IWKA Aktiengesellschaft

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RISK MANAGEMENT

The IWKA Group conducts business around the globe and participates in a number of market sectors, which exposes the company to a variety of risks. It is impossible to imagine doing business as an entrepreneur without being prepared to accept calculated risks. However, the key is to identify risks that threaten the existence of the company at an early stage and to avoid or mitigate them as much as possible. Unavoidable consequences must be managed or transferred. Our goal is to systematically and continually improve shareholder value and achieve our targets while knowingly accepting unavoidable risks. The key is to keep risks that we can influence manageable. IWKA systematically identifies external and internal risks in all divisions and subsidiaries and evaluates them consistently throughout the Group with respect to potential level of damage and likelihood of the events occurring. The managers of the divisions and subsidiaries are directly responsible for the early identification, control and communication of risks. Risk coordinators in the business units ensure that the reporting process is uniform. The risk management system is coordinated at Group headquarters 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 risks at an early stage and take appropriate steps to counter them. 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 integrated into the risk management system is suitable for identifying risks at an early stage that threaten the existence of the company.

MARKET AND BUSINESS RISKS

Companies doing business in the mechanical engineering business sector are exposed to a series of risks. Demand depends on the economic cycle, which affects the investment plans of our regular customers in the various market subsectors. Since it conducts business around the globe, IWKA is also exposed to country risks, exchange-rate fluctuations, financial and technical risks and the risk of substantial price increases of key raw materials, such as those experienced recently with oil and steel.

During the 2005 financial year, we continued to implement our ongoing cost-cutting and efficiency improvement programs to address the business impact of the general economic conditions. Further activities were also defined and included in a group-wide program.

Restructuring the company's divisions contributes significantly to reducing the Group's business risks. The various operating companies are coordinated by management companies, which are charged with the task of minimizing divisional business risks, identifying opportunities and exploiting them in ways that lead to higher profits. A key element is the integration and cooperation within and between divisions.

PLANT CONSTRUCTION

The key risks associated with plant construction are the high complexity of IWKA's products, the long duration of the project-management phase and the infrequency of the orders received. In addition, our revenues and profits are at risk when carmakers' production quantities do not increase, or even decline. Because the value chain is coming apart, carmakers are increasingly attempting to outsource manufacturing activities. This enables subsuppliers to participate in new business opportunities. IWKA limits the risks of the new pay-on-production business models by using structured financing and having appropriate contractual agreements.

PACKAGING

Business in the European companies continues to be dominated by high exports, and is thus also particularly sensitive to the value of the US dollar versus the euro. In addition, concentration in the marketplace and the overcapacities that occur as a result always have an impact on the demand for packaging machines. The high price of steel, particularly the stainless steel preferred in the packaging industry, also erodes the margins we are able to achieve with our products.

ROBOTICS

The risks in the robotics markets relate primarily to the continuing price pressure in the automotive industry. The tense business situation in some areas is causing capital spending plans to be shelved. This makes it more and more difficult to forecast the project business.

The business situation in some major automotive companies is causing them to extend the service life of their robots, which in turn leads to lower spending on replacements. KUKA Roboter will only be able to counter such trends by continuously developing new products and applications that offer customers quantifiable financial advantages and have very fast paybacks.

The risk in developing and implementing applications for new general industry markets is higher in some areas. This has been shown, for example, with product introductions in the medical equipment and entertainment sectors.

CORPORATE STRATEGY RISKS

The aim of IWKA's three business divisions is to be technology leaders in their chosen markets and thereby become the market leader. Enhancing our technologies through coordinated innovation programs is therefore of key importance. To a large extent, this also entails identifying the opportunities and risks of technical innovations in a timely manner and evaluating them with respect to feasibility. This also ensures that the strategic risks are identified at an early stage, so that adequate countermeasures can be quickly implemented.

Using efficient quality assurance systems in combination with regular certification programs helps convince our customers that we offer high quality and strengthens our companies' positions in their target markets.

Acquisitions and investments go hand-in-hand with complex risk factors. Acquisitions and integration projects at IWKA are therefore managed using documented processes to make sure that material risks are identified and monitored.

PERSONNEL RISKS

IWKA Aktiengesellschaft relies on qualified specialists and managers to achieve its goals. In today's very competitive marketplace, it is therefore an ongoing challenge to attract these human resources to the Group and ensure they identify with the company long-term. There is a particularly high demand for well educated and motivated employees in growth markets, which is why in-house qualification programs are required. 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.

Human resources management, training and continuing education programs ensure that employees at all levels of the company become entrepreneurial in the way they think and do their day-to-day jobs. This is supported by tying variable incentives to managers' remuneration packages, which are paid according to business performance.

INFORMATION SYSTEMS RISKS

All business processes are modeled on a modern IT system. The growing information technology-related risk associated with the rapidly increasing integration of IT-supported business processes demands that IWKA continuously analyze and optimize its current information technologies in order to ensure the highest possible level of security. The existing methods are continuously updated and improved.

FINANCIAL RISKS/EXCHANGE RATE RISKS

IWKA manages and, if necessary, hedges against the risks associated with group-wide credit, liquidity, interest and exchange requirements. Risk hedging related to interest and currency exchange rates (price change risks) is done almost exclusively by actively using standard derivatives to hedge the underlying transaction. Both the trading and use of derivatives is regulated by internal guidelines and undergoes continuous internal risk analysis. In addition, it is monitored annually by the German public auditors. Transaction-related currency exchange risks are hedged using forward foreign exchange contracts (primarily futures and swap transactions). We reduce the risk associated with the volatility of leading currencies and the resulting exchange risk (competitive risk) by using production facilities in various countries.

We reduce the overall liquidity risk by closely monitoring the Group's companies and controlling the payment flows (receivables as well as working capital management). The IWKA Group also has adequate lines of credit with banks. The company also has a number of medium and long-term lending agreements and a commercial paper program that were not fully utilized as of December 31, 2005, thanks to adequate liquidity.

SUMMARY

An overall assessment of the risks shows that the IWKA Group is primarily exposed to market risks. In particular, this includes the business cycle and the dependence on important major customers in the automotive and consumer goods sector. Risks resulting from value-added processes are controlled by our risk management system, and their potential negative impact is therefore limited.

In summary, there are risks associated with high raw material prices, continued price pressure and exchange rates, which the Group is addressing by implementing numerous performance improvement and cost cutting programs. The IWKA Group risks are manageable and transparent, and as far as we are able to foresee, do not threaten the company's survival. Neither do we see any risks that could threaten the company's future business or legal existence.