 October 2019, the Supervisory Board appointed Supervisory Board member Uwe Stahmer as an interim member of the Management Board. Following the resignation of Spokesman of the Management Board Guido Decker with effect as of 30 September 2019, the Management Board thus consists of at least two persons, as required by the Articles of Association.

The KAP AG Supervisory Board appointed Eckehard Forberich as a new member and Spokesman of the Management Board with effect as of 1 March 2020. On the appointment of the new member of the Management Board, Uwe Stahmer stepped down from his interim position on the Management Board and resumed his position on the Supervisory Board, which had been put on hold while he served on the Management Board. The members of the Supervisory Board would like to thank him for his work as an interim member of the Management Board.

THANKS

The Supervisory Board would like to thank the members of the Management Board, the segment managers, the managing directors of the segment companies and all the employees for their dedication and their achievements in the challenging 2019 financial year.

Fulda, 10 March 2020

For the Supervisory Board



Christian Schmitz

Chairman of the Supervisory Board