IFRS consolidated financial statements of

HENSOLDT AG

as of December 31, 2020

Consolidated income statement

		Fiscal year	
in € million	Note	2020	2019
Revenue	11	1,206.9	1,114.2
Cost of sales	11	-936.1	-859.3
Gross profit		**270.8**	**254.9**
Selling and distribution expenses		-90.2	-84.8
General administrative expenses		-87.2	-76.3
Research and development costs	12	-25.1	-31.0
Other operating income	13	18.9	25.3
Other operating expenses	13	-16.1	-24.8
Share of profit / loss from investment accounted for using the equity method	8	-2.6	-1.2
Earnings before finance result and income taxes (EBIT)		**68.5**	**62.1**
Interest income	14	4.0	58.9
Interest expense	14	-137.7	-83.5
Other finance income / costs	14	-10.0	-1.9
Finance result		**-143.7**	**-26.5**
Earnings before income taxes		**-75.2**	**35.6**
Income taxes	15	10.7	-27.4
Group result		**-64.5**	**8.2**
thereof attributable to the owners of HENSOLDT AG		*-65.2*	*5.9*
thereof attributable to non-controlling interests		*0.7*	*2.3*
Earnings per Share			
Basic and diluted earnings per share (EUR)	16	-0.75	0.07

The following disclosures in the notes are an integral part of these consolidated financial statements.

Consolidated statement of comprehensive income

in € million	Note	Fiscal year 2020	2019
Group result		**-64.5**	**8.2**
Other comprehensive income			
Items that will not be reclassified to profit or loss			
Measurement of defined benefit plans	32.1	-40.4	-64.6
Tax on items that will not be reclassified to profit or loss		13.0	24.7
Subtotal		**-27.4**	**-39.9**
Items that will not be reclassified to profit or loss			
Difference from currency translation of financial statements		-9.5	3.6
Cash flow hedge - unrealized gains/losses	36.3	-2.3	-1.6
Cash flow hedge - reclassification to profit or loss		0.9	1.2
Tax effect on unrealized gains/losses		0.4	-0.3
Subtotal		**-10.5**	**2.8**
Other comprehensive income net of tax		**-37.9**	**-37.0**
Total comprehensive loss in the financial year		**-102.4**	**-28.8**
thereof attributable to the owners of HENSOLDT AG		*-101.8*	*-31.6*
thereof attributable to non-controlling interests		*-0.7*	*2.8*

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Consolidated statement of financial position

ASSETS		Dec. 31,	Dec. 31,
in € million	Note	2020	2019
Non-current assets		**1,313.4**	**1,392.6**
Goodw ill [1]	17	637.2	637.2
Intangible assets	17	386.2	403.3
Property, plant and equipment	18	103.1	92.9
Right-of-use assets	28	143.5	154.9
Investments accounted for using the equity method	8	0	1.2
Other investments and other non-current financial assets	19	11.3	14.7
Non-current other financial assets	26	1.0	53.2
Other non-current assets	27	4.8	4.9
Deferred tax assets	15	26.3	30.4
Current assets		**1,634.2**	**1,063.1**
Other non-current financial assets, due on short-notice	19	11.2	3.0
Inventories	20	403.7	411.1
Contract assets	11	204.4	165.9
Trade receivables	21	282.0	290.8
Other current financial assets	26	7.1	5.8
Other current assets[1]	27	78.7	46.1
Income tax receivables	15	1.6	3.2
Cash and cash equivalents	35.1	645.5	137.4
Total assets		**2,947.6**	**2,455.7**

[1]Adjustment of previous year's figures due to IFRS 3: Goodw ill €- 9.6 million ; other current assets €+ 11.7 million (please refer to Note 7.1)

The following disclosures in the notes are an integral part of these consolidated financial statements.

EQUITY AND LIABILITIES		Dec. 31,	Dec. 31,
in € million	Note	2020	2019
Share capital	33.1	105.0	10.0
Capital reserve		596.8	396.7
Other reserves		-86.3	-49.8
Retained earnings		-281.6	-215.8
Equity held by shareholders of HENSOLDT AG		**333.9**	**141.2**
Non-controlling interests		12.9	13.6
Equity, total	33	**346.8**	**154.8**
Non-current liabilities		**1,257.1**	**1,517.9**
Non-current provisions	23	482.6	413.6
Non-current financing liabilities	35	601.3	887.7
Non-current contract liabilities	11	16.0	16.3
Non-current lease liabilities	28	140.3	147.5
Other non-current financial liabilities	26	0.2	0.2
Other non-current liabilities	27	8.9	7.7
Deferred tax liabilities	15	7.7	44.8
Current liabilities		**1,343.7**	**783.0**
Current provisions	23	193.6	185.1
Current financing liabilities	35	363.3	11.3
Current contract liabilities	11	416.8	317.1
Current lease liabilities	28	13.7	13.0
Trade payables	22	164.0	168.8
Other current financial liabilities	26	97.8	20.5
Other current liabilities[1]	27	86.9	67.1
Tax liabilities	15	7.6	0.1
Total equity and liabilities		**2,947.6**	**2,455.7**

[1]Adjustment of previous year's figures due to IFRS 3: €+2.1 million (please refer to Note 7.1)

The following disclosures in the notes are an integral part of these consolidated financial statements.

Consolidated statement of cash flows

		Fiscal year	
in € million	Note	2020	2019
Group result		**-64.5**	**8.2**
Depreciation and amortization	17/18/28	120.8	129.6
Allowances on inventories, trade receivables and contract assets		-2.4	13.2
Profit/loss from disposals of non-current assets		0.0	0.4
Share of profit in entities recognized according to the equity method		2.6	1.2
Financial expenses (net)		128.2	24.6
Other non-cash expenses/income		-5.1	-5.4
Change in			
Provisions		46.4	-0.4
Inventories		5.3	-17.8
Contract balances		61.4	-89.4
Trade receivables		5.3	56.4
Trade payables		-8.6	-13.4
Other assets and liabilities		-17.8	4.6
Interest paid		-43.6	-45.1
Transaction costs on refinancing paid		-14.9	0.0
Income tax expense (+) / income (-)		-10.7	27.4
Income taxes payments (-) / refunds (+)		-5.5	-10.9
Cash flows from operating activities		**196.9**	**83.2**
Acquisition/addition of intangible assets and property, plant and equipment	17/18	-97.4	-80.5
Proceeds from sale of intangible assets and property, plant and equipment	17/18	0.2	0.5
Acquisition of associates, other investments and other non-current investments	19	-6.6	-3.9
Disposals of associates, other investments and other non-current investments		2.3	2.1
Acquisition or subsidiaries net of cash acquired	7	6.4	-83.8
Other		0.1	0.0
Cash flows from investing activities		**-95.0**	**-165.6**

		Fiscal year	
in € million	Note	2020	2019
Proceeds from financial liabilities (syndicated loan)	35.3	950.0	2.4
Repayment of financial liabilities (syndicated loan)	35.3	-920.0	0.0
Increase of other financial liabilities	35.3	97.1	0.0
Dividend payments to non controlling interests		-0.2	-0.2
Payment of lease liabilities	35.3	-14.3	-11.3
Issue of shares	35.3	300.0	0.0
Transaction costs on issue of equity	35.3	-1.6	0.0
Cash flows from financing activities		**411.0**	**-9.1**
Effects of movements in exchange rates on cash and cash equivalents		-2.5	1.4
Other adjustments		-2.3	0.0
Net changes in cash and cash equivalents		**508.1**	**-90.2**
Cash and cash equivalents			
Cash and cash equivalents on January 1st		**137.4**	**227.5**
Cash and cash equivalents on December 31st		**645.5**	**137.4**

The following disclosures in the notes are an integral part of these consolidated financial statements.

Consolidated statement of changes in equity

in € million	Share capital	Capital reserve	Retained earnings	Other reserves: Remea-surement of pensions	Other reserves: Cash flow hedge	Other reserves: Currency translation	Treasury shares	Subtotal	Non-controlling interests	Equity
As of Jan 1, 2019	**0.03**	**46.3**	**-220.7**	**0.6**	**-3.4**	**-9.4**	**-10.6**	**-197.2**	**10.9**	**-186.3**
Group Result	-	-	5.9	-	-	-	-	**5.9**	2.3	**8.2**
Other comprehensive income	-	-	-	-39.9	-0.7	3.0	-	**-37.5**	0.5	**-37.0**
Total comprehensive income	**-**	**-**	**5.9**	**-39.9**	**-0.7**	**3.0**	**-**	**-31.6**	**2.8**	**-28.8**
Contribution of shareholder loan	-	371.0	-	-	-	-	-	**371.0**	-	**371.0**
Cancellation of treasury shares	-	-10.6	-	-	-	-	10.6	**-**	-	**-**
Adjustement from reorganization	10.0	-10.0	-	-	-	-	-	**0.0**	-	**0.0**
Addition from business combinations	-	-	-	-	-	-	-	**-**	0.6	**0.6**
Dividends on non-controlling interests	-	-	-	-	-	-	-	**-**	-0.2	**-0.2**
Other	-	-	-1.0	-	-	-	-	**-1.0**	-0.4	**-1.5**
As of Dec. 31, 2019	**10.0**	**396.7**	**-215.8**	**-39.3**	**-4.1**	**-6.4**	**-**	**141.2**	**13.6**	**154.8**
Group Result	-	-	-65.2	-	-	-	-	**-65.2**	0.7	**-64.5**
Other comprehensive income	-	-	-	-27.4	-0.5	-8.6	-	**-36.5**	-1.4	**-37.9**
Total comprehensive income	**-**	**-**	**-65.2**	**-27.4**	**-0.5**	**-8.6**	**-**	**-101.8**	**-0.7**	**-102.4**
Issue of share capital from own funds	70.0	-70.0	-	-	-	-	-	**-**	**-**	**-**
Issue of share capital from IPO	25.0	275.0	-	-	-	-	-	**300.0**	**-**	**300.0**
Transaction costs	-	-4.9	-	-	-	-	-	**-4.9**	**-**	**-4.9**
Dividends on non-controlling interests	-	-	-	-	-	-	-	**-**	**-0.2**	**-0.2**
Other	-	-	-0.7	-	-	-	-	**-0.7**	**0.2**	**-0.4**
As of Dec. 31, 2020	**105.0**	**596.8**	**-281.6**	**-66.7**	**-4.7**	**-15.0**	**-**	**333.9**	**12.9**	**346.8**

The following disclosures in the notes are an integral part of these consolidated financial statements.

Notes to the consolidated financial statements

I. Basis of presentation

1. The Company

These IFRS consolidated financial statements comprise HENSOLDT AG (the "Company") with its registered office at Willy-Messerschmitt-Str. 3, 82024 Taufkirchen, Germany, under HRB 258711, Munich District Court and its subsidiaries (the "Group", "HENSOLDT" or "HENSOLDT Group").

The fiscal year is the calendar year.

The HENSOLDT Group is a multinational business in the defense and security electronics market with its headquarters based in Germany. The main product portfolio ranges from radars, to electronic warfare and avionics, to optical and optronic equipment.

The consolidated financial statements of HENSOLDT AG are included in the financial statements of Square Lux TopCo S.à r.l., Luxembourg. Square Lux TopCo S.à r.l., Luxembourg prepares the consolidated financial statements for the smallest and largest group of companies. The registered office of Square Lux TopCo S.à r.l. is located at 2, Rue Edward Steichen, 2450 Luxembourg, and registered with the Registre de Commerce et des Sociétés under number B204231.

2. Significant accounting policies

2.1. Basis of preparation

As a listed company, HENSOLDT AG has prepared its consolidated financial statements in accordance with section 315e para. 1 of the German Commercial Code (HGB) ("consolidated financial statements in accordance with International Financial Reporting Standards") in compliance with International Financial Reporting Standards (IFRSs) and related interpretations of the International Accounting Standards Board (IASB) as adopted by the European Union in accordance with Regulation (EC) No 1606 / 2002 of the European Parliament and of the European Council on the application of international accounting standards.

Changes in important accounting policies are described in Note 4.

These consolidated financial statements were approved by the Management Board for distribution to the Supervisory Board on March 8, 2021.

The consolidated financial statements are presented in euros (€), which is the Group's functional currency. Unless otherwise stated, all financial figures are rounded to the nearest hundred thousand.

These consolidated financial statements were prepared based on the assumption of the Group's continuation as a going concern.

Unless otherwise stated, the consolidated financial statements have been prepared on a historical cost basis. The principal accounting policies are set out below.

2.2. Basis of consolidation

Business combinations

The Group accounts for business combinations using the acquisition method if the acquired group of activities and assets meets the definition of a business and control is transferred to the Group. The consideration transferred for the acquisition and the identifiable assets acquired are generally recognized at fair value. In determining whether a particular group of activities and assets is a business, HENSOLDT assesses whether the group of acquired assets and activities includes at a minimum, an input and substantive process and whether the acquired group is capable of generating output. Any goodwill that arises is tested for impairment annually. Any gain on a bargain purchase is recognized directly in the consolidated income statement. Transaction costs are expensed as incurred unless they are related to the issue of debt or equity securities.

The consideration transferred does not include amounts related to the settlement of pre-existing relationships. Such amounts are generally recognized in the consolidated income statement.

Any contingent consideration is measured at fair value as of the acquisition date. If the contingent consideration is classified as equity, it is not remeasured and any settlement is recognized in equity. Otherwise, other contingent considerations are measured at fair value on the reporting date and subsequent changes in the fair value of the contingent considerations are recognized in the consolidated statement of comprehensive income.

Subsidiaries

Subsidiaries are companies controlled by the Group. The Group controls a company when it is exposed to or has rights to variable returns from its involvement with the company and has the ability to affect those returns through its power over the company. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

Non-controlling interests

Non-controlling interests are valued at the date of acquisition at the relevant share in the acquired company's identifiable net assets.

Changes in the Group's interest in a subsidiary that do not result in a loss of control are accounted for as equity transactions.

If the Company is obligated to buy back shares of external shareholders due to written put-options, the potential purchase price liability according to contractual provisions is recognized at fair value as of the reporting date in other liabilities. Changes in the market value are recognized in the consolidated income statement.

Investments accounted for using the equity method

Interests of the Group accounted for using the equity method include interests in associates and joint ventures.

Associates are companies in which the Group has a significant influence, but not control or joint control in respect to financial and business policies. A joint venture is an arrangement, over which the Group exercises joint control and in which it has rights to the net assets of the arrangement rather than rights to its assets and obligations for its liabilities.

Investments in associates and joint ventures are accounted for using the equity method. They are initially recognized at cost, which also includes transaction costs. After initial recognition, the consolidated financial statements contain the Group's share in the total comprehensive income of the equity-accounted investee until the date at which significant influence or joint management ends. If the losses of an associate or joint venture attributable to HENSOLDT equal or exceed the value of its interest in such entity, no further share of losses is recognized unless HENSOLDT has incurred obligations or made payments on behalf of the entity. The interest in an associate or joint venture is the carrying amount of the investment plus any financial assets that are, in substance, attributable to HENSOLD's net investment in the entity such as a loan.

Consolidation of intercompany transactions

Intra-group balances and transactions, and any unrealized income and expenses arising from intra-group transactions, are eliminated. Unrealized gains on transactions with equity-accounted investees are derecognized against the investment according to the Group's share in the investment. Unrealized losses are eliminated in the same way as unrealized gains, but only if there are no indications of impairment.

2.3. Revenue from contracts with customers

Revenue recognition

The Group recognizes revenue if the control over distinct goods and services transfers to the customer, i.e. when the customer is able to determine the use of the transferred goods or services and to primarily obtain the remaining benefits therefrom. Precondition in this respect is that a contract with enforceable rights and obligations is in place and, inter alia, recovery of the consideration, taking account of the credit rating of the customer, is probable.

Revenue equals the transaction price to which the HENSOLDT Group expects to be entitled to under the relevant contract. Variable considerations (such as price escalations, contractual penalties, revisions following price audits) are reflected in the transaction price if it is highly probable that such variable consideration may be collected or when the uncertainty associated with such variable consideration no longer exists. The amount of the variable consideration is determined either according to the expected value method or using the most likely amount, depending on which method better predicts the variable consideration.

If a contract comprises several distinct goods or services, the transaction price is allocated to the performance obligation based on the relative stand-alone selling price. If stand-alone selling prices are not directly observable, the Group estimates these in an appropriate amount. If no observable prices exist, particularly as the goods and services offered by HENSOLDT are highly complex and individual, the stand-alone selling price of each separate performance obligation is estimated based on the expected costs plus a margin. This procedure is also regularly utilized in the pricing process during contract negotiations.

When the Group transfers control of goods produced or services rendered to the customer over time, revenue is recognized over time, if one of the following criteria is met:

- The customer simultaneously receives and consumes the benefits provided by the Group (e.g. maintenance contracts, training services);
- It creates a good which is controlled by the customer as the good is created or enhanced (e.g. work in progress); or

- It produces a good with no alternative use and the Group has an enforceable right to payment (including a reasonable margin) for the work completed to date, in the event of contract termination at the convenience of customers.

For each performance obligation to be satisfied over time pursuant to IFRS 15, the HENSOLDT Group recognizes revenue over time by determining the progress towards complete satisfaction of that performance obligation. The HENSOLDT Group applies one single method to determine the progress for each performance obligation to be satisfied over time, with the selected method being consistently applied to similar performance obligations and similar circumstances. The measurement of progress towards complete satisfaction of a performance obligation is based either on inputs or outputs. When progress is measured by inputs, the cost-to-cost method is used. HENSOLDT uses this method as it, by the Group's view, best reflects the progress towards the satisfaction of the performance obligation. If costs are incurred that do not contribute to the progress of the satisfaction of the performance obligation, such as unplanned scrapping costs, or costs incurred that are disproportionate to the measurement of progress due to unexpected additional costs, these costs are excluded from the measurement of progress or, alternatively, the originally budgeted amount is revised.

If none of the abovementioned criteria for recognizing revenue over time are met, revenue is recognized at a point in time, i.e. the point in time when HENSOLDT has transferred control of the asset to the customer. Generally, this is the point in time of the delivery of the goods or upon acceptance of the goods or services by the customer.

Performance obligations

The following section sets forth the significant performance obligations from contracts with customers and elaborates on the nature and timing of the satisfaction of the performance obligations, including significant payment terms, and the related revenue recognition policies.

Standardized products and systems with limited customization

When manufacturing and installing standardized products and systems or delivering spare parts, customer-specific adjustments are only made to a limited extent. Customers obtain control of standardized products when the goods have been delivered and accepted at their premises Invoices are generated at that point in time. Pursuant to the contractual terms, invoices are usually payable between 30 and 60 days. Depending on the contractual terms and conditions revenue is recognized either once the goods are delivered or once the goods are accepted by the customers at their premises.

Customized development, manufacture and supply of products and systems

Generally, HENSOLDT does not have an alternative use for products and systems for which the development or manufacturing is highly customized. If a contract is terminated by the customer, HENSOLDT is generally entitled to reimbursement of the costs incurred up to that point, including an appropriate margin. Invoices are issued in accordance with the contractual terms and are generally payable between 30 and 60 days. Revenue and associated costs are recognized over time. Progress is determined by applying the cost-to-cost method. Amounts for performance obligations satisfied but not yet invoiced are presented as contract assets, and payments received in advance of satisfying the performance obligations are presented as contract liabilities.

Service and support

The Group provides, among others, maintenance and training services. The customer simultaneously receives and consumes the benefits provided by HENSOLDT's performance as HENSOLDT provides the services. Invoices are issued in accordance with the contractual terms and are generally payable between 30 and 60 days. Revenue and associated costs are mainly recognized over time. Progress is determined based on the cost-to-cost method. Amounts for performance obligations satisfied but not yet invoiced are presented as contract assets, and payments received in advance of satisfying the performance obligations are presented as contract liabilities.

Variable components

All of the abovementioned performance obligations of HENSOLDT may include variable consideration components. HENSOLDT's contracts with customers may include the following variable consideration components: price adjustments from escalations, price audits and contractual penalties. For contracts with variable consideration components, revenue is recognized to the extent that it is highly probable that a significant reversal of the amount of cumulatively recognized revenue will not be required. Accordingly, positive variable consideration components (e.g., price escalations) are recognized as an increase of the transaction price if there is an estimated probability of at least 80% that they will be realized. Conversely, negative variable consideration components (e.g. contractual penalties or price audit reimbursements) are recognized as a reduction of the transaction price if they occur with an estimated probability of 20% or more.

Contract assets, contract liabilities and trade receivables

If one of the contract parties has met its contractual obligations, depending on whether or not the HENSOLDT Group has performed its contractual obligations or the customer has paid the agreed consideration at the same time, a contract asset, contract liabilities or a receivable is recognized.

If HENSOLDT satisfies its contractual obligations by transferring goods and services to a customer but before the customer pays a consideration or is required to pay pursuant to the contractual terms, the Group recognizes a contract asset to the amount of the satisfied performance less any amounts recognized as receivable.

A receivable is recognized if an amount of consideration that is unconditional is due from the customer (i.e., only the passage of time is required before payment of the consideration is due).

A contract liability is recognized if a payment is received or a payment is due (whichever is earlier) from a customer before the Group transfers the related goods or services. Contract liabilities are recognized as revenue when the Group fulfills its performance obligation under the contract (i.e., transfers control of the related goods or services to the customer).

2.4. Intangible assets and goodwill

Intangible assets

Intangible assets with limited useful lives are generally amortized on a straight-line basis over their respective expected useful lives to their estimated residual values. In general, the expected useful life for patents, licenses and similar rights is between 3 to 5 years, with the exception of intangible assets with finite useful lives acquired in business combinations. These consist in particular of order backlogs and customer relationships as well as technologies. The useful lives of these intangible assets, in certain transactions, ranged from 2 to 11 years for order backlogs and between 8 to 10 years for customer relationships, as well as from 3 to 12 years for technologies. Brands with indefinite useful lives are not amortized but tested for impairment annually. The brand HENSOLDT is to be used in the long term and the Group intends to operate on the market under the name HENSOLDT for an unlimited amount of time. There is no indication of a limited useful life to the brand or indications as to the period on which a time limit could exist. Amortization costs for intangible assets are recognized as a part of cost of sales.

Goodwill

Goodwill arising from business combinations is measured at cost less accumulated impairment losses. Goodwill is tested for impairment annually or if an objective indication of impairment exists. For the purpose of impairment testing, goodwill acquired in a business combination is, starting from the acquisition date, allocated to the Group's cash generating units (CGUs) that are expected to benefit from the combination. This applies irrespective of whether other assets or liabilities of the entity acquired are assigned to these CGUs.

Research and development

Research costs are recognized in the consolidated income statement as incurred.

Development costs are capitalized if they can be reliably estimated, the product or process is technically and commercially feasible, future benefit is probable and the Group intends and has sufficient resources to be able to complete development and use or sell the asset.

Development activities are usually carried out in a phased approach. In this phased approach the Group generally assumes that the criteria for recognition under IAS 38 are satisfied if the Preliminary Design Review (PDR: for established technologies) or Critical Design Review (CDR: for new technologies) was successfully completed.

Other development expenditure is recognized in the consolidated income statement as research and development costs as soon as it is incurred. Capitalized development expenditure is measured at cost less accumulated amortization and accumulated impairment losses. The Company reviews capitalized development for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. In addition, intangible assets not yet available for use are subject to an annual impairment test. Impairment testing of other intangible assets involves the use of estimates in determining the assets' recoverable amount which can have a material impact on the respective values and ultimately the amount of any impairment. Capitalized development expenditure is generally amortized on a straight-line-basis over the estimated useful life (between 5 and 7 years) of the internally generated intangible asset. Amortization and impairment losses of the capitalized development expenditure is recognized under cost of sales.

2.5. Property, plant and equipment

Property, plant and equipment are measured at cost less accumulated depreciation and impairment losses. Property, plant and equipment are depreciated on a straight-line basis. The following useful lives have been assumed:

Buildings	betw een	5 and 50 years
Technical equiptment and machinery	betw een	4 and 10 years
Other equipment, opearting and office equipment	betw een	3 and 13 years

2.6. Inventories

Inventories are measured at the lower of cost (generally the average cost) and net realizable value. Net realizable value is the estimated selling price in the ordinary course of business, less the estimated costs of to sell.

Manufacturing costs include all costs directly attributable to the manufacturing process, such as material costs, wage and production-related overheads (based on normal operating capacity and normal use of materials, labor and other production costs) including write-downs. If any inventory risks exist, e.g. due to reduced usability after longer storage periods or lower replacement costs, appropriate write-downs are recognized. Write-downs on inventories are recognized when it is probable that projected contract costs will exceed total contract revenue.

2.7. Leases

The Group only substantially engages in lease activities as a lessee. The Group leases many assets including property, technical equipment, IT equipment and vehicles.

At inception of a contract, the Group assesses whether a contract is or contains a lease. A contract is or contains a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration.

At commencement or on modification of a contract that contains a lease component, the Group allocates the consideration in the contract to each lease component on the basis of its stand-alone price. This policy applies to lease contracts concerning buildings. Due to materiality, the Group has elected not to separate non-lease components for all other classes of lease contracts.

The Group recognizes a right-of-use asset and a lease liability at the lease commencement date. The right-of-use asset is initially measured at cost, which comprises the initial amount of the lease liability adjusted for any lease payments made at or before the commencement date, plus any initial direct costs incurred and an estimate of costs to dismantle and remove the underlying asset or to restore the underlying asset or the site on which it is located, less any lease incentives received.

The right-of-use asset is subsequently depreciated using the straight-line method from the commencement date to the earlier of the end of the useful life of the right-of-use asset or the end of the lease term. The estimated useful lives of right-of-use assets are determined on the same basis as those of property and equipment. In addition, the right-of-use asset is periodically reduced by impairment losses, if any, and adjusted for certain remeasurements of the lease liability.

The lease liability is initially measured at the present value of the lease payments that are not paid at the commencement date, discounted using the interest rate implicit in the lease or, if that rate cannot be readily determined, the Group’s incremental borrowing rate. Generally, the Group uses its incremental borrowing rate as the discount rate. The Group determines its incremental borrowing rate by obtaining interest rates from various external financing sources and makes certain adjustments to reflect the terms of the lease. Country specific interest rates are used in South Africa.

Lease payments included in the measurement of the lease liability comprise the following:

- Fixed payments, including in-substance fixed payments;
- Variable lease payments that depend on an index or a rate, initially measured using the index or rate as at the commencement date;
- Lease payments in an optional renewal period if the Group is reasonably certain to exercise an extension option, and penalties for early termination of a lease unless the Group is reasonably certain not to terminate early.

The lease liability is measured at amortized cost using the effective interest method. It is remeasured when there is a change in future lease payments arising from a change in an index or rate, if there is a change in the Group’s estimate of the amount expected to be payable under a residual value guarantee, or if the Group changes its assessment of whether it will exercise a purchase, extension or termination option. When the lease liability is remeasured, a corresponding adjustment is made to the carrying amount of the right-of-use asset or is recorded in the consolidated income statement if the carrying amount of the right-of-use asset has been reduced to zero.

The Group presents right-of-use assets and lease liabilities as a separate line item in the statement of financial position.

Short-term leases and leases of low-value assets

The Group does not recognize right-of-use assets and lease liabilities for short-term leases that have a lease term of 12 months or less and leases of low-value assets (e.g. office equipment). The Group recognizes the lease payments associated with these leases as an expense in the consolidated income statement on a straight-line basis over the lease term.

2.8. Employee benefits

Short-term employee benefits

Obligations under short-term employee benefits are measured as expenses as soon as the employees perform the work involved. A liability must be recognized for the amount to be paid if the Group currently has a legal or constructive obligation to pay this amount on the basis of work done by an employee and the obligation can be reliably estimated.

Defined contribution plans

Obligations for contributions to defined contribution plans are recognized as expenses as soon as the associated work is performed.

Defined benefit plans

The Group's net obligation for defined benefit plans is calculated separately for each plan by estimating the future benefits for which the employees have accrued entitlement in the current and in earlier periods. This amount is discounted and the estimated fair value of plan assets is then deducted from this.

The defined benefit obligations are calculated annually by a certified actuary using the projected unit credit method. If the calculation results in a potential asset for the Group, the recognized asset is limited to the present value of economic benefits available in the form of any future refunds from the plan or reductions in future contributions to the plan.

Remeasurements of the net defined benefit liability are recognized directly in other comprehensive income. Remeasurements of the net defined benefit liability comprise actuarial gains and losses and the return on plan assets (excluding interest). The Group determines the net interest expense (income) on the net defined benefit liability (plan asset) for the reporting period by applying the discount rate used to measure the defined benefit obligation at the beginning of the annual reporting period. This discount rate is applied to the net defined benefit liability (asset) on that date. Any changes to the net defined benefit liability (asset) due to payment of contributions or benefits during the reporting period are taken into account. Net interest and other expenses relating to defined benefit plans are recognized in the consolidated income statement.

If a plan amendment or curtailment occurs, any past service cost resulting from a plan amendment or gain or loss on curtailment is recognized directly in the consolidated income statement in the finance result.

Other long-term employee benefits

The Group's net obligations for other long-term employee benefits are the future payments due to employees in exchange for services provided during employment in the current and in earlier periods. These payments are discounted to present value. Remeasurements are recognized in the consolidated income statement in the period in which they occur.

2.9. Other provisions

Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability. The unwinding of the discount is presented as finance cost.

Provision for onerous contracts

The Group recognized provisions for onerous contracts if it is probable that total contract costs will exceed the total contract revenue. The provision is measured at the lower amount of expected costs for terminating the contract and the expected net costs from performing the contract. Before a provision for onerous contracts is recognized, the associated inventories are written off.

Onerous sales contracts are identified by monitoring the progress of the contract and the underlying project and by updating the estimate of contract costs, which involves significant and complex assumptions, assessments and estimates in connection with obtaining a certain performance standard and estimates relating to other costs (see Note 3, Note III.11 and Note IV.23).

Warranties

A provision for warranties is recognized when the underlying products or services are sold or rendered and a contractual or constructive obligation exists to repair damage to sold products within a certain period at the Company’s expense. A warranty case can only occur after the performance obligation has been satisfied. To this extent, such costs have no influence on the measurement of progress in the fulfillment of the performance obligation. The provision is based on the individual assessment of future costs to be incurred. Recognition takes place pro-rata based on certain criteria, such as, for example, delivered products or a certain project progress.

If the warranty is classified as a separate service, a separate performance obligation is identified for the warranty.

2.10. Financial instruments

Recognition and initial measurement

The Group recognizes trade receivables from the date that they arise. All other financial assets and liabilities are recognized for the first time when the entity becomes a party according to the contractual provisions of the instrument.

A financial asset (except for a trade receivable without financing component) or a financial liability is measured at fair value on initial recognition. For an item which is not measured at fair value with changes through profit or loss (FVtPL), transaction costs are included that can be directly allocated to its acquisition or issuance. Trade receivables without a significant financing component are measured at their transaction price on initial recognition.

Classification and subsequent measurement

Financial assets

For initial recognition, financial assets are classified and measured based on the business model (under which the assets are held) and the characteristics of their cash flows.

Financial assets are not reclassified after initial recognition unless the Group changes its business model to manage financial assets.

The Group classifies its financial assets into the following measurement categories:

- "measured at amortized cost" (AC)
- "at fair value with changes through profit or loss" (FVtPL) and
- "at fair value through other comprehensive income" (FVtOCI).

A financial asset is measured at amortized cost if it meets both of the following conditions and is not designated as FVtPL:

- The financial asset is held within a business model whose objective is to hold the financial asset to collect the contractual cash flows, and
- The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

A debt instrument is designated at FVtOCI if both of the following conditions are met and it was not designated at FVtPL:

- The financial asset is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets; and
- The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

Trade receivables are generally allocated to the "held to collect" business model and measured at amortized cost, i.e. in subsequent periods receivables are recognized net of principal repayments, installments and impairment losses, plus any reversals of impairment losses. Receivables that are meant to be sold to a factoring party, are held in a business model “held to collect and sale”. These receivables are measured at fair value. At initial recognition of an equity instrument that is not held for trading, the Group can irrevocably elect to present subsequent value changes of the investment in other comprehensive income. This option is generally exercised within the group. All financial assets that are not measured at amortized cost or at FVtOCI are measured at FVtPL. This includes all derivative financial assets (see Note VI.36).

At initial recognition the Group can irrevocably elect to designate financial assets, which meet the conditions for measurements at amortized cost or at FVtOCI, at FVtPL if measurement and recognition inconsistencies (accounting mismatch) that arise are being eliminated or significantly reduced.

Financial assets at FVtPL: These assets are subsequently measured at fair value. Net gains and losses, inclusive of any interest and dividend income, are recognized in the consolidated income statement. For derivatives designated as hedging instruments in an effective hedge, see Note VI.36.

Financial assets at amortized cost: These assets are measured at amortized cost using the effective interest method. Amortized cost is diminished by impairment losses. Interest income, foreign exchange gains and losses as well as impairment losses are recognized in consolidated income statement. A gain or loss arising from derecognition is recognized in the consolidated income statement. The impairment requirements on financial assets are described in Note 2.14.

Certain equity investments, especially immaterial other investments or interests in joint ventures or associates that are not consolidated using the at-equity method due to materiality, are measured at cost.

Debt instruments at FVtOCI: These assets are subsequently measured at fair value. Interest income, which is calculated using the effective interest method, foreign exchange gains and losses as well as impairment losses are recognized in the consolidated income statement. Other net gains or losses are recognized in other comprehensive income. For derecognition, the accumulated other comprehensive income is reclassified to consolidated income statement.

Equity instruments at FVtOCI: These assets are subsequently measured at fair value. Dividends are recognized as income in the consolidated income statement unless the dividends clearly represent cover of a part of costs of the investment. Other net gains or losses are recognized in other comprehensive income and are never reclassified to the consolidated income statement.

Financial liabilities

Financial liabilities are classified and measured at amortized cost or at FVtPL. A financial liability is classified at FVtPL if it is classified as held for trading, is a derivative or is designated as such on initial recognition.

Other financial liabilities are subsequently measured at amortized cost using the effective interest method. Interest expenses and foreign currency translation differences are recognized in the consolidated income statement. Gains or losses arising from derecognition are recognized in the consolidated income statement

Derecognition

The Group derecognizes a financial asset when the contractual rights to receive the cash flows of an asset expire or it transfers the rights to receive the cash flows in a transaction in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred or in which the group neither transfers nor retains substantially all of the risks and rewards of ownership and it does not retain control of the financial asset.

The Group sells trade receivables with a minimum amount of €100.0 thousand on a case-by-case basis, applying multiple criteria, to external factoring parties. In this process, the Group determines whether the risk and rewards of ownership of the financial asset are fully transferred. Subsequently, the financial asset is derecognized and the Group assesses whether a continuing involvement exists and if so, a corresponding item must be recognized.

Financial liabilities are derecognized when the contractual obligations are discharged, canceled or expire. The Group also derecognizes a financial liability if its contractual terms are changed and the cash flows of the adjusted liability differ significantly. In this case a new financial liability based on the adjusted terms is recognized at fair value.

On derecognition of a financial liability, the difference between the carrying amount of the settled liability and the consideration paid (including transferred non-cash assets or assumed liabilities) is recognized in the consolidated income statement.

Netting

Financial assets and liabilities are offset and the net amount is presented in the statement of financial position when the Group has a current, legally enforceable right to offset the amounts and intends either to settle them on a net basis, or to realize the asset and settle the related liability simultaneously.

Derivative financial instruments and hedge accounting

Derivative financial instruments

The HENSOLDT Group carries out some of its transactions in foreign currency, such as customer or supplier contracts. HENSOLDT enters into forward exchange transactions and commits to purchases and sales in corresponding foreign currencies to limit the risks to income and costs from currency fluctuations.

In addition, the HENSOLDT Group is exposed to interest rate risk stemming from its Term Loan with variable interest rate; the risk is hedged by use of interest rate swaps. Derivate contracts to mitigate foreign exchange risks and interest rate risk are concluded with different banks.

Derivatives are measured at fair value on initial recognition; attributable transaction costs are recognized in the consolidated income statement when incurred. For the purposes of subsequent measurement, derivatives are measured at FVtPL. Embedded derivatives are separated from the host contract and accounted for separately if the host contract is not a financial asset and certain criteria are met.

Hedge accounting ensures that derivative gains or losses are recorded through profit or loss (primarily as a part of revenue) in the same period in which the hedged items or transactions are recognized through profit or loss. By contrast, changes in the value of derivative contracts are recognized in total comprehensive income if the hedged items or transactions have not yet been recognized in the consolidated income statement.

At the inception of the designated hedge, the Group documents the risk management objectives and strategies that it is pursuing in respect of hedging. The Group also documents the financial relationship between the hedged item and the hedging instrument and whether there is an expectation that the changes in cash flows of the hedged item and the hedging instrument will offset each other.

For the purpose of assessing whether there is an economic relationship between the hedged items and the hedging instruments, the Group assumes that the reference interest rate will not change as a result of the reform of the interest rate benchmark.

The Group continues to apply the existing accounting policies of IAS 39 for hedging transactions.

The fair value of derivative financial instruments, that are designated in a hedge accounting relationship as well as the development of the hedging reserve are shown in Note VI.36.3.

Cash flow hedges

If a derivative is designated as a cash flow hedging instrument, the effective portion of changes in the fair value is recognized in other comprehensive income and the cumulative change is transferred to the hedging reserve. Any ineffective portion of changes in fair value of the derivative is recognized in the consolidated income statement. For all other hedged forecast transactions, the accumulated amount, which was transferred to the hedging reserve, is reclassified in the consolidated income statement in the period or periods in which the hedged forecast future cash flows affect the consolidated income statement.

If the hedge no longer meets the criteria for hedge accounting or the hedging instrument is sold, expires, terminated or exercised, then hedge accounting is discontinued prospectively. If the hedged future cash flows are no longer forecast, the amounts that were transferred to the hedging reserve are directly reclassified in the consolidated income statement.

2.11. Income tax

Income tax expense comprises current and deferred taxes.

Current Taxes

Current taxes comprises the expected tax payable or receivable on the taxable income or loss for the year and any adjustment to the tax payable or receivable in respect of previous years. The amount of current tax payable or receivable is the best estimate of the tax amount expected to be paid or received that reflects uncertainty related to income taxes, if any. It is measured using tax rates enacted or substantively enacted at the reporting date. Current tax also includes any tax arising from the assesment of dividends.

Current tax assets and liabilities are offset if there is a legally enforceable right to offset current tax assets against current tax liabilities and the current taxes relate to the same taxable entity and the same tax authority.

Deferred taxes

Applying the liability method of IAS 12, deferred taxes are calculated on the basis of temporary differences between the tax and financial reporting valuation approaches including differences from consolidation, loss and interest carryforwards as well as tax credits. The calculation uses the tax rates that are expected to apply to the period when the asset is realized or the liability is settled. The amount is calculated on the basis of the tax rates and tax laws applicable as of the reporting date or will be applicable in the near future.

Deferred tax liabilities are recognized for all taxable temporary differences, with the exception of:

- the initial recognition of goodwill; or
- an asset or liability from a transaction which is not a business combination and at the date of the transaction affects neither the income (loss) for the period nor taxable profit (taxable loss), or
- all taxable temporary differences associated with investments in subsidiaries, associates, interests in joint ventures, where HENSOLDT is able to control the timing of the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future.

The carrying amount of deferred tax assets is reviewed at each reporting date and reduced to the extent that it is no longer likely that sufficient taxable earnings will be available against which the deferred tax asset could be offset. Deferred tax assets that are not recognized are reviewed at each reporting date and recognized to the extent to which it has become likely that future taxable earnings will permit the realization of the deferred tax asset. Each uncertain tax treatment is considered individually or together as a group, depending on which approach better predicted the resolution of the uncertainty. The entity uses either the most likely amount or the expected value method to measure such uncertainty. The decision is based on which method better predicts the resolution of the uncertainty.

Deferred taxes relating to items recognized directly in equity are also posted directly in equity. Deferred taxes are recognized either in other comprehensive income or directly in equity, depending on the underlying business transaction involved.

Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current taxes assets against current tax liabilities and the deferred taxes relate to the same taxable entity and the same taxation authority.

2.12. Foreign currency

Foreign currency transactions

Transactions in foreign currencies are translated into the respective functional currencies of Group companies at the exchange rates at the dates of the transactions.

Monetary assets and liabilities denominated in foreign currencies are translated into the functional currency at the exchange rate at the reporting date. Non-monetary assets and liabilities that are measured at fair value in a foreign currency are translated into the functional currency at the exchange rate when the fair value was determined. Non-monetary items that are measured based on historical cost in a foreign currency are translated at the exchange rates at the date of the transaction. Foreign currency differences are generally recognized in the consolidated income statement presented as finance costs.

However, foreign currency differences arising from the translation of the following items are recognized in OCI:

- An investment in equity securities designated at FVtOCI (except on impairment, in which case foreign currency differences that have been recognized in OCI are reclassified to the consolidated income statement);
- A financial liability designated as a hedge of the net investment in a foreign operation to the extent that the hedge is effective; and
- Qualifying cash flow hedges to the extent that the hedges are effective.

Foreign operations

The assets and liabilities of foreign operations, including goodwill and fair value adjustments arising on acquisition are translated into euros at the exchange rates at the reporting date. Income and expenses of foreign operations are translated into euros at yearly average exchange rates. Foreign currency differences are recognized in OCI and accumulated in the translation reserve, except to the extent that the translation difference is allocated to non-controlling interests.

2.13. Statement of cash flows

Under the indirect determination of cash flow, the changes in items in the statement of financial position related to operating activities are adjusted by currency translation effects and by changes in the scope of consolidation. For this reason, they cannot be directly reconciled with the relevant changes on the basis of the published consolidated statement of financial position.

2.14. Impairment

Non-derivative financial assets

The Group recognizes allowances for expected credit losses (ECL) for:

- financial assets at amortized cost

- contract assets

HENSOLDT measures its impairment allowances on trade receivables and contract assets using the simplified approach. In accordance with the simplified approach, the Company shall measure the loss allowance at an amount equal to lifetime expected credit losses. Consequently, no review is required as to whether a significant increase in credit risk occurred requiring a transfer from Level 1 to Level 2.

For all other financial assets within the scope of IFRS 9 impairment requirements, no allowance for impairment losses is recognized for reasons of materiality. This assumption is reviewed on a regular basis.

To assess whether the credit risk of a financial asset since initial recognition has significantly increased and for the assessment of expected credit losses, the Group considers reasonable and supportable information which is relevant and available without undue cost or effort. This covers both quantitative and qualitative information and analysis, which is based on past experience of the Group and in-depth assessments, inclusive of forward-looking information. If there are objective indications of impairment, interest income must also be recognized on the basis of the net carrying amount (carrying amount less allowance for losses on loans and advances) (Level 3).

Presentation of impairment for expected credit losses in the statement of financial position

Impairment losses on financial assets measured at amortized cost are deducted from the gross carrying amount of the assets.

Credit impaired financial assets

At each reporting date, the Group assesses whether financial assets measured at amortized cost are credit-impaired. A financial asset is credit-impaired if one or more events occurs which has adverse effects on the expected future cash flows of the financial asset.

Indicators that a financial asset is credit-impaired include the following observable data:

- significant financial difficulty of the issuer or the borrower,
- a breach of contract, such as a default or past-due situation of more than 90 days, or
- it is probable that the borrower will become insolvent or enter into other bankruptcy proceedings.

Write-off

The gross carrying amount of a financial asset is written off when according to an appropriate assessment the Group has no reasonable expectations that the financial asset can be partly or wholly realized.

Non-financial assets

At the end of each reporting period the Group assesses whether there is an indication of impairment of a non-financial asset or a CGU to which the asset belongs (e.g. changes in the legal framework, introduction of new technology, etc.). In addition, intangible assets with indefinite useful lives, intangible assets not yet available for use as well as goodwill are tested for impairment in the fourth quarter of each fiscal year, regardless of whether there are any indications of impairment. For impairment testing, goodwill is allocated to a CGU or group of CGUs to thus reflect the manner in which goodwill is monitored for internal management purposes.

To determine if an impairment has occurred, assets are combined into the smallest group of assets that generate cash inflows from continuing use and are largely independent from the cash inflows of other assets or CGUs. Goodwill acquired from a business combination is allocated to the CGUs or groups of CGUs which are expected to benefit from the synergies of the combination. This applies irrespective of whether other assets or liabilities of the entity acquired are assigned to these CGUs.

The recoverable amount of an asset or CGU is the higher of its value in use and its fair value less costs to sell. To assess the value in use, the estimated future cash flows are discounted to their present value using a discount rate that reflects the present market assessment of the time value of money and the specific risks relating to an asset or a CGU.

Impairment exists when the carrying amount of an asset or CGU exceeds its recoverable amount. The recoverable amount of an asset or CGU is the higher of its fair value less costs to sell and its value in use. The calculation of fair value less costs to sell is based on available data from binding sale transactions for similar assets or observable market prices less directly attributable costs to sell the asset. If insufficient information is available to determine the fair value less costs to sell of an asset or CGU, the value in use of the asset or CGU is used instead.

Impairment losses are recognized in the consolidated income statement. Impairment losses recognized on CGUs are allocated first to any goodwill allocated to the CGU, and then to the carrying amounts of the other assets of the CGU (group of CGUs) on a pro rata basis.

An impairment loss on goodwill cannot be reversed. Impairment losses on other assets can only be reversed to the extent that the carrying amount of the asset does not exceed the carrying amount that, less depreciation or amortization, would have been determined if no impairment had been recognized.

2.15. Fair value measurement

A number of the Group's accounting policies and disclosures require the measurement of fair values for both financial and non-financial assets and liabilities.

The fair value is the price at which an asset would be sold or a liability transferred under current market conditions on the measurement date in an orderly transaction on the primary market or, if such a market is not available, the most advantageous market to which the Group has access at this point in time. The fair value of a liability reflects the non-performance risk.

The Group uses the following hierarchy to determine and present fair value of the financial instruments for each valuation method:

- Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities
- Level 2: Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly
- Level 3: Methods by which input parameters that substantially impact the fair value determination are not based on observable market data

If an asset or liability measured at fair value has a bid or ask price, then the Group measures assets or long positions at the bid price and liabilities and short positions at the ask price.

The best indication of the fair value at initial recognition of a financial instrument is generally the transaction price, i.e. the fair value of the consideration paid or received. If the Group determines that at initial recognition the fair value is different to the transaction price and the fair value is evidenced neither (a) by a quoted price in an active market for an identical asset or liability nor (b) based on a measurement technique for which all unobservable inputs can be considered insignificant in relation to the measurement, then this financial instrument is initially measured at fair value, adjusted to defer the difference between the fair value on initial recognition and the transaction price. Subsequently, this difference is recognized in the consolidated income statement on an appropriate basis over the life of the instrument, however no later than when the valuation is wholly supported by observable market data or the transaction is closed out.

The significant, non-observable input factors and the measurement adjustments are regularly reviewed. If information from third parties, such as price quotations from brokers or price information services, is used to determine the fair values, the evidence obtained from third parties is examined to determine whether such measurements fulfil the requirements of IFRS, including the classification in the fair value hierarchy.

The Group uses the following methods to determine the fair value:

Equity instruments

The fair value of unlisted equity instruments cannot be reliably determined, as the area of reasonable approximation of the fair value is decisive and the probabilities of the various estimates within the area cannot be appropriately assessed. With due consideration of materiality, these instruments are measured at cost and their carrying amounts are used in the place of fair value.

Assets from customer financing and other loans

The carrying amounts shown in the financial statements are used as rough estimates of the fair value.

Trade and other receivables, contract assets and other receivables

The carrying amounts shown in the financial statements are used as reasonable approximation of the fair value due to the relatively short period between the receivable arising and it falling due.

Cash and cash equivalents

Cash and cash equivalents comprises cash on hand, cash at bank and checks. The carrying amounts shown in the financial statements are used as reasonable approximation of the fair value due to the relatively short period between the instrument arising and its term or maturity.

Plan assets

Other investments include shares in a limited partnership (HENSOLDT Real Estate GmbH & Co. KG). The limited partnership essentially includes real estate assets, which are evaluated based on current market prices. The fair value of the plan assets represents a material part of the net assets of the limited partnership.

Pooled investment instruments include shares of investment funds, for which market prices are available.

Derivatives

The fair values of derivative instruments are based on quoted market prices where available but in most cases are determined using accepted measurement methods such as option pricing models and discounted cash flow models. Measurement is based on observable market data such as exchange rates, rates for forward exchange transactions, interest rates and yield curves.

The fair values of derivatives are measured on the basis of input parameters from Level 2.

Price determination for forward exchange transactions: the fair value is determined by using the quoted forward rate as of the reporting date and net present value calculations based on yield curves with high credit ratings in the relevant currencies.

Price determination for interest rate futures: the fair value is calculated as the present value of estimated future cash flows. Estimates of future cash flows from variable interest payments are based on quoted rates for interest rate futures, future prices and interbank interest rates. The estimated cash flows are discounted using a yield curve that was constructed from similar sources and reflects the relevant comparable interbank interest rate used by market participants for pricing the interest rate futures. The fair value estimate is adjusted for the credit risk which reflects the credit risk of the Group and the contracting party. This is calculated using credit spreads derived from credit default swap and bond prices.

Financial liabilities

The fair values recognized for financial liabilities, which are not bond or debt securities, are determined on the basis of input parameters from Level 2 in which planned or expected cash flows are discounted with corresponding market interest rates. The fair value of the written put option granted to minority shareholders is based on a discounted cash flow model using a 3-year business plan.

Trade payables, contract liabilities as well as current other financial liabilities

The carrying amounts of trade payables, contract liabilities and other current financial liabilities are seen as reasonable approximations of the fair value due to the relatively short period between the instrument arising and its maturity.

3. Key estimates and assessments

The preparation of the Group's consolidated financial statements requires management to make judgements, estimates and assumptions that affect the reported amounts of income, expenses, assets and liabilities, as well as the related disclosure of contingent liabilities. Uncertainty about these assumptions and estimates could result in outcomes that require a material adjustment to the carrying amount of assets or liabilities affected in future periods. Estimates and underlying assumptions are reviewed on an ongoing basis. Changes to estimates are recognized prospectively.

3.1. Revenue recognition over time

Revenue from the rendering of performance obligations over time is recognized using the percentage-of-completion method (Cost-to-Cost method). Under this method, exact estimates of contract results at the stage of completion and level of progress are necessary. To determine the progress of the contract the key estimates include total contract costs, the remaining costs until completion, the overall contract revenue and the contract risks.

Management regularly reviews all estimates used for these contracts and adjusts them as required (for more information please refer to Note 2.3).

3.2. Capitalization of development cost

When capitalizing development costs, the Group makes estimates regarding the development costs as well as estimates as to whether the product or the process is technically and commercially viable.

3.3. Assets acquired and liabilities assumed as well as goodwill

Measurement of the fair value of assets acquired and liabilities assumed in the course of company acquisitions, which form the basis of the measurement of goodwill, requires significant estimates. Land, buildings and machinery are usually measured independently while marketable securities are measured at market prices. If intangible assets are identified, based on the type of intangible asset and the complexity of determining its fair value, the Group consults either an independent external valuation expert or develops the fair value internally using suitable valuation techniques that are based in general on the forecast of total expected future net cash flows.

These measurements are closely related to management's assumptions regarding the future development of related assets and the discount rate to be applied.

3.4. Impairment testing

Please refer to Note 2.14 and Note IV.17.2 for further information on the significant estimates and judgments in regard to impairment testing.

3.5. Provisions

The measurement of provisions, e.g. for contract losses, warranties and arbitration or court proceedings, is based on best available estimates. Onerous contracts are determined by monitoring the progress of projects and updating estimates of contract costs or contract income, which also requires judgment in relation to reaching certain performance standards and estimates of guarantees and follow-up costs. The extent of the assumptions, assessments and estimates in these monitoring processes depends on the size and type of the Group's contracts and the associated projects.

3.6. Employee benefits

The Group recognizes pension and other retirement benefits in accordance with actuarial valuations. These valuations are based on statistical and other factors for anticipating future events. The assumptions can deviate significantly from actual developments due to changing market and economic conditions and thus lead to a significant change in employee benefits obligations and the related future costs (see Note V.32).

In addition to uncertainties arising from the assumptions of employees' future behavior when exercising the payout option, the Group is exposed to other actuarial uncertainties relating to defined benefits obligations, including the following:

Market risk

The market values of plan assets are subject to fluctuations which can impact the net defined benefit obligation.

Interest rate risk

The value of the defined benefit obligation and the plan assets is significantly affected by the discount rate used. In general, the defined benefit obligation is sensitive to movements in interest rates which leads to volatile results of the valuation.

Inflation risk

Defined benefit obligations can be sensitive to movements in the inflation rate, whereby a higher inflation rate could lead to an increase in the obligation. As some pension plans are directly tied to salary, pay increases can lead to an increase in pension obligations.

Longevity risk

Pension obligations are sensitive to the life expectancy of their beneficiaries. Increased life expectancy leads to an increase in the valuation of the pension obligation.

The weighted average assumptions for the most important pension plans used to calculate the actuarial value of the obligation as of December 31, are as follows:

	Pension plans in Germany	
	Dec. 31,	Dec. 31,
Assumptions in %	2020	2019
Discount rate	1.1%	1.4%
Wage increase rate (until age 36)	3.0%	3.0%
Wage increase rate (from age 36)	2.0%	2.0%
Inflation rate	1.0%	1.0%

For Germany the Group derives the discount rate used to determine defined benefits obligations from the yields for high quality corporate bonds. The discount rate for the estimated term of the respective pension plan is then extrapolated along the yield curve.

The pay increase rates are based on long-term expectations of the respective employer that are derived from the inflation rate assumed. Payments for pension growth rates are derived from the respective inflation rate for the plan.

The inflation rate for plans corresponds to the expected increase in the cost of living.

Moreover, an assumption is made as to what extent the employees choose a one-off payment, installment payment or pension when the benefit falls due. In light of the prolonged decline in interest rates in conjunction with no expected change to this trend in the foreseeable future and actual observed selection choices upon retirement since the creation of HENSOLDT, in the previous year, management has revised its demographic assumptions related to the behavior of beneficiaries under the German pension plan. This resulted in a significant increase in pension liability.

The calculation of pension obligations is based on the current 2018 G biometric reference tables provided by Heubeck.

3.7. Contingent legal liabilities

Group companies can be parties to legal disputes in a variety of ways as described in Note IV.24. The outcome of these issues can have a material impact on the Group's financial position, operating profit and cash flows. Management regularly analyzes current information on these issues and recognizes provisions in the amount of likely cash outflows, including estimated legal costs. In deciding on the need for provisions, management takes into account the degree of probability of an unfavorable outcome and the possibility of reliably estimating the amount of damage. Filing an action or formally exercising damage claims against Group companies or the announcement of such an action or exercising of damage claims does not automatically mean that a provision is appropriate.

3.8. Income taxes

In terms of income taxes, material estimates and assessments arise in respect of deferred tax assets. The assessment of impairment of deferred tax assets depends on the management's estimate of the utilization of the deferred tax assets. This is dependent on taxable profits in the periods when the tax measurement differences are reversed and the tax loss carryforwards can be utilized. On the basis of individual company planning and taking into account tax adjustment effects, the Company assumes that the advantages of deferred tax assets can be realized in the next four to five years on the basis of sufficient, future taxable income. The main influencing factor for the occurrence of loss carryforwards were one-off transformation-related effects, as well as IPO related restructuring and refinancing.

3.9. Lease term

Determining the lease term of a contract with renewal and termination options – Group as lessee

The Group determines the lease term as the non-cancellable term of the lease, together with any periods covered by an option to extend the lease if it reasonably certain to be exercised, or any periods covered by an option to terminate the lease, if it is reasonably certain not to be exercised.

HENSOLDT has several lease contracts that include extension and termination options. The Group applies judgement in evaluating whether it is reasonably certain whether or not to exercise the option to renew or terminate the lease. The Group considers all relevant factors that create economic incentives to exercise either the renewal or termination. After the commencement date, HENSOLDT reassesses the lease if there is a significant event or change in circumstances that is within its control and affects its ability to exercise or not to exercise the option to renew or to terminate.

HENSOLDT includes the extension period as part of the lease term for certain property leases when HENSOLDT is reasonably certain it will exercise the option. Furthermore, the periods covered by termination options are included as part of the lease term only when they are reasonably certain not to be exercised.

Please refer to Note IV.28 for information on potential future lease payments relating to periods following the commencement date of extension and termination option that are not included in the lease term.

3.10. Determination of fair values

Several accounting policies and disclosures require the measurement of fair values, for both financial and non-financial assets and liabilities. When measuring the fair value of an asset or a liability, the Group uses observable market data as far as possible. Using unobservable market parameters, key estimates and assessments need to be determined. HENSOLDT regularly reviews significant unobservable inputs and valuation adjustments. Please refer to Note 2.15.

4. Changes in significant accounting policies

Standard and changes	Date of effectiveness from IASB for the annual reporting period beginning on or after	EU Endorsement status	Material impact on HENSOLDT Group's Financial Statement
Amendments to References to the Conceptual Framework in IFRS Standards	Jan. 1, 2020	Confirmed	No
Amendments to IFRS 3 "Business combinations"	Jan. 1, 2020	Confirmed	No
Amendments to IAS 1 and IAS 9: "Definition of Material"	Jan. 1, 2020	Confirmed	No
Interest Rate Benchmark Reform Phase 1 (Amendments to IFRS 9, IAS 39 and IFRS 7)	Jan. 1, 2020	Confirmed	No
Adjustments to IFRS 16: "COVID-19 related lease concessions"	Jun. 1, 2020	Confirmed	No

5. Standards issued but not yet effective

A range of new or revised standards, changes and improvements to standards and interpretations are not yet applicable to the fiscal year ending December 31, 2020, and were not applied when preparing these consolidated financial statements. Amendments to standards not separately listed are not expected to have an impact on the Group.

Standard and changes	Date of effectiveness from IASB for the annual reporting period beginning on or after	EU Endorsement status	Expected to have a material impact on HENSOLDT Group's Financial Statement
Interest Rate Benchmark Reform Phase 2 (Amendments to IFRS 9, IAS 39 and IFRS 7)	Jan. 1, 2021	Confirmed	No
Amendments to IAS 37: Onerous contracts	Jan. 1, 2022	Not yet confirmed	No
Amendments to IFRS 3: Amendments to References to the Conceptual Framework in IFRS Standards	Jan. 1, 2022	Not yet confirmed	No
Amendments to IAS 16: Property, Plant and Equipment, Proceeds from intended use	Jan. 1, 2022	Not yet confirmed	No
Amendments to IAS 1: Classification of Liabilities as Current or Non-current	Jan. 1, 2023	Not yet confirmed	No

II. Group structure

6. Consolidated group

The shareholdings as of December 31, 2020, are listed in the following table:

Company	Registered Office	Equity interest	Type of interest
HENSOLDT AG	Taufkirchen / Germany	-	PC
HENSOLDT Holding GmbH	Taufkirchen / Germany	<100%*	FC
HENSOLDT Holding Germany GmbH	Taufkirchen / Germany	<100%*	FC
HENSOLDT Avionics Holding GmbH (former: EuroAvionics Holding GmbH)	Pforzheim / Germany	100.0%	FC
HENSOLDT Avionics GmbH (former: EuroAvionics GmbH)	Pforzheim / Germany	100.0%	FC
EuroAvionics UK Ltd.	Slinfold, West Sussex / United Kingdom	100.0%	FC
EuroAvionics Schweiz AG	Sissach / Switzerland	100.0%	FC
EuroAvionics US HoldCo. Inc.	Sarasota / USA	100.0%	FC
EuroAvionics USA LLC	Sarasota / USA	100.0%	FC
GEW Integrated Systems (Pty) Ltd.	Brummeria / South Africa	75.0%	FC
GEW Technologies (Pty) Ltd.	Brummeria / South Africa	75.0%	FC
HENSOLDT Optronics GmbH	Oberkochen / Germany	<100%*	FC
HENSOLDT Optronics (Pty) Ltd.	Irene / South Africa	70.0%	FC
HENSOLDT Sensors GmbH	Taufkirchen / Germany	<100%*	FC
HENSOLDT UK Limited	Enfield / United Kingdom	100.0%	FC
KH Finance No.2	Enfield / United Kingdom	100.0%	FC
KH Finance Ltd.	Enfield / United Kingdom	100.0%	FC
Kelvin Hughes Ltd.	Enfield / United Kingdom	100.0%	FC
Kelvin Hughes BV	Rotterdam / The Netherlands	100.0%	FC
A/S Kelvin Hughes	Ballerup / Denmark	100.0%	FC
Kelvin Hughes LLC	Alexandria (Virginia) / USA	100.0%	FC
HENSOLDT Singapore Pte. Ltd.	Singapore / Singapore	100.0%	FC
HENSOLDT Holding France S.A.S.	Paris / France	100.0%	FC
HENSOLDT France S.A.S.	Paris / France	100.0%	FC
Kite Holding France S.A.S.	Paris / France	100.0%	FC
HENSOLDT Australia Pty Ltd	Fyshwick, Canberra / Australia	100.0%	FC
Nexeya France S.A.S.	Toulouse / France	100.0%	FC
Midi Ingénierie S.A.S.	Toulouse / France	85.0%	FC
Antycip Technologies S.A.S.	Massy / France	100.0%	FC
Penser Maitriser Technicité Logistique - P.M.T.L S.A.S.	Cologne / France	100.0%	FC

Company	Registered Office	Equity interest	Type of interest
HENSOLDT Space Consulting S.A.S. (former: Nexeya Conseil et Formation S.A.S.)	Toulouse / France	100.0%	FC
Nexeya Canada Inc.	Markham / Canada	100.0%	FC
HENSOLDT Cyber GmbH	Taufkirchen / Germany	51.0%	EQ

PC = Parent Company
EQ = Joint ventures pursuant to IFRS 11 accounted for using the equity method
FC = Consolidated affiliated company.
*Interest of federal German Republic w ith a nominal value of 1 euro each

The consolidated financial statements include the financial statements of HENSOLDT AG and the financial statements of all directly and indirectly by HENSOLDT AG controlled material subsidiaries. The group entities prepare their financial statements as at same reporting date as for which the Group prepares its consolidated financial statements. 32 entities (PY: 32) were fully consolidated. One entity was included in the Group using the equity method. 13 companies (PY: 13) as listed below were not consolidated.

Company	Registered Office	Equity in € million	Profit/loss in € million	Equity interest	Type of interest
Atlas Optronics LLC[1]	Abu Dhabi / United Arab Emirates	N/A	N/A	49.0%	AC
Deutsche Elektronik Gesellschaft für Algerien (DEGFA) GmbH[1]	Ulm / Germany	10.4	-0.3	66.7%	JV
EURO-ART Advanced Radar Technology GmbH[1]	Munich / Germany	0.2	0.0	25.0%	AC
EURO-ART International EWIV[1]	Munich / Germany	1.1	0.0	50.0%	AC
EUROMIDS S.A.S.[1]	Paris / France	3.2	0.3	25.0%	AC
LnZ Optronics Co., Ltd.[1]	Seoul / South-Korea	1.4	0.0	50.0%	AC
HENSOLDT do Brasil Segurança e Defesa Electrónica e Optica Ltda[1]	Belo Horizonte / Brazil	-0.1	0.1	99.0%	NC
Société Commune Algérienne de Fabrication de Systèmes Electroniques (SCAFSE) SPA[1]	Sidi Bel Abbès / Algeria	27.4	1.6	49.0%	JV
HENSOLDT Inc.[1]	Wilmington (North-Carolina) / USA	-4.8	-1.7	100.0%	NC
HENSOLDT Private Ltd.[3]	Bangalore / India	0.1	0.1	100.0%	NC
Nexeya USA Inc.[2]	Beaufort (North Carolina) / USA	0.0	0.0	100.0%	NC
Antycip Iberica SL[1]	Barcelona / Spain	0.0	0.0	100.0%	NC
PMTL-PEINTURE COMPOSITE S.A.S.[2]	L'Isle-Jourdain / France	0.1	-0.1	49.8%	AC

NC: Non-consolidated affiliated company for reasons of immateriality valued at cost
AC: Associated company valued at cost for reasons of immateriality
JV: Joint ventures pursuant to IFRS 11 valued at cost for reasons of immateriality
[1]Equity and profit / loss 2019
[2]Equity and profit / loss June 30, 2020
[3]Equity and profit / loss March 31, 2020
N/A: No financial data available.

7. Acquisitions

7.1. Acquisitions in the previous reporting period

Nexeya France S.A.S.

As at October 1, 2019, HENSOLDT acquired 100.0% of the shares and voting rights in Nexeya France S.A.S., Toulouse, France (“Nexeya”). The preliminary purchase price amounted to €88.8 million. The process of the determining the final purchase price resulted in the adjustment of the purchase price by €9.6 million to €79.2 million and of the recognized goodwill from €49.8 million to €40.2 million, respectively, in the fiscal year 2020. The adjustment (assets +€11.7 million, liabilities +€2.1 million) was made retrospectively as of December 31, 2019, adjusting the prior-year comparative figures.

7.2. Acquisitions after balance the reporting period

HENSOLDT Analytics GmbH GmbH und Tellumat (Pty) Ltd.

At the beginning of 2021, 100.0% of the shares in HENSOLDT Analytics GmbH (formerly known as: SAIL LABS Technology GmbH), Vienna, and two business units (ATM and Defence Division) of Tellumat (Pty) Ltd, South Africa, were acquired. The total preliminary purchase price amounted to €7.7 million.

8. Investments accounted for using the equity method

HENSOLDT Cyber GmbH, Taufkirchen, District of Munich, is a 51.0% joint venture founded in 2017 by HENSOLDT Holding Germany GmbH and Secure Elements GmbH, Munich. The Company's purpose is the development, production, integration and sale of solutions in the areas of IT hardware, software and services.

The share capital of the company amounts to €25.0 thousand. In the previous year, HENSOLDT Holding Germany GmbH contributed payments in the amount of €3,0 million into the capital reserve . In 2020, HENSOLDT Cyber GmbH reported a loss of €5.1 million. The at-equity valuation of the investment of €1.2 million was fully written off in 2020 (PY: €1.2 million). A short-term loan granted by HENSOLDT Holding Germany GmbH as part of the net investment in HENSOLDT Cyber GmbH was reduced by the pro-rata loss of €1.4 million. After the impairment, the loan amounted to €7.8 million.

9. Transactions with related parties

9.1. Related parties and entities

In accordance with IAS 24, transactions with individuals or entities that control or are controlled by the HENSOLDT Group must be disclosed unless they have already been included as consolidated entities in the consolidated financial statements. In addition, there is an obligation to disclose transactions with associates and persons who have significant influence over the operating and financial policies of the HENSOLDT Group. Significant influence in this context can be based on a shareholding in HENSOLDT AG of 20,0% or more or another key management position.

As of August 17, 2020, the key management personnel of the HENSOLDT Group is the Management Board and the Supervisory Board of HENSOLDT AG.

Until August 17, 2020, the key management personnel was the Management Board of HENSOLDT GmbH as well as the supervisory board of HENSOLDT Holding GmbH.

Related parties of HENSOLDT AG are:

Members of the Management Board:

- Thomas Müller, CEO;
- Axel Albert Hans Salzmann, CFO; and
- Peter Fieser, CHRO.

Members of the Supervisory board:

- Johannes P. Huth, Partner of an investment company, Chairman of the supervisory board;
- Armin Maier-Junker, Chairman of the Works Council and the General Works Council of HENSOLDT Sensors GmbH, Deputy Chairman of the supervisory board;
- Jürgen Bühl, Trade Union Secretary of the IGM Management Board;
- Dr. Frank Döngi, Chairman of the Company Spokesperson Committee of senior management (as of March 01, 2020);
- Winfried Fetzer, Chairman of the Works Council, Chairman of the General Works Council of HENSOLDT Optronics GmbH;
- Prof. Dr. h.c. Wolfgang Ischinger;
- Ingrid Jägering;
- Marion Koch, Member of the Works Council of HENSOLDT Sensors GmbH (as of August 11, 2020);
- Christian Ollig;
- Prof. Dr. Burkhard Schwenker;
- Julia Wahl, Union Secretary of IGM (as of January 31, 2019);
- Claire Wellby (from March 01, 2020);
- Thomas Hoepfner, Chairman of the Works Council / Deputy Chairman of the General Works Council of HENSOLDT Sensors GmbH (until August 10, 2020);
- Martin Mix (till February 29, 2020);
- Peter Härtle, Chairman of the Company Spokesperson Committee of senior management (until February 29, 2020); and
- Ingo Zeeh, Member of the Works Council of HENSOLDT Optronics (as of January 01, 2021).

Square Lux Holding II S.à r.l., Luxembourg, (hereinafter also "Square") holds a direct majority interest as controlling company in HENSOLDT AG (formerly: HENSOLDT GmbH) since November 29, 2019. Until the IPO in 2020, Square held 100,0% of the shares, as of December 31, 2020 Square holds 68,3% of the shares.

Through other parent companies of Square, the Company's ultimate parent is KKR Square Aggregator L.P., Canada (hereinafter also "KKR") and its subsidiaries. KKR is a holding company of investment funds indirectly held by Kohlberg Kravis Roberts & Co L.P. and its affiliates. HENSOLDT AG is also indirectly majority-owned by Square Lux Midco 1 & Co S.C.A., Luxembourg, which is owned by KKR.

Companies affiliated with the controlling companies are the following companies held by Kohlberg Kravis Roberts & Co L.P.: KKR Capital Markets Partners LLP, KKR Capital Markets (Ireland) Limited, KKR Capstone Americas LLP, KKR Capital Markets Ltd, KKR Capstone EMEA (International) LLP, and Square Lux Finco S.à r.l., Luxembourg, as an affiliate of Square.

Other related parties of HENSOLDT AG are companies in which HENSOLDT AG either directly or indirectly holds a majority interest.

Additional related parties are HENSOLDT Sensors GmbH's pension fund, HENSOLDT Pension Trust e.V. (including its subsidiaries), as well as the non-consolidated subsidiaries of the Group.

Management participation

The members of the Management Board of HENSOLDT AG, as well as other executives and board members of the HENSOLDT Group can indirectly participate in HENSOLDT AG by indirect acquisitions of ordinary shares and in some cases also of interest-bearing Convertible Preferred Equity Certificates issued by Square Lux Midco 1 & Co S.C.A. In the absence of a monetary benefit at the time of the entry or exit of the participants, no expense is recognized in the consolidated financial statements at any time (neither in the event of an exit nor in the event of the resignation of the manager).

9.2. Related party transactions

In the course of its operating activities, the HENSOLDT Group exchanges goods and services with numerous companies.

	Fiscal year	
in € million	2020	2019
Revenues		
Joint ventures	13.8	57.4
Associates	51.3	13.7
Non-consolidated companies	22.4	25.3
Other income and cost reimbursements		
Parent company	5.2	-
Joint ventures	1.1	0.8
Other related parties	10.1	14.2

	Fiscal year	
in € million	2020	2019
Purchases of goods and services		
Joint ventures	0.6	0.2
Associates	3.9	0.5
Non-consolidated companies	1.1	1.6
Other related parties	24.8	13.7
Other expenses		
Other related parties	-	21.4

in € million	Dec. 31, 2020	Dec, 31 2019
Receivables		
Joint ventures	74.0	71.9
Associates	20.9	14.7
Non-consolidated companies	4.3	5.5
Other related parties	0.1	0.1
Liabilities		
Joint ventures	0.9	1.5
Associates	3.2	2.5
Non-consolidated companies	0.2	0.0
Other related parties	4.1	4.8

In course of HENSOLDT AG's IPO, HENSOLDT AG has charged expenses to the net amount of €5.2 million on a pro-rata basis to the parent company under the cost-sharing and compensation agreement in which the Company entered into with Square Lux Holding II S.à r.l., Luxembourg.

Expenses with other related parties include expenses associated with the IPO and fees for KKR Capital Markets Partners LLP for the accompanying refinancing of the Group in the amount of €4.2 million (PY: €0.0 million), fees for KKR Capstone Americas LLP in the amount of €30 thousand (PY: €0.0 million), fees for KKR Capital Markets (Ireland) Ltd. in the amount of €5.5 million (PY: €0.0 million), and expenses related to leased buildings in the amount of €15.1 million (PY: €13.7 million). Other expenses include interest paid to Square Lux Finco S.à r.l.in the amount of €0.0 million (PY: €21.4 million),

Receivables and liabilities from related parties in 2020 mainly relate to trade receivables and trade liabilities. Receivables from joint ventures include a loan of €7.8 million (PY: €3.0 million) to HENSOLDT Cyber GmbH.

Further information regarding the financing of pension plans of the Group which are considered related parties are presented under Note V.32.

9.3. Related parties

The members in key positions of HENSOLDT AG and the Group are, as of August 17, 2020, the members of the Management Board and the members of the Supervisory Board of HENSOLDT AG. Until August 17, 2020, they were the members of the Management Board of HENSOLDT GmbH and the members of the Supervisory Board of HENSOLDT Holding GmbH.

In the previous year, until November 29, 2019, the Group's key management personnel consisted of the Management Team and the Supervisory Board of HENSOLDT Holding GmbH. The Management Team of HENSOLDT Holding GmbH consisted of the members of the Management Board and other executive positions. Since November 29, 2019, HENSOLDT GmbH has been the new parent company of the Group.

Remuneration of the Management Board

The members of the Management Board received salaries and other short-term benefits (including bonuses) totaling €3.2 million (PY: €2.8 million) for the fiscal year. The members of the Management

Board were granted contributions to the company pension scheme totaling €0.4 million (PY: €0.4 million).

Therefore, the total compensation and benefits granted to the members of the Management Board amounted to €3.6 million (PY: €3.3 million).

Remuneration of the Supervisory Board

The compensation of the members of the Supervisory Board comprised a general compensation and an additional compensation for committee activities amounting in total to €0.6 million (PY: €0.5 million), including attendance fees.

Information on the compensation of individual Management Board and Supervisory Board members is presented in the compensation report, which is part of the combined management report.

III. Group performance

10. Operating segments

10.1. Segmentation

The HENSOLDT Group´s segmentation corresponds to its internal steering, controlling and reporting structures. In accordance with IFRS 8, HENSOLDT has identified the reportable segments Sensors and Optronics.

Sensors segment

The Sensors segment provides system solutions and comprises the three divisions Radar, Identification Friend or Foe (“IFF”) & Data Communications (“COMMS”), Spectrum Dominance & Airborne Solutions, and Customer Services, as well as Others/Elimination. The solutions of the Radar, IFF & COMMS and the Spectrum Dominance & Airborne Solutions divisions are complementary in the value chain, resulting in interdependencies between the two such as shared engineering and operations. As an aftersales division, the Customer Services division is positioned further down the value chain and largely dependent on the primary business of the other two divisions of the Sensors segment.

Radar, IFF & COMMS

Within the Radar, IFF & COMMS division, the Group develops and manufactures mobile and stationary radar and IFF systems used for surveillance, reconnaissance, air traffic control (ATC) and air defense. These systems are deployed on various platforms, including the Eurofighter, the German Navy's Frigate 125 and the US Navy’s Littoral Combat Ship. The Radar, IFF & COMMS division also includes systems for establishing secure data connections for air, sea and land platforms.

Spectrum Dominance & Airborne Solutions

The Spectrum Dominance & Airborne Solutions division includes electronic systems for the acquisition and evaluation of radar and radio signals and jammers, which are used, for example, to protect convoys or individual vehicles against improvised explosive devices. In addition to applications on the electromagnetic spectrum for land, sea and air applications, the product range is being extended to include defensive cyber-solutions. Furthermore, the Group offers electronic self-protection systems integrating missile, laser and radar warning sensors with countermeasures for air, sea and ground platforms and provides military and civil avionics systems such as situational awareness systems, mission computers and flight data recorders. Systems from the Spectrum Dominance & Airborne Solutions division are used in fighter aircraft such as the Eurofighter and Tornado, the Airbus A400M transport aircraft and various helicopter models.

Customer Services

The Customer Services division encompasses a range of customer support and service activities, as well as maintenance over the entire lifecycle of the platforms and systems developed in the other two divisions of the Sensors segment. Simulation solutions, training courses and special services are also offered within this division.

Others/Elimination includes others, mainly comprising components for anti-aircraft missile defense systems, funded military studies and funding projects, and the elimination of intra-segment revenue between the three divisions of the Sensors segment.

Optronics segment

The Optronics segment comprises optronics and optical and precision instruments for military, security and civil applications that can be used on land, in water and in the air. On land, the product range includes rifle scopes, sights, laser rangefinders, night vision devices, and thermal imaging cameras that assist snipers and infantry soldiers with observation and target acquisition. In addition, devices for surveillance and target acquisition are offered for armored vehicles. For use at sea, submarine periscopes, optronic mast systems and other electro-optical systems are offered. In the air, the product portfolio includes stabilized sensor platforms with image stabilizers for helicopters, manned fixed-wing aircraft and drones, which support their surveillance and target acquisition. HENSOLDT also offers mobile and stationary surveillance solutions for security applications, as well as special equipment for industrial and space applications within this segment. Further, support and services for Optronics products forms part of the Optronics segment.

10.2. Segment information

The operating segments of the HENSOLDT Group are internally steered and controlled by the means of its most important KPIs, revenue, order intake and adjusted EBITDA. In addition, HENSOLDT uses adjusted EBIT as a further key performance indicator as well as order backlog as an additional key operating metric. The following table shows the KPIs that the Management Board uses to evaluate the performance of each operating segment as well as additional information.

				2020
in € million	Sensors	Optronics	Elimination/ Transveral/ Others	Group
Order Intake	2,238.1	308.3	-5.1	2,541.3
Order Backlog as per December 31	2,825.5	600.0	-1.5	3,424.0
Revenues from external customers	922.5	284.4	0.0	1,206.9
Intersegment revenues	1.1	3.7	-4.8	-
Segment revenues	**923.6**	**288.1**	**-4.8**	**1,206.9**

				2020
in € million	Sensors	Optronics	Elimination/ Transveral/ Others	Group
Material non-cash items other than depreciation and amortisation:				
Additions to other provisions	-85.3	-45.6	-	-130.9
Dissolution of other provisions	13.1	4.9	-	18.0
Entity's interest in the profit or loss of associates and joint ventures accounted for by the equity method	-	-	-2.6	-2.6

in € million	Sensors	Optronics	Elimination/ Transveral/ Others	2020 Group
EBITDA	**155.3**	**64.9**	**-30.9**	189.3
Separation cost	-	-	0.0	0.0
Transaction cost	-	-	0.9	0.9
IPO cost	-	-	15.8	15.8
Other non-recurring effects	0.9	0.7	11.7	13.3
Adjusted EBITDA	**156.2**	**65.6**	**-2.5**	**219.3**
Margin adjusted EBITDA [1]	16.9%	22.8%		18.2%
Depreciation and Amortization	-90.5	-30.2	-0.1	-120.8
EBIT	**64.8**	**34.7**	**-31.0**	**68.5**
Effect on earnings from purchase price allocations	54.0	14.7	-	68.6
Separation cost	-	-	0.0	0.0
Transaction cost	-	-	0.9	0.9
IPO cost	-	-	15.8	15.8
Other non-recurring effects	0.9	0.7	11.7	13.4
Adjusted EBIT	**119.7**	**50.1**	**-2.6**	**167.2**
Margin adjusted EBIT [1]	13.0%	17.4%		13.9%

1 Based on external revenue

in € million	Sensors	Optronics	Elimination/ Transveral/ Others	2020 Group
EBIT	**64.8**	**34.7**	**-31.0**	**68.5**
Finance income/costs	-	-	-	-143.7
EBT	**-**	**-**	**-**	**-75.2**

Other non-recurring effects in 2020 include efforts for efficiency programs (HENSOLDT GO!), post-merger-integration and structural development of the HENSOLDT Group.

in € million	Sensors	Optronics	Elimination/ Transveral/ Others	2019 Group
Order Intake	657.5	383.3	-0.8	1,040.0
Order Backlog as per December 31	1,567.8	634.5	-	2,202.3
Revenues from external customers	836.6	275.5	2.1	1,114.2
Intersegment revenues	0.5	2.0	-2.5	-0.0
Segment revenues	**837.1**	**277.4**	**-0.3**	**1,114.2**

in € million	Sensors	Optronics	Elimination/ Transveral/ Others	2019 Group
Material non-cash items other than depreciation and amortisation:				
Additions to other provisions	-75.9	-68.1	-	-144.0
Dissolution of other provisions	24.9	17.7	-	42.5
Capitalized interest	-	-	-21.4	-21.4
Entity's interest in the profit or loss of associates and joint ventures accounted for by the equity method	-	-	-1.2	-1.2

in € million	Sensors	Optronics	Elimination/ Transveral/ Others	2019 Group
EBITDA	**162.5**	**53.3**	**-19.9**	**195.9**
Separation cost	-	-	-4.9	-4.9
Transaction cost	-	-	0.5	0.5
IPO cost	-	-	5.5	5.5
Other non-recurring effects	-	1.0	17.6	18.6
Adjusted EBITDA	**162.5**	**54.3**	**-1.2**	**215.6**
Margin adjusted EBITDA [1]	*19.4%*	*19.6%*		*19.3%*
Depreciation and Amortization[2]	-101.9	-31.6	-0.3	-133.8
EBIT	**60.6**	**21.6**	**-20.2**	**62.1**
Effect on earnings from purchase price allocations	61.9	16.9	-	78.8
Separation cost	-	-	-4.9	-4.9
Transaction cost	-	-	0.5	0.5
IPO cost	-	-	5.5	5.5
Other non-recurring effects	-	1.0	17.9	18.8
Adjusted EBIT	**122.4**	**39.5**	**-1.2**	**160.8**
Margin adjusted EBIT [1]	*14.6%*	*14.2%*		*14.4%*

1 Based on external revenue

				2019
in € million	Sensors	Optronics	Elimination/ Transveral/ Others	Group
EBIT	**60.6**	**21.6**	**-20.2**	**62.1**
Finance result	-	-	-	-26.5
EBT	**-**	**-**	**-**	**35.6**

Other non-recurring effects in 2019 include efforts for efficiency programs (“HENSOLDT GO!”), M&A projects, post-merger-integration and structural development of the HENSOLDT Group.

10.3. Geographical information

	Fiscal year	
in € million	2020	2019
Revenue		
Europe	920.2	742.8
(thereof Germany)	*622.8*	*483.3*
Middle East	155.8	164.8
APAC	44.2	82.4
North America	53.1	40.9
Africa	48.0	86.3
LATAM	13.3	19.2
Other regions/Consolidation	-27.6	-22.3
	1,206.9	**1,114.2**

	31. Dec.	31.Dec.
in € million	2020	2019
Non-current assets		
Germany	1,136.3	1,129.9
Other regions	133.6	158.3
	1,269.9	**1,288.3**

10.4. Major customers

Within its two segments, the HENSOLDT Group has three customers that each generate more than 10% of total revenue. From the first customer a revenue of €250,7 million (PY: €239.6 million) was recognized, revenue from the second customer amounted to €149.2 million (PY: €115.4 million). Revenue of €119.0 million (PY: €124.2 million) was recognized from the third customer.

11. Revenue and cost of sales

11.1. Revenue

For reporting purposes, the Group distinguishes between two categories for revenue recognition: sales and aftersales. The aftersales category includes revenue related to the sale of goods and/or the provision of services in connection with a previous sale of goods (e.g. sale of spare parts, maintenance). Revenue from the sale of goods and the provision of services that do not fall into the aftersales category are reported as sales.

The following table provides a breakdown of revenue from contracts with customers by revenue recognition category (sales and aftersales) and the point of time of revenue recognition (at a point in time and over time).

				Fiscal year
in € million	Sensors	Optronics	Other	2020
Revenue from contracts with customers				
Sales	655.5	246.9	-	902.3
Aftersales	267.8	35.2	-	303.0
Exchange rate differences	-0.7	2.3	-	1.6
Total	**922.5**	**284.4**	**-**	**1,206.9**

				Fiscal year
in € million	Sensors	Optronics	Other	2020
Point of time of revenue recognition				
Revenue recognition at a point in time	480.5	276.1	-	756.6
Revenue recognition over time	442.7	6.0	-	448.7
Exchange rate differences	-0.7	2.3	-	1.6
Total	**922.5**	**284.4**	**-**	**1,206.9**

				Fiscal year
in € million	Sensors	Optronics	Other	2019
Revenue from contracts with customers				
Sales	625.4	241.7	-	867.0
Aftersales	210.1	34.3	-	244.4
Exchange rate changes	1.1	-0.5	2.1	2.7
Total	**836.6**	**275.5**	**2.1**	**1,114.2**

				Fiscal year
in € million	Sensors	Optronics	Other	2019
Point of time of revenue recognition				
Revenue recognition at a point in time	497.6	259.6	-	757.2
Revenue recognition over time	337.9	16.4	-	354.3
Exchange rate changes	1.1	-0.5	2.1	2.7
Total	**836.6**	**275.5**	**2.1**	**1,114.2**

11.2. Contract assets and contract liabilities

in € million	Contract assets	Contract liabilities
As of Jan. 01, 2019	**80.7**	**357.6**
Revenue recognized in the reporting period that was included in the contract liability balance at the beginning of the period	-	-145.4
Increases due to cash received, except for amounts which were recognized as revenue during the reporting period	-	116.8
Reclassifications from contract assets, which were recognized at the beginning of the period, to receivables	-31.3	-
Increases due to changes in the determination of stage of completion	90.3	-
Changes in the estimate of the transaction price or contract modification	2.0	-4.7
Changes due to business combinations	23.6	3.4
Other	0.7	5.8
As of Dec. 31, 2019	**165.9**	**333.5**
Revenue recognized in the reporting period that was included in the contract liability balance at the beginning of the period	-	-82.8
Increases due to cash received, except for amounts which were recognized as revenue during the reporting period	-	193.7
Reclassifications from contract assets, which were recognized at the beginning of the period, to receivables	-33.9	-
Increases due to changes in the determination of stage of completion	79.2	-
Changes due to business combinations	-	-
Other	-6.8	-11.5
As of Dec. 31, 2020	**204.4**	**432.8**

An impairment of €0.3 million (PY: €0.4 million) is included in the carrying amount of the contract assets.

Revenue from performance obligations, which had been (partially) fulfilled in prior periods, in the amount of €0.9 million (PY: €3.8 million) was recognized in the reporting period.

11.3. Transaction price for remaining performance obligations

As of December 31, 2020, the total amount of the transaction price allocated to remaining performance obligations amounted to €3,424 million (PY: €2,202 million). Management expects that 30.6% of this transaction price will be recognized as revenue in the next reporting period and a further 36.0% in the period between 2022 and 2023. The remaining 33.4% will be recognized in fiscal year 2024 and following years.

11.4. Cost of sales

Cost of sales includes amortization from adjustments to the fair values of assets as part of the purchase price allocations of €68.6 million (PY: €78.8 million).

Inventories recognized as an expense in the reporting period amounted to €774.4 million (PY: €698.8 million).

12. Research and development costs

Research and development costs amounted to €25.1 million (PY: €31.0 million). For the capitalization of development costs, please refer to Note IV.17.

13. Other operating income and expenses

13.1. Other operating income

	Fiscal year	
in € million	2020	2019
Reinvoiced services	16.5	22.7
Others	2.4	2.6
Other operating income	**18.9**	**25.3**

Other operating income mainly relates to recharged facility- and administrative services as well as IT services.

13.2. Other operating expenses

	Fiscal year	
in € million	2020	2019
Reinvoiced costs	15.0	20.0
Other	1.1	4.8
Other operating expenses	**16.1**	**24.8**

Other operating expenses mainly relates to facility and administrative services.

14. Finance result

in € million	Fiscal year 2020	2019
Interest income from plan assets	2.6	3.6
Other interest income	0.6	54.4
thereof changes in fair value of embedded derivatives	*-*	*54.2*
Other	0.9	0.9
Interest income	4.0	58.9
Loan (Term Loan)	-108.2	-34.4
thereof changes in fair value of embedded derivatives	*-50.9*	*-*
thereof catch-up effect from preliminary contract termination	*-27.9*	*-*
Revolving Credit Facility	-5.2	-2.6
Shareholder loan (Square Lux Finco S.à r.l.)	-	-21.4
Interest expense from swap	-4.3	-3.4
Interest expenses on provisions for employee benefits	-8.1	-8.6
Interest expenses on lease liabilities	-9.7	-9.8
Other	-2.3	-3.3
Interest expense	-137.7	-83.5
Bank fees	-7.6	-5.2
Foreign currency translation of monetary items	-2.0	2.6
Other	-0.4	0.7
Other finance income/costs	-10.0	-1.9
Total finance costs	-143.7	-26.5

15. Income tax

Income taxes are broken down as follows:

in € million	Fiscal year 2020	2019
Current tax expense expenses (-) / income (+)	-9.4	-8.8
thereof which income tax attributable to the prior year	*-0.3*	*2.2*
Deferred taxes expense (-) / income (+)	20.1	-18.6
thereof changes in temporary differences	*12.4*	*-13.0*
Recognized tax expense (-) / income (+)	**10.7**	**-27.4**
Deferred tax income recognized directly in equity	13.3	24.5

For German companies, a corporation tax rate of 15.0% was used for the calculation of deferred taxes. In addition, a solidarity surcharge of 5.5% on the corporation tax and a trade tax rate of 12.5% were taken into account. This resulted in an overall tax rate of 28.3% for German companies. For international group companies, the respective country-specific tax rates were used for the calculation of current and deferred taxes.

The following table presents the reconciliation of expected tax expense and reported tax expense. Expected tax expense is determined by multiplying consolidated profit before tax by the total tax rate of 28.3% applicable in 2020:

	Fiscal year	
in € million	2020	2019
Earnings before income tax profit (+) / loss (-)	-75.2	35.6
Income tax rate	*28.3%*	*28.3%*
Expected income taxes on this expense (-) / income (+)	21.3	-10.1
Effects deriving from differences to the expected tax rate	-0.3	0.1
Change in the tax rate and tax law s	-0.1	-0.1
Taxes for prior years	1.8	3.4
Non-deductible interest expenses	-1.2	-1.7
Other non-deductible expenses and taxes as w ell as effects from change from permanent balance sheet differences	-2.3	-6.7
Tax-exempt income	0.6	0.2
Changes in the expected utilization of deferred tax assets	-8.5	-13.6
Other	-0.6	1.1
Income tax as per income statement expense (-) / income (+)	**10.7**	**-27.4**
Effective tax rate in %	*14.3%*	*77.0%*

Deferred tax assets and deferred tax liabilities are recognized in accordance with IAS 12 *Income Taxes* if future tax effects, either due to temporary differences between the carrying amounts of existing assets and liabilities and their tax bases or due to loss carryforwards, are expected. Deferred tax assets and deferred tax liabilities resulting from valuation differences in the balance sheet items are composed as follows:

in € million	Dec. 31, 2020	Dec. 31, 2019
Deferred tax assets		
Assets		
Intangible assets	-	0.0
Property, plant and equipment	0.7	0.8
Financial assets	0.2	0.3
Inventories and contract assets	3.5	43.0
Receivables and other assets	1.7	5.8
Liabilities		
Provisions	96.6	85.5
Liabilities	146.8	50.2
Loss carryforwards	31.8	34.4
Tax credits	10.2	0.3
Other	0.0	1.3
Deferred tax assets (gross)	**291.5**	**221.7**
Netting	-265.3	-191.4
Deferred tax assets (net)	**26.3**	**30.4**

in € million	Dec. 31, 2020	Dec. 31, 2019
Deferred tax liabilities		
Assets		
Intangible assets	131.1	97.7
Property, plant and equipment	3.8	4.3
Financial assets	0.9	0.2
Inventories and contract assets	74.6	63.0
Receivables and other assets	3.0	18.5
Liabilities		
Provisions	23.9	31.1
Liabilities	35.3	21.5
Other	0.3	0.0
Deferred tax liabilities (gross)	**273.0**	**236.2**
Netting	-265.3	-191.4
Deferred tax liabilities (net)	**7.7**	**44.8**
Excess of deferred tax assets (+) / deferred tax liabilities (-)	**18.5**	**-14.5**

The assessment of whether deferred tax assets are impaired depends on the management's estimate if there will be a future taxable profits available against which the Group can use the benefits therefrom.

As of December 31, 2020, the Company did not recognize any deferred tax liabilities for profits of subsidiaries that were not distributed to the parent company. The Group assumes that, for the time being, the profits of its subsidiaries will not be distributed in the foreseeable future. Temporary differences in connection with investments in subsidiaries for which no deferred tax liabilities were recognized amounted to €2.4 million (PY: €2.8 million).

As of December 31, 2020, the following loss and interest carryforwards are recognized (gross):

in € million	Dec. 31, 2020	Dec. 31, 2019
Corporate tax loss carryforw ards	155.6	129.2
Trade tax loss carryforw ards	155.1	123.1
Interest carryforw ards	180.8	150.8
Tax credits	-0.0	0.3

No deferred tax assets were recognized for the following loss and interest carryforwards, as the Company deems it unlikely that there will be taxable profits available against which the Group can use to recover the tax losses (gross amounts):

in € million	Dec. 31, 2020	Dec. 31, 2019
Corporate tax loss carryforw ards	44.9	8.7
Trade tax loss carryforw ards	44.9	8.3
Interest carryforw ards	140.1	150.8

The tax loss carryforwards for which no deferred tax assets were recognized are unlimited usable.

16. Earnings per share

Earnings per share are calculated by dividing the earnings attributable to the holders of the parent company's ordinary shares by the weighted average number of ordinary shares outstanding during the year. There were no conversion or option rights outstanding during the current and previous reporting period. Therefore, diluted earnings per share are identical with basic earnings per share.

	Fiscal year	
in € million	2020	2019
Consolidated profit attributable to the ow ners of HENSOLDT AG	-65.2	5.9
Weighted average number of ordinary shares (in millions)	86.6	80.0
Basic and diluted earnings per share (in €)	**-0.75**	**0.07**

The earnings per share were, due to the issue of equity to the amount of €70.0 million from own funds in 2020, determined under the assumption that HENSOLDT AG had already issued 80.0 million shares in 2019.

IV. Operating assets and liabilities

17. Intangible assets

Intangible assets (excluding goodwill) as of December 31 consisted of the following:

in € million	Licenses, patents and other rights	Other intangible assets	Capitalized development costs	Customer relationship, technology, order backlog, brand	Advance payments and construction in progress	Total
Cost						
As of Jan. 01, 2019	**6.3**	**0.3**	**60.9**	**505.7**	**3.1**	**576.4**
Acquisition through business combinations	0.4	-	0.6	35.1	0.3	36.3
Additions	3.0	0.0	55.1	-	1.0	59.1
Reclassifications	0.5	-	-	-	-0.4	0.2
Currency translation	0.0	-	0.7	-	-	0.7
As of Dec. 31, 2019	**10.2**	**0.3**	**117.3**	**540.8**	**4.0**	**672.7**
Additions	2.8	0.1	62.1	-	1.2	66.1
Disposals	-	-	-12.6	-	-	-12.6
Reclassifications	-	-	-	-	-2.6	-2.6
Currency translation	-	-	-1.5	-	-	-1.5
As of Dec. 31, 2020	**13.0**	**0.4**	**165.3**	**540.8**	**2.6**	**722.1**
Accumulated amortization and impairment losses						
As of Jan. 01, 2019	**-3.4**	**-0.1**	**-14.8**	**-159.3**	**-**	**-177.6**
Additions	-3.6	-0.1	-9.7	-78.0	-	-91.5
Currency translation	-	-	-0.2	-	-	-0.2
As of Dec. 31, 2019	**-7.1**	**-0.3**	**-24.6**	**-237.3**	**-**	**-269.4**
Additions	-2.5	-0.1	-9.0	-67.9	-	-79.5
Disposals	0.0	-	12.6	-	-	12.6
Currency translation	-	-	0.3	-	-	0.3
As of Dec. 31, 2020	**-9.6**	**-0.4**	**-20.7**	**-305.3**	**-**	**-336.0**
Carrying amount						
As of Dec. 31, 2019	**3.1**	**0.0**	**92.7**	**303.5**	**4.0**	**403.3**
As of Dec. 31, 2020	**3.4**	**0.0**	**144.6**	**235.5**	**2.6**	**386.1**

The category “customer relationship, technology, order backlog and brand” includes the HENSOLDT brand with an indefinite useful live.

The carrying amount of the HENSOLDT brand amounted to €55.4 million as of December 31, 2020 (PY: €55.4 million).

In fiscal year 2020, no impairment losses were recognized.

17.1. Development costs

The Group capitalized development costs in fiscal year 2020 of €62.1 million (PY: €55.1 million) as internally generated intangible assets, primarily for development of various radar and sensor technologies such as ASR-NG, TRML4D, TRS4D, IMEX/RESM, Spexer FLASH-NG, ARGUS-LWS.

In 2020, two development projects that had already started were fully impaired due to changed requirements. The impairment loss of €0.9 million was recognized in cost of sales. In 2019, no impairment losses were recognized for either development work commenced or completed.

17.2. Goodwill

For impairment testing goodwill is allocated to the CGUs Sensors and Optronics, which are also operating and reportable segments.

in € million	Sensors	Optronics	Total
Goodwill as of Jan 1, 2019	**510.0**	**83.8**	**593.8**
Additions Nexeya	49.8	-	49.8
Additions HENSOLDT France SAS	3.2	-	3.2
As of Dec. 31, 2019	**563.0**	**83.8**	**646.8**
Purchase price adjustments Nexeya	-9.6	-	-9.6
As of Jan. 01, 2020	**553.4**	**83.8**	**637.2**
As of Dec. 31, 2020	**553.4**	**83.8**	**637.2**

The recoverable amount of both CGUs is based on their value in use, determined by discounting the future cash flows to be generated from continuing use of the CGU. The carrying amount of both CGUs was determined to be lower than their value in use. As the carrying amount of the CGUs did not exceed the value in use of the CGUs, no impairment on goodwill was recorded.

The calculation of the value in use, which is performed in the fourth quarter of each year as of September 30, is based on a DCF model. The cash flows are derived from the budget for the next three years and do not include restructuring activities, which the Group is not yet obligated to do, nor significant future investments that will improve the performance of the assets of the CGU tested. The recoverable amount depends on the discount rate used for the DCF model, the expected future cash flows and the growth rate used for extrapolation purposes. These estimates are mainly relevant for goodwill and other intangible assets with indefinite useful lives recognized by HENSOLDT.

Following key assumptions were used in the estimation of the value in use:

	Dec. 31, 2020		Dec. 31,2019	
Assumptions in %	Sensors	Optronics	Sensors	Optronics
Discount rate (post-tax)	6.0%	6.0%	5.9%	5.9%
Sustainable growth rate	1.0%	1.0%	1.0%	1.0%
Projected sustainable EBIT margin	13.0%	13.0%	13.3%	13.3%

Discount rates represent the current market assessment of the risks specific to each CGU, taking into consideration the time value of money and individual risks of the underlying assets that have not been incorporated in the cash flow estimates. The calculation of the discount rate is based on the specific circumstances of the Group and its operating segments and is derived from its weighted average cost of capital (WACC). The WACC takes into account both debt and equity as well as a branch specific debt ratio. The cost of equity is derived market based from the return on investment expected by the Group's equity investors depending on their risk expectation. The cost of debt is based on the interest-bearing borrowings the Group is obliged to service. The sector specific risk is accounted for by applying a beta factor that is evaluated annually based on publicly available market data. The corresponding pre-tax discount rate amounts to 8.03% (PY: 7.95%) for the CGU Sensors and 8.30% (PY: 8.20%) for the CGU Optronics.

The forecasted cash flows used by the Group in its DCF model are based on the operational business plan. This business plan includes a detailed planning horizon for three years and is, taking into account the long-term nature of the Company's projects, converged into a steady-state on which a perpetual annuity is calculated. The perpetual annuity underlies a sustainable growth rate of 1.0%.

Based on the market position, HENSOLDT assumes for further significant revenue growth in both segments for the detailed planning horizon.

When performing the impairment test for both CGUs, HENSOLDT conducted sensitivity analyses for the sustainable EBIT margin, the discount rate and the sustainable growth rate. These analyses – which included varying the essential valuation parameters within an appropriate range – did not reveal any risk of impairment to goodwill.

18. Property, plant and equipment

Property, plant, and equipment as of December 31 consisted of the following:

in € million	Land, improvements and buildings	Technical equipment and machinery	Other equipment, operating and office equipment	Construction in progress	Total
Cost					
As of Jan. 01, 2019	**8.8**	**74.1**	**28.1**	**15.4**	**126.3**
Acquisition through business combinations	1.4	0.7	0.4	1.5	4.0
Additions	0.3	8.8	6.4	5.8	21.4
Disposals	-0.2	-0.8	-0.4	-	-1.4
Reclassifications	2.6	1.2	1.1	-5.0	-0.2
Currency translation	0.2	0.4	0.2	0.0	0.7
As of Dec. 31, 2019	**13.1**	**84.4**	**35.6**	**17.7**	**150.9**
Additions	0.2	16.7	7.6	6.6	31.0
Disposals	-0.0	-2.1	-0.4	-0.1	-2.6
Reclassifications	1.1	9.5	0.4	-8.5	2.5
Currency translation	-0.3	-1.2	-0.4	-0.1	-2.0
As of Dec. 31, 2020	**14.1**	**107.3**	**42.8**	**15.6**	**179.8**
Accumulated amortization and impairment losses					
As of Jan. 01, 2019	**-0.5**	**-25.6**	**-10.9**	**-**	**-37.1**
Additions	-0.5	-14.2	-6.4	-	-21.1
Disposals	-	0.3	0.2	-	0.5
Reclassifications	-	-	-	-	-
Currency translation	-0.0	-0.2	-0.1	-	-0.2
As of Dec. 31, 2019	**-1.1**	**-39.7**	**-17.2**	**-**	**-58.0**
Additions	-0.5	-14.6	-6.8	-	-21.9
Disposals	-	2.1	0.3	-	2.4
Reclassifications	-	0.0	0.1	-	0.1
Currency translation	0.0	0.5	0.2	-	0.7
As of Dec. 31, 2020	**-1.6**	**-51.7**	**-23.4**	**-**	**-76.7**
Carrying amount					
As of Dec. 31, 2019	**12.0**	**44.8**	**18.4**	**17.7**	**92.9**
As of Dec. 31, 2020	**12.5**	**55.7**	**19.3**	**15.6**	**103.1**

In the fiscal years 2020 and 2019, no impairment losses were recognized.

19. Other investments and other non-current financial assets

in € million	Dec. 31, 2020	Dec. 31, 2019
Other investments	11.2	11.2
Other non-current financial assets	0.1	3.5
Other investments and other non-current financial assets	**11.3**	**14.7**
Other non-current financial assets, due at short-notice	**11.2**	**3.0**
Gesamt	**22.5**	**17.6**

Other investments relate mainly to the investment in Deutsche Elektronik Gesellschaft für Algerien mbH of €9.3 million (PY: €9.3 million).

Interests in other non-current financial assets due at short notice mainly include a loan to HENSOLDT Cyber GmbH in the amount of €7.8 million, which was, in the previous year, presented as other non-current financial assets in the amount of €3.0 million.

20. Inventories

in € million	Gross amount	Impairment	Net carrying amount Dec. 31, 2020	Net carrying amount Dec. 31, 2019
Raw materials and supplies	210.5	-43.9	166.5	165.9
Work in process	246.8	-33.4	213.4	221.5
Finished goods and parts for resale	36.4	-12.6	23.7	23.7
Total	**493.6**	**-89.9**	**403.7**	**411.1**

Impairments on inventories recognized in the consolidated income statement during the fiscal year amounted to €7.7 million (PY: €9.3 million). No significant reversal of impairment losses was recognized as reduction of material cost in the fiscal year.

21. Trade receivables

in € million	Dec. 31, 2020	Dec. 31, 2019
Receivables from the sale of goods and services	294.2	305.0
Impairment	-12.2	-14.2
Total	282.0	290.8

Trade receivables amounting to €129.5 million (PY: €48.8 million) were transferred to a factoring party and derecognized (non-recourse factoring). Further trade receivables amounting to €3.8 million (PY: €4.7 million) do not qualify for derecognition as the credit risk is not transferred to the factoring party (recourse factoring). For the cash received from the factoring party, a corresponding other financial liability is recognized.

The allowance for trade receivables developed as follows:

in € million	2020	2019
As of Jan. 1	14.2	9.9
Acquisition through business combinations	-	0.2
Additions	3.8	5.5
Utilization	-4.2	-
Reversals	-1.6	-1.4
Currency translation	-0.0	-0.0
As of Dec. 31	12.2	14.2

The credit and market risks as well as impairment losses are presented in Note VI.36.

Contract assets and liabilities are presented in Note III.11.

22. Trade payables

As in the prior year, all trade payables as of December 31, 2020, are due within one year.

23. Provisions

The measurement of provisions, e.g. for contract losses, warranties and court proceedings, is based on best available estimates.

	31. Dez.	31. Dez.
in € million	2020	2019
Pension provisions (note 32)	429.8	358.6
Other provisions	246.5	240.1
Total	**676.2**	**598.7**
thereof non-current	*482.6*	*413.6*
thereof current	*193.6*	*185.1*

Other provisions developed as follows over the course of the year:

in € million	Warranties	Personnel-related provisions	Contract losses	Outstanding costs	Other risks and costs	Total
As of Jan. 1, 2020	**82.4**	**49.4**	**2.5**	**24.1**	**81.8**	**240.1**
Utilized	-28.2	-29.6	-	-8.6	-34.3	**-100.7**
Reversal	-7.0	-2.5	-0.1	-1.9	-6.5	**-18.0**
Additions	33.7	35.7	1.6	12.4	47.4	**130.9**
Exchange rate differences	-0.6	-0.1	-	-1.3	-0.5	**-2.5**
Unwinding of discount	0.1	-	-	-	0.1	**0.2**
Reclassifications	-	0.2	-	-	-3.8	**-3.6**
As of Dec. 31, 2020	**80.4**	**53.1**	**4.0**	**24.7**	**84.2**	**246.4**
thereof current	*40.0*	*33.5*	*4.0*	*24.7*	*69.7*	***171.9***
thereof non-current	***40.4***	***19.6***	***-***	***-***	***14.5***	***74.5***

Provisions for warranties cover contractual or factual obligations to repair or reimburse for damages or functional defects in products sold within a certain period at the Group's own expense.

Provisions for outstanding costs relate mainly to deferrals for supplies not yet invoiced and outstanding own services under long-term construction contracts.

The provisions for other risks and costs relate, among other things, to contract-related provisions for subsequent work on performance obligations already fulfilled. In the fiscal year, an amount of €3.8 million was reclassified from provisions to liabilities.

For the non-current other provisions of the Company, it is generally assumed that they will lead to a cash outflow in the next 2 to 5 years.

24. Legal disputes and damage claims

Legal disputes and damage claims include various proceedings, official investigations and proceedings as well as damage claims that are pending or will be initiated or claimed against the Group in the future. These proceedings are subject to much uncertainty and the result of individual issues cannot be reliably predicted. The Group believes that it has recognized adequate provisions to cover current or potential litigation risks. It is quite possible that the final ruling in some cases could lead to expenses beyond those accounted for in the recognized provisions. The term “'quite possible” used here means that the chance of a future transaction or future occurrence of an event is more than unlikely, however less than likely.

Within the scope of its ordinary business operations, the HENSOLDT Group is, from time to time, involved in different court and arbitration proceedings. In January 2020, a major customer filed an arbitration claim with the contractually agreed arbitration board regarding a partially fulfilled contract and demanded refund of payments already made (approximately €31.0 million plus interest) plus further costs and expenses. HENSOLDT considers the asserted claims to be without merit and filed an arbitration counterclaim in May 2020, asserting a claim for performance of the contract, i.e. for payment in accordance with the underlying contract (approximately €11.0 million plus interest). A sufficiently certain statement about the outcome of the arbitration proceedings is still not possible.

Beyond that, the HENSOLDT Group is not currently aware of any official, judicial or arbitration proceedings (including pending and threatened proceedings) during the previous twelve months or longer that could significantly impact or significantly impacted on the Group's assets, liabilities, financial position and financial performance. As of the reporting date, provisions for legal disputes and damage claims of a negligible amount were recognized under other provision for other risks and costs.

25. Contingent assets and contingent liabilities

Due to the type of its transactions, the Group is exposed to the risk of contingent liabilities. The following table shows the undiscounted maximum amounts for which the HENSOLDT Group is liable as of the reporting date due to major types of guarantees (including sureties):

in € million	Dec. 31, 2020	Dec. 31, 2019
Loan guarantees / sureties	25.4	38.4
Contractual guarantees / sureties	420.9	410.1
Other guarantees and sureties	50.0	37.1
Total	**496.3**	**485.6**

The line item loan guarantees/sureties show to what extent the HENSOLDT Group is liable for financial obligations to third parties. For loan guarantees/sureties, the Company generally guarantees that if the principal debtor does not pay the debt or is not able to pay the debt then the Company will fulfill such financial obligations. The maximum liability coverage corresponds to utilization of the outstanding liability of the credit or – in the event of credit facilities that can be utilized in variable amounts – the maximum amount that can be claimed. The table includes the maximum liability coverage. The terms of these loan guarantees/sureties extend up to one year or in some cases there are indefinite loan guarantees/sureties.

In addition, the HENSOLDT Group guarantees the fulfillment of its own contractual guarantees/securities, mainly due to advance payments and performance guarantees/sureties. If the HENSOLDT Group does not meet its contractual obligations, the HENSOLDT Group or one of its subsidiaries can be held liable up to an agreed maximum amount. Generally, the terms of these contingent liabilities run up to 10 years. In some cases, they run up to 20 years or there are indefinite contractual guarantees/securities.

The other guarantees and sureties relate to bid bonds, performance guarantees, custom guarantees and rental guarantees.

26. Other financial assets and other financial liabilities

26.1. Other financial assets

in € million	Dec. 31, 2020	Dec. 31, 2019
Positive fair values of derivative financial instruments[1]	0.3	51.5
Miscellaneous other non-current financial assets	0.7	1.8
Total other non-current financial assets	**1.0**	**53.2**
Positive fair values of derivative financial instruments[1]	5.1	4.9
Receivables from employees	0.8	0.2
Miscellaneous other current financial assets	1.1	0.6
Total other current financial assets	**7.1**	**5.8**
Total	**8.0**	**59.0**

[1] See Note VI.36

26.2. Other financial liabilities

in € million	Dec. 31, 2020	Dec. 31, 2019
Miscellaneous other non-current financial liabilities	0.2	0.2
Total other non-current financial liabilities	**0.2**	**0.2**
Liabilities for derivative financial instruments[1]	6.4	10.9
Liabilities from factoring contracts[2]	91.3	-
Miscellaneous other current financial liabilities	0.1	9.6
Total other current financial liabilities	**97.8**	**20.5**
Total	**98.0**	**20.7**

[1] See Note VI.36
[2] Liabilities from factoring contracts result from the fact that the collection of payments by the factoring party was not yet due as of the balance sheet date.

27. Other assets and liabilities

27.1. Other assets

in € million	Dec. 31, 2020	Dec. 31, 2019
Other	4.8	4.9
Total other non-current assets	**4.8**	**4.9**
Advance payments	57.9	23.0
VAT	12.5	5.4
Miscellaneous other current assets	8.2	17.7
Total other current assets	**78.7**	**46.1**
Total	**83.5**	**50.9**

27.2. Other liabilities

in € million	Dec. 31, 2020	Dec. 31, 2019
Liabilities to employees	8.9	7.7
Total other non-current liabilities	**8.9**	**7.7**
Tax liabilities (not incl. income tax)	37.2	23.7
Liabilities to employees	30.2	25.1
Liabilities to social security agencies	5.8	4.7
Other	13.7	13.6
Total other current liabilities	**86.9**	**67.1**
Total	**95.8**	**74.8**

28. Leases

28.1. Amounts recognized in the consolidated statement of financial position

The following amounts relate to leases accounted for as right-of-use assets as of December 31, 2020.

in € million	Dec. 31, 2020	Dec. 31, 2019
Land and buildings	137.9	147.2
Technical equipment and machinery	2.4	4.2
Other equipment, factory and office equipment	3.2	3.4
Total	**143.5**	**154.9**

Additions to right-of-use assets in 2020 were €9.7 million (PY: €21.4 million).

The lease liability recognized on the consolidated statement of financial position comprises the following:

in € million	Dec. 31, 2020	Dec. 31, 2019
Current	13.7	13.0
Non-current	140.3	147.5
Total	**154.0**	**160.5**

28.2. Amounts recognized in the consolidated income statement

in € million	Fiscal year 2020	2019
Land and buildings	16.2	14.4
Technical equipment and machinery	0.9	0.8
Other equipment, factory and office equipment	2.1	1.8
Total depreciation charge	**19.2**	**17.0**

in € million	Fiscal year 2020	2019
Interest on lease liabilities	9.7	9.8
Income from sub-leasing right-of-use assets presented in "other revenue"	-0.1	-0.5
Expense related to short-term leases □	0.9	2.7
Expense relating to leases of low -value assets that are not short-term leases	2.0	1.3
Total amounts recognised in profit or loss	**12.5**	**13.2**

The total cash outflow for lease payments in 2020 amounted to €24.0 million (PY: €21.1 million).

HENSOLDT has several lease contracts that include extension options and termination options. The exercise of such options is decided by management to provide flexibility in managing the leased-asset portfolio and align with HENSOLDT's business needs. Management exercises significant judgement in determining whether these extension and termination options are reasonably certain to be exercised (see Note I.3.9).

V. Expenses and employee benefits

29. Headcount

	Fiscal year 2020	2019
Production, research and development, service	4,289	3,938
Sales and distribution	191	114
Administration and general services	637	550
Apprentices, trainees, etc.	418	395
Total [1]	**5,535**	**4,997**

[1] Average figures in FTE´s (Full Time Equivalents)

30. Personnel expenses

in € million	Fiscal year 2020	2019
Wages, salaries	429.2	391.7
Social security contributions	69.6	56.2
Net periodic employee benefit expenses	27.7	21.8
Total	**526.5**	**469.7**

31. Personnel-related provisions

Several German group entities offer models for lifetime working or retirement accounts, which represent defined benefit plans due to a pledged interest on contributions or nominal contributions and are to be classified as post-employment benefits in accordance with IAS 19. The obligations of €17.2 million (PY: €16.1 million) are fully offset against corresponding assets. The regular contributions of employees to their lifetime working accounts lead to a corresponding personnel expense in the reporting period which is recognized in personnel expenses.

Other personnel-related provisions developed as follows:

in € million	Long service aw ards/ bonuses	Partial retirement	Other personnel expenses	Total
As of Jan. 01, 2020	**46.2**	**2.3**	**0.9**	**49.4**
Utilized	-25.9	-3.1	-0.6	-29.6
Reversal	-1.9	-0.3	-0.3	-2.5
Additions	32.5	3.2	-	35.7
Effect of movements in exchange rates	-0.1	0	0	-0.1
Reclassifications	-	0.2	-	0.2
As of Dec. 31, 2020	**50.8**	**2.3**	**0.0**	**53.1**

32. Pension benefits

in € million	Dec. 31, 2020	Dec. 31, 2019
Provisions for employee benefits	276.5	225.7
Provisions for deferred compensation	153.3	132.9
Total	**429.8**	**358.6**

32.1. Provisions for pension plans

Provision for pension plans

Provisions for German pension obligations (defined benefit obligations or “'DBO”) are recognized based on defined benefit plans for old-age, invalidity and survivor's pension benefits. The benefits are based on the employee's length of service and remuneration.

Most domestic employees are under the “P3 Plan”, which allows a choice between immediate payments of their accumulated savings, payment in installments or an annuity.

Contractual trust arrangements or “CTA” exist to finance domestic pension obligations. The structure of the contractual trust arrangement is based on mutual trust agreements. Assets transferred to the contractual trust arrangement are considered plan assets under IAS 19.

In terms of the significant accounting policies and significant estimates and assessments, e.g. actuarial assumptions, please refer to the Note I.2.8 and Note I.3.6.

Changes in the defined benefit obligations and plan assets

	DBO		Plan assets		Total	
in € million	2020	2019	2020	2019	2020	2019
As of Jan. 1	**428.7**	**330.3**	**203.0**	**166.0**	**225.7**	**164.3**
Assumption due to business combinations	-	5.3	-	-	-	5.3
Expenses for pension benefit entitlements	22.2	16.4	-	-	22.2	16.4
Interest expenses/income	5.9	6.4	2.7	3.3	3.2	3.1
Payments	-4.2	-3.2	-3.8	-2.8	-0.4	-0.4
Actuarial gains/losses deriving from						
Changes in demographic assumptions	-	39.0	-	-	-	39.0
Changes in financial assumptions	29.1	25.6	-	-	29.1	25.6
Adjustments based on experience	9.8	12.3	-	-	9.8	12.3
Plan assets	-	-	9.9	36.5	-9.9	-36.5
Other changes in consolidation, transfers	-3.2	-3.4	-	-	-3.2	-3.4
As of Dec. 31	**488.3**	**428.7**	**211.8**	**203.0**	**276.6**	**225.7**

The weighted average duration of the defined benefit obligation for pensions and deferred compensation is 19 years.

As of December 31, reported as:

	Pension plans	
	Dec. 31,	Dec. 31,
in € million	2020	2019
Defined benefit obligation	488.3	428.7
Plan assets	-211.8	-203.0
Total	**276.5**	**225.7**

The breakdown of the defined benefit obligation for pension plans between active, former and retired members for the most important plans is as follows:

	Dec. 31,	Dec. 31,
in %	2020	2019
Active	80%	81%
Eligible employees	5%	5%
Pensioner	15%	14%
	100%	**100%**

The expected employer's contribution to defined benefit plans for the fiscal year 2021 amounts to €13.9 million (PY: €11.8 million).

32.2. Provisions for deferred compensation

This amount represents obligations that arise when employees convert a part of their remuneration or bonus into an equivalent entitlement to deferred compensation, which is treated as a defined benefit plan upon termination of employment. The development of DBO and plan assets is as follows:

Changes in the defined benefit obligations and plan assets

	DBO		Plan assets		Total	
in € million	2020	2019	2020	2019	2020	2019
As of Jan. 1	**147.9**	**115.8**	**15.0**	**14.0**	**132.9**	**101.8**
Expenses for pension benefit entitlements	3.5	3.8	-	-	3.5	3.8
Interest expenses/income	2.1	2.2	0.2	0.3	1.9	1.9
Payments	-1.2	-1.1	-	0.1	-1.2	-1.2
Actuarial gains/losses deriving from						
Changes in demographic assumptions	-	9.7	-	-	-	9.7
Changes in financial assumptions	7.5	10.4	-	-	7.5	10.4
Adjustments based on experience	2.6	4.7	-	-	2.6	4.7
Plan assets	-	-	-1.3	0.6	1.3	-0.6
Other changes in consolidation, transfers	-0.7	-2.8	-	-	-0.7	-2.8
Participant contributions	5.5	5.2	-	-	5.5	5.2
As of Dec. 31	**167.2**	**147.9**	**13.9**	**15.0**	**153.3**	**132.9**

As of December 31, reported as:

in € million	Deferred compensation 2020	2019
Defined benefit obligation	167.2	147.9
Plan assets	-13.9	-15.0
Total	**153.3**	**132.9**

The breakdown of the defined benefit obligations for deferred compensation between active, former and retired members for the most important plans is as follows:

in %	Dec. 31, 2020	Dec. 31, 2019
Active	77%	77%
Eligible employees	8%	8%
Pensioner	15%	15%
	100%	**100%**

The following table shows how the present value of defined benefit obligations of pension plans and deferred compensation would have been affected by changes in actuarial assumptions as prepared as of December 31, 2020:

		Dec. 31, 2020		Dec. 31, 2019	
in € million	Change	Increase	Decrease	Increase	Decrease
Present value of obligation					
Discount rate	by 0.5 percentage points	-52.3	72.8	-44.4	62.5
Wage increase rate	by 0.25 percentage points	0.9	-0.9	0.9	-0.9
Pension increase rate	by 0.25 percentage points	10.3	-0.1	9.0	-0.1
Life expectancy	by 1 year	15.3	-15.3	12.6	-12.7
Exercising of pension option	by 10 percentage points	25.8	-25.8	21.5	-21.5

Sensitivities are calculated using the same method (present value of the defined benefit obligation calculated using the projected unit credit method) as used for the calculation of post-employment benefits. The sensitivity analysis is based on a change of one assumption while maintaining all other assumptions unchanged. This is unlikely to occur in practice. Changes to more than one assumption can correlate, which can have differing effects on the DBOs than the effects as described above. If the assumptions change in different levels, the effects on the defined benefit obligation are not necessarily linear.

Asset-liability matching strategy (Investment of plan assets)

The HENSOLDT Group identified the deterioration of the financing status due to an unfavorable development of the fair value of plan assets and/or the defined benefits obligations as a result of changing parameters as a risk.

For this reason, the HENSOLDT treasury department implements a security-oriented investment concept specified by HENSOLDT Strategic Investment Committee, which is focused on the DBOs and the steering and optimization of the plan assets.

The fair value of the plan assets for pensions and deferred compensation can be allocated to the following classes:

	Quoted prices		Unquoted prices		Total	
	Dec. 31,		Dec. 31		Dec. 31,	
in € million	2020	2019	2020	2019	2020	2019
Other investments	-	-	179.2	167.8	179.2	167.8
Pooled investment instruments	46.4	50.2	-	-	46.4	50.2
Total	**46.4**	**50.2**	**179.2**	**167.8**	**225.6**	**218.0**

Other investments relate to limited partnership interests in HENSOLDT Real Estate GmbH & Co. KG.

The employer's contribution to state and private pension funds, which is mainly made in Germany, is considered as a defined contribution obligation. The contributions in 2020 amount to €28.0 million (PY: €27.4 million).

VI. Capital structure and financial instruments

33. Equity

33.1. Equity attributable to owners of the parent company

As of December 31, 2020, the parent company is HENSOLDT AG.

As of December 31, 2020, the share capital of HENSOLDT AG amounts to €105.0 million and is divided into 105 million ordinary bearer shares (no-par value shares).

With the entry in the Commercial Register on August 17, 2020, HENSOLDT GmbH was converted into HENSOLDT AG. Prior to the conversion, the share capital of the Company was increased from €10.0 million by €70.0 million to €80.0 million from capital reserves by resolution of the shareholders on August 4, 2020 and entry in the Commercial Register on August 6, 2020.

At the time of the conversion of HENSOLDT GmbH into HENSOLDT AG, the share capital of HENSOLDT GmbH amounted to €80.0 million.

In the course of the initial public offering, the share capital of the Company was increased by additional €25.0 million to €105.0 million by resolution of September 3, 2020 and entry in the Commercial Register on September 24, 2020.

The share premium from the issuance of the 25.0 million new shares in the amount of €275.0 million less €4.9 million non-deductible transaction costs and bank fees of the banks accompanying the initial public offering, was transferred to the capital reserve. On September 24, 2020, all 105 million shares of HENSOLDT AG were admitted to trading on the Frankfurt Stock Exchange with admission to the sub-segment of the regulated market with additional post-admission obligations (Prime Standard) and the following day, trading commenced.

In accordance with the articles of association, the share capital of the Company may be increased by the Executive Board until August 11, 2025, with the approval of the Supervisory Board, by issuing new ordinary bearer shares against cash and/or non-cash contributions on one or more occasions by up to a total of €36.0 million. (Authorized Capital 2020/I).As of December 31, 2020, the Company has not utilized the Authorized Capital 2020/I. Accordingly, the Authorized Capital 2020/I amounts to €36.0 million as of December 31, 2020.

In addition, the share capital of the Company has been conditionally increased by up to €16.0 million by issuing up to 16 million new no-par value bearer shares on or before August 11, 2025 against contributions in cash or in kind (Conditional Capital 2020/I).The conditional capital increase shall only be implemented to the extent that the holders or creditors of option or conversion rights or those obliged to exercise the conversion/option exercise their option or conversion rights or, to the extent that they are obligated to exercise the conversion/option, fulfill their obligation to exercise the conversion/option or to the extent that the Company exercises an option to grant shares in the Company in whole or in part instead of payment of the cash amount due. As of December 31, 2020, the Company has not utilized the Conditional Capital 2020/I. Accordingly, the Conditional Capital 2020/I amounts to €16.0 million as of December 31, 2020.

The previous year's figures relate to the share capital of the HENSOLDT GmbH (see I.2.1 Basis of Preparation). HENSOLDT GmbH's share capital was fully paid in and amounted to €10.0 million as of December 31, 2019.

Other reserves include cumulative other comprehensive income.

Retained earnings contain earnings of the companies included in the consolidated financial statements including earnings in the fiscal year, provided these have not been distributed.

33.2. Treasury shares

By way of shareholder resolution dated November 15, 2019, and with effect as of November 18, 2019, 6,275 treasury shares of HENSOLDT Holding GmbH in the amount of €10.6 million were cancelled and offset against the capital reserve.

33.3. Non-controlling interests

The non-controlling interests reflect the share of other shareholders in the net asset value of consolidated subsidiaries.

						Dec. 31,
in € million	Hensoldt Optronics (Pty) Ltd.	GEW Technologies (Pty) Ltd.	Midi Ingénierie S.A.S.	**Total**	Intragroup eliminations/ adjustments	2020
Percentage of non-controlling interests	**30%**	**7%**	**15%**			
Non-current assets	9.8	6.6	0.1	**16.5**	-	16.5
Current assets	51.5	46.1	3.6	**101.2**	-	101.2
Non-current liabilities	-2.9	-0.7	-0.3	**-3.9**	-	-3.9
Current liabilities	-23.9	-20.0	-0.6	**-44.6**	-	-44.6
Net assets	**34.4**	**32.0**	**2.8**	**69.2**	**-**	**69.2**
Net assets of non-controlling interests	**10.3**	**2.1**	**0.4**	**12.9**	**-**	**12.9**
Revenue	39.9	32.9	3.8	**76.6**	-	76.6
Profit	1.6	1.7	1.0	**4.3**	-	4.3
Other comprehensive income/loss	-4.6	-5.2	-0.1	**-9.9**	-	-9.9
Total comprehensive income/loss	**-3.0**	**-3.5**	**0.9**	**-5.6**	**-**	**-5.6**
Profit attributable to non-controlling interests	**0.5**	**0.1**	**0.1**	**0.7**	**-**	**0.7**
Other comprehensive income/loss attributable to non-controlling interests	**-1.4**	**-0.4**	**-0.0**	**-1.7**	**0.3**	**-1.4**
Cash flows from operating activities	4.4	-5.5	0.1	**-1.0**	-	-1.0
Cash flows from investing activities	-1.0	-0.7	-0.0	**-1.7**	-	-1.7
Cash flows from financing activities	-1.8	-1.3	-2.7	**-5.8**	-	-5.8
thereof dividends of non-controlling interests	-	*-0.1*	*-0.2*	***-0.3***	-	*-0.3*
Effects of movements in exchange rates on cash and cash equivalents	-0.1	-3.2	-	-3.3	-	-3.3
Net increase (decrease) in cash and cash equivalents	**1.5**	**-10.7**	**-2.6**	**-11.7**	**-**	**-11.7**

in € million	Hensoldt Optronics (Pty) Ltd.	GEW Tech-nologies (Pty) Ltd.	Midi Ingénierie S.A.S.	**Gesamt**	Intragroup eliminations/ adjustments	Dec. 31, 2019
Percentage of non-controlling interests	**30%**	**7%**	**15%**			
Non-current assets	13.1	7.8	0.1	**20.9**	-	20.9
Current assets	56.4	56.5	5.8	**118.7**	-	118.7
Non-current liabilities	-3.8	-0.4	-0.2	**-4.4**	-	-4.4
Current liabilities	-28.3	-26.9	-1.1	**-56.3**	-	-56.3
Net assets	**37.5**	**36.9**	**4.6**	**78.9**	**-**	**78.9**
Net assets of non-controlling interests	**11.2**	**2.5**	**0.7**	**14.4**	**-0.8**	**13.6**
Revenue	50.2	38.1	1.8	**90.1**	-	90.1
Profit	5.6	6.5	0.9	**13.0**	-	13.0
Other comprehensive income/loss	1.5	0.8	0.0	**2.3**	-	2.3
Total comprehensive income/loss	**7.1**	**7.3**	**0.9**	**15.3**	**-**	**15.3**
Profit attributable to non-controlling interests	**1.7**	**0.4**	**0.1**	**2.3**	**-**	**2.3**
Other comprehensive income/loss attributable to non-controlling interests	**0.5**	**0.1**	**0.0**	**0.5**	**-**	**0.5**
Cash flows from operating activities	-7.6	-2.8	1.4	**-9.0**	-	-9.0
Cash flows from investing activities	-3.3	-0.5	-0.0	**-3.8**	-	-3.8
Cash flows from financing activities (dividends of non-controlling interests: in € million 0)	10.5	-3.7	-0.4	**6.5**	-	6.5
Effects of movements in exchange rates on cash and cash equivalents	-	1.1	-	**1.1**	-	1.1
Net increase (decrease) in cash and cash equivalents	**-0.4**	**-5.9**	**1.0**	**-5.2**	**-**	**-5.2**

Under corporate law, the non-controlling shareholder of GEW Technologies (Pty) Ltd. has a 25.0% interest in GEW Technologies (Pty) Ltd. and its subsidiary GEW Integrated Systems (Pty). The non-controlling shareholder was issued with 500 shares, of which 392 shares are treated as treasury shares until full payment of the purchase price. This results in a financial stake of non-controlling interests of 6.7%. In connection with the shares considered as treasury shares, there is a put option in favor of the non-controlling shareholder which is recognized at market value under other non-current financial liabilities, if the shares exceed the deferred purchase price. Due to a decrease in the pro rata market value of GEW Technologies (Pty) Ltd., the value of the put option has been below the deferred purchase price since December 2019. Therefore, no other non-current financial liabilities were recognized as of this date. In 2019, fair value changes of €1.2 million have been recognized in the consolidated income statement and are presented within other finance result.

34. Capital management

The capital structure of the HENSOLDT Group is made up of equity capital attributable to the shareholders of the parent company and of debt capital. A capital structure that optimizes capital costs of equity and debt is being targeted. The Group is not subject to any statutory capital requirements.

The non-current syndicated loan agreement (Term Loan) is, like the previous loan, tied to compliance with a financial covenant that refers to the ratio of net liabilities to adjusted earnings before interest, taxes, depreciation and amortization (consolidated EBITDA) as defined in the Senior Facility Agreement. In 2020 the financing conditions were met at all times. The availability and conditions of the loan are tied to this financial covenant. In the event of a breach, the financing partners are authorized to terminate the syndicated loan. There are no indications that the covenant cannot be fully complied with in the foreseeable future (see Note 36).

In order to hedge against changes in interest rates and exchange rates, the Group concludes derivative hedging contracts for variable interest-bearing liabilities and loans in foreign currency.

35. Net debt

in € million	Dec. 31, 2020	Dec. 31, 2019
Cash and cash equivalents	645.5	137.4
Non-current financial liabilities	-601.3	-887.7
Current financial liabilities	-363.3	-11.3
Total	**-319.2**	**-761.6**

35.1. Cash and cash equivalents

Cash and cash equivalents consist of the following items:

in € million	Dec. 31, 2020	Dec. 31, 2019
Cash at bank and liquid funds	645.5	137.4
Total	**645.5**	**137.4**

35.2. Financing liabilities

Financial liabilities consist of current and non-current loans.

The conditions and repayment schedules of the loans as of December 31, 2020, are as follows:

Loans	Capital amount in € million	Issue date	Coupon or interest rate	Interest	Effective interest rate	Due date
Loan (Term Loan)	600.0	09/30/2020	3M Euribor + 2,25%	variable	2.64%	09/29/2025
Revolving Credit Facility	350.0	09/30/2020	3M Euribor + 2,00%	variable	0.0	09/29/2025
Loan (BPI France)	1.7	11/29/2017	zero-floored 3M-Euribor + 0,40%	variable	0.73%	12/31/2021
Loan (PGE)	3.0	04/30/2020	0.00%	fix	0.00%	04/30/2021
Loan (PGE)	7.0	03/23/2020	0.00%	fix	0.00%	03/23/2021
Loan (BPI France)	0.7	12/08/2017	1.31%	fix	1.64%	06/30/2025
Loan (EuroAvionics)	0.1	07/27/2020	2.78%	fix	4.84%	06/30/2023
Overdraft Facility (Optronics PTY)	6.4	10/31/2018	7.00%	fix	7.00%	01/21/2021

The conditions and repayment schedules of the loans as of December 31, 2019, are as follows:

Loans	Capital amount in € million	Issue date	Coupon or interest rate	Interest	Effective interest rate	Due date
Loan (Term Loan)	920.0	28/02/2017/ 18/04/2017/ 26/07/2017/ 28/02/2018/ 06/12/2018	3M Euribor + 3,25%	variable	3.91%	02/28/2024
Loan (BPI France)	5.0	11/29/2017	zero-floored 1M-Euribor + 1,00%	variable	1.07%	11/30/2020

In connection with the IPO, HENSOLDT AG has restructured its liabilities as of September 30, 2020. For this purpose, a new syndicated loan agreement “Senior Facility Agreement” consisting of a term loan in the amount of €600.0 million and a revolving credit facility (RCF) in the amount of €350.0 million was concluded. As of the balance sheet date, the revolving credit facility was fully utilized in the amount of €350.0 million. This is repayable on a short-term.

The post-IPO financing is secured by HENSOLDT AG pledging its shares in the subsidiaries HENSOLDT Sensors GmbH, HENSOLDT Optronics GmbH, HENSOLDT Holding France S.A.S. and Nexeya France S.A.S.

The interest rate swap agreements concluded in previous years are continued to hedge the variable-rate term loan. The transaction costs incurred for obtaining the term loan are allocated to the loan in the application of the effective interest rate method. The transaction costs for the revolving credit facility have been capitalized as other assets and are amortized over the term of the agreement.

For the South African subsidiary Optronics (Pty) Ltd., there is a credit line in the amount of ZAR 120.0 million available, of which €6.4 million (ZAR 115.2 million) was drawn as of December 31, 2020.

In addition, the French subsidiary Nexeya S.A.S. drew two government-guaranteed loans with a total value of €10.0 million at an interest rate of 0% in the course of the Corona crisis. A further loan in the amount of €1.7 million exists since 2017. The loans are unsecured.

The total amounts of financial liabilities to banks and shareholder as of December 31, amount to:

in € million	< 1 year	1 to 5 years	> 5 years	Total
Liabilities due to banks	363.3	601.3	-	964.7
As of Dec. 31, 2020	**363.3**	**601.3**	**-**	**964.7**

This includes liabilities from recourse factoring amounting to € 3.8 million (PY: €4.7 million). Furthermore, as of the reporting date other current financial liabilities in the amount of € 91.3 million existed from cash receipts from transferred receivables, which shall be forwarded to the factor on the due date.

in € million	< 1 year	1 to 5 years	> 5 years	Total
Liabilities due to banks	11.3	887.7	-	899.0
As of Dec. 31, 2019	**11.3**	**887.7**	**-**	**899.0**

35.3. The reconciliation of changes in financial liabilities to cash flows from financing activities

The following table shows the cash flows from financing activities in a reconciliation from the opening balances to the closing balances for the liabilities and equity components attributable to financing activities including the accompanying financial assets and liabilities from hedging transactions of these financing activities.

			Non-cash changes			
	Jan. 1,	Net cash changes	Change in Consol. group	Changes in fair value	Other changes	Dec. 31,
in € million	2020					2020
Non-current borrowing						
Repayment TLB	887.7	-920.0	-	-	32.3	-
Proceeds TLB	-	600.0	-	-	-8.4	591.6
Bank loans (net)	-	10.0	-	-	-0.3	9.7
Current borrowing						
Current borrow ing	11.3	353.2	-	-	-1.2	363.3
Other financing liabilities	7.7	84.0	-	-	-	91.7
Change in financial liabilities due to financing avtivities	**906.7**	**127.2**	**-**	**-**	**22.4**	**1,056.3**
Lease liabilties (current / non-current)	**160.5**	**-14.3**	**-**	**-**	**7.8**	**154.0**
Share capital	10.0	25.0	-	-	70.0	105.0
Capital reserve	396.7	273.4	-	-	-73.4	596.8
Other reserves	-49.8	-	-	-	-36.5	-86.3
Reained earnings	-215.8	-	-	-	-65.8	-281.6
Non-Controlling interests	13.6	-0.2	-	-	-0.4	12.9
Change in equity due to financing activities	**154.8**	**298.1**	**-**	**-**	**-106.1**	**346.8**
Change in assets (-) and liabilities (+) to hedge non-current borrow ing	-41.3	-	-	46.9	-	5.6
Cash Flow from financing activities		**411.0**				**411.0**

	Jan. 1,	Net cash changes	Non-cash changes: Change in Consol. group	Changes in fair value	Other changes	Dec. 31,
in € million	2019					2019
Non-current borrowing						
Repayment TLB	349.6	-	-	-	-349.6	-
Proceeds TLB	880.4	-	-	-	7.3	887.7
Bank loans (net)	-	-	-	-	-	-
Current borrowing						
Current borrowing	3.4	3.6	4.2	-	0.1	11.3
Other financing liabilities	1.2	-1.2	4.7	-	3.0	7.7
Change in financial liabilities due to financing avtivities	**1,234.5**	**2.4**	**8.9**	**-**	**-339.1**	**906.7**
Lease liabilties (current / non-current)	**-**	**-11.3**	**11.1**	**-**	**160.8**	**160.5**
Share capital	0.0	0.0	10.0	-	-0.0	10.0
Treasury shares	-10.6	-	-	-	10.6	-
Capital reserve	46.3	-	-10.0	-	360.4	396.7
Other reserves	-12.2	-	-	-	-37.5	-49.8
Reained earnings	-220.7	-	-	-	4.9	-215.8
Non-Controlling interests	10.9	-0.2	0.6	-	2.3	13.6
Change in equity due to financing activities	**-186.3**	**-0.2**	**0.6**	**-**	**340.7**	**154.8**
Change in assets (-) and liabilities (+) to hedge non-current borrowing	14.1	-	-	-55.4	-	-41.3
Cash Flow from financing activities		**-9.1**				**-9.1**

36. Information on financial instruments

36.1. Financial risk management

Based on its activities, the Group is exposed to a range of financial risks: (i) market risks, in particular foreign exchange risk and interest rate risk, (ii) liquidity risk and (iii) credit risk.

Overall, the Group's financial risk management system concentrates on minimizing unforeseeable market risks and their potential negative effects on the Group's operating and financial performance.

The Group's financial risk management is generally carried out by Treasury in compliance with the guidelines approved by the Chief Financial Officer.

Further information on risks relating to financial instruments can be found in the risk report of the consolidated group management report, which is prepared in addition to the IFRS consolidated financial statements.

The Group uses financial derivatives exclusively to mitigate risks (hedging) and applies hedge accounting for a minor part of its hedging portfolio.

Market risk

Foreign exchange risk

The Group is exposed to foreign exchange risks due to its operations in various countries around the globe that do not use the euro.

For orders received that are invoiced in foreign currency, the Group concludes forward exchange transactions in order to rule out or minimize foreign exchange risks. Forward exchange contracts are exclusively concluded with prime international banks. The necessary measures and rules related to the hedging of orders not invoiced in euro are set out in the Group-wide treasury policy.

The Group's main hedging instruments are forward exchange transactions.

Related to hedging its foreign currency transactions in South Africa, the Group uses the cash flow hedge accounting model.

In the fiscal year a gain on foreign currency translation of €0.5 million (PY: €2.1 million) was recognized in the consolidated income statement

Sensitivity of foreign exchange risk

The sensitivity analysis approximately quantifies the risk that can occur based on set assumptions if certain parameters are changed to a defined extent. Currency risks pertain in particular to the US dollar (USD), South African rand (ZAR) and pound sterling (GBP).

The following disclosures describe the Group's view of the sensitivity of an increase or decrease in the USD, ZAR, etc. against the EUR. The change is the value applied in the internal reporting of exchange rate risk and represents the Group´s assessment regarding a possible change in exchange rates. Currency risks within the meaning of IFRS 7 result from financial instruments that are denominated in a currency other than the functional currency and are of a monetary nature. Translation differences from the translation of financial statements of foreign group entities into the Group's currency remain unconsidered. The sensitivity analysis includes the HENSOLDT Group's main financial instruments outstanding on the reporting date.

The effects on the consolidated profit and other comprehensive income are as follows:

If the EUR had appreciated/depreciated by 20.0% or 50.0% against the USD, ZAR and GBP as of December 31, 2020/2019, the consolidated profit and other comprehensive income would have changed in the manner shown below:

in € million	Changes in the amount of	Dec. 31, 2020	Changes in the amount of	Dec. 31, 2019
EUR/GBP	+/- 20.0%	-5.3 / 8.0	+/- 10.0%	-3.1 / 4.7
EUR/ZAR	+/- 50.0%	-1.3 / 2.0	+/- 10.0%	1.1 / -3.2
EUR/USD	+/- 20.0%	-5.3 / 7.9	+/- 10.0%	-1.4 / 2.0

The changes compared to the reported consolidated profit result mainly from financial instruments that are denominated in a foreign currency. Foreign currency exposure is hedged using a macro-hedging approach. In this analysis, it was assumed that all other influencing factors remain equal.

Interest rate risk

The Group is exposed to interest rate risks due to its borrowing at fixed and floating rates. Interest rate risks are a result in particular of variable portions of interest, which depend on current market interest rates; these have an impact on the cash flow from financing activities. The cash flow risk is mainly due to the change in market interest rates. An increase in the market interest rate implies the risk of an increasing negative cash flow from financing activities, and vice versa.

Interest rate swaps were concluded for the variable interest-bearing syndicated loan. The changes in the fair values of interest rate derivatives are recognized in the consolidated income statement.

Sensitivity of interest rate risk

A change of +/- 50 basis points in interest rates as of the reporting date would have decreased/increased equity and the consolidated loss by €5.5 million or €0.1 million (PY: €6.4 million or €4.9 million). The main drivers being the loans and swaps taken out by HENSOLDT. This analysis assumes that all other variables, in particular exchange rates, remain constant.

Liquidity risk

The Group's policy is to maintain sufficient cash and cash equivalents at all times in order to be able to meet current and future obligations when due. The Group manages its liquidity by retaining a sufficient amount of liquid assets.

Adverse developments on the capital markets could increase the Group's borrowing costs and limit its financial flexibility. Management monitors the Group's cash reserves as well as the expected cash flows from operating activities.

The contract terms of the Group's financial liabilities, based on undiscounted cash flows and including interest payments, where applicable, are as follows:

in € million	Carrying amount	Contractual cash flows	< 1 year	1 to 5 years	> 5 years
Non-derivative financial liabilities					
Banks	964.7	1,036.2	383.7	652.5	-
Other	255.6	255.6	255.6	-	-
Derivative financial liabilities					
Interest rate swaps	5.6	5.6	-	5.6	-
Forward exchange transactions	0.8	0.8	0.8	-	-
Lease liability	154.0	205.9	23.5	85.8	96.6
As of December 31, 2020	**1,380.6**	**1,504.1**	**663.6**	**743.9**	**96.6**

in € million	Carrying amount	Contractual cash flows	< 1 year	1 to 5 years	> 5 years
Non-derivative financial liabilities					
Banks	899.0	1,032.3	26.8	1,005.5	-
Other	176.4	176.4	176.4	-	-
Derivative financial liabilities					
Interest rate swaps	9.5	10.0	4.4	5.6	-
Forward exchange transactions	1.4	1.4	1.4	-	-
Lease liability	160.5	222.0	23.0	85.7	113.2
As of December 31, 2019	**1,246.9**	**1,442.1**	**232.1**	**1,096.8**	**113.2**

HENSOLDT Group's liquidity risk relates primarily to the compliance with the financial covenants agreed upon with the banks in the context of corporate financing, which in the course of the restructuring of the liabilities, were renegotiated in 2020.

The Senior Facility Agreement defines target values in relation to certain financial covenants. In case of non-compliance with the covenants, the lenders are entitled to terminate the loan. This could result in a going concern risk for the HENSOLDT Group if no alternative funding would be available at the time when the liabilities to banks fall due. The agreed target values have been set in such a way that the Group only runs the risk of not complying with them in the event of an extreme deterioration of its financial situation. Furthermore, the Group can obtain the banks' approval at an early stage to exceed or fall below the set values. The financial ratios are monitored on an ongoing basis.

The HENSOLDT Group's aim is compliance with the financial covenant at all times and to ensure via monthly simulations of budgets that the financial covenants will be complied with in future quarters.

The probability of occurrence of the risk of non-compliance with financial covenants is considered to be low.

For short-term liquidity management, group-wide rolling liquidity planning, updated bi-weekly, is used and this constitutes the operative instrument for short-term liquidity management of the HENSOLDT Group. Moreover, liquidity is ensured at all times via a revolving credit facility of €350.0 million.

Credit risk

The Group is exposed to a credit risk from non-fulfillment of financial instruments, either by customers or counterparties to the financial instruments. However, the Group prepared guidelines in order to avoid the concentration of credit risks and to ensure that the credit risk remains limited.

Where activities of the central treasury department are affected, the credit risk resulting from financial instruments is managed at group level.

The Group monitors the development of individual financial instruments and the impact of market developments on their performance and takes appropriate measures in the event of foreseeable unfavorable developments on the basis of predefined procedures and escalation levels.

Products and services are sold to customers following a proper internal credit check.

The recognized amount of the financial assets, including contract assets, represents the maximum credit risk.

Assessment of the expected credit losses for customers

The estimated expected credit losses on trade receivables were calculated on the basis of actual credit losses in recent years. Credit risks were segmented according to common credit risk attributes. These are the risk assessments on the basis of rating grades of the Standard & Poor's rating agency and taking into account the geographic location.

The following table includes information on the credit risk and the expected credit losses for trade receivables as well as contract assets as of December 31:

in € million	Rating at Standard & Poor's	Loss rate (weighted average)	Gross carrying amount	Loss allowance	Impaired credit-worthiness
Rating 1-6: low risk	BBB-bis AAA	0.1%	249.4	-0.4	No
Rating 7-9: moderate risk	BB-bis BB+	0.2%	245.3	-0.5	No
Rating 10: below average	B-bis CCC-	1.1%	3.9	-0.0	No
Classification 11: doubtful	C bis CC	-	-	-	Yes
Classification 12: loss	D	-	-	-	Yes
Allowance step 1 and 2				-0.9	
Specific allowance step 3				-11.3	Yes
As of Dec. 31, 2020			**498.6**	**-12.2**	

in € million	Rating at Standard & Poor's	Loss rate (weighted average)	Gross carrying amount	Loss allowance	Impaired credit-worthiness
Rating 1-6: low risk	BBB-bis AAA	0.5%	226.1	-1.0	No
Rating 7-9: moderate risk	BB-bis BB+	0.4%	230.8	-1.0	No
Rating 10: below average	B-bis CCC-	1.1%	14.1	-0.2	No
Classification 11: doubtful	C bis CC	-	-	-	Yes
Classification 12: loss	D	-	-	-	Yes
Allowance step 1 and 2				-2.2	
Specific allowance step 3				-12.0	
As of Dec. 31, 2019			**470.9**	**-14.2**	

in € million	Dec. 31, 2020	Dec. 31, 2019
Contract assets	204.4	165.9
Trade receivables	282.0	290.8
Total	486.4	456.7

The change in loss rates compared with the previous year is mainly due to the shortening of the estimated maturity of the receivables on the basis of actual maturities.

Expected credit losses for other financial assets in the scope of the IFRS 9 impairment requirements have not been recognized due to materiality.

36.2. Carrying amounts and fair values of financial instruments

The Group's financial assets mainly consist of cash, short and medium-term deposits and trade receivables. The financial liabilities include trade payables and payables to financial institutions. All purchases and sales of financial assets are recorded on the settlement date in line with market convention.

Within the Group, derivatives that are not designated as hedging relationships in accordance with IFRS are classified as 'measured at fair value with changes in value recognized through profit or loss'.

The HENSOLDT Group classifies its financial instruments based on their accounting category. The following table includes the carrying amounts and fair values of financial instruments according to class and valuation category as of December 31:

Dec. 31, 2020				
in € million	Category	Carrying amount	Fair value	Level
Assets				
Other investments and other non-current financial assets[1]	FVtOCI	11.3	11.3	-
Other non-current financial assets, due at short-notice	AC	11.2	11.2	-
Trade receivables	AC	240.1	240.1	-
Trade receivables (intented for factoring)[1]	FVtOCI	41.9	41.9	-
Other financial assets:				
Derivative istruments for cash flow hedges	FVtOCI	0.4	0.4	2
Other derivative instruments	FVtPL	5.0	5.0	2
Non-derivative instruments[1]	AC	2.7	2.7	-
Cash and cash equivalents	AC	645.5	645.5	1
Total financial assets		**958.1**	**958.1**	
Liabilities				
Financial liabilities				
Liabilities to banks	FLAC	964.7	971.1	2
Trade payables	FLAC	164.0	164.0	-
Other financial liabilities:				
Other derivative instruments	FVtPL	6.4	6.4	2
Liability from put option	FVtPL	-	-	3
Other miscellanous financial liabilities	FLAC	91.7	91.7	-
Total financial liabilities		**1,226.8**	**1,233.1**	

Dec. 31, 2019				
in € million	Category	Carrying amount	Fair value	Level
Assets				
Other investments and other non-current financial assets[1]	FVtOCI	14.7	14.7	-
Other non-current financial assets, due at short-notice	AC	3.0	3.0	-
Trade receivables	AC	290.8	290.8	-
Other financial assets:				
Other derivative instruments	FVtOCI	0.1	0.1	2
Other derivative instruments	FVtPL	56.3	56.3	2
Non-derivative instruments[1]	AC	2.6	2.6	-
Cash and cash equivalents	AC	137.4	137.4	1
Total financial assets		**504.8**	**504.8**	
Liabilities				
Financial liabilities				
Liabilities to banks	FLAC	899.0	961.9	2
Trade payables	FLAC	168.8	168.8	-
Other financial liabilities:				
Derivative istruments for cash flow hedges	FVtOCI	-	-	
Other derivative instruments	FVtPL	10.9	10.9	2
Liability from put option	FVtPL	-	-	3
Sonstige	FLAC	9.6	9.6	-
Total financial liabilities		**1,088.3**	**1,151.2**	

[1]Fair Value corresponds to cost due to materiality

There is a put option (fair value €0.0) in favor of the non-controlling shareholder of GEW Technologies (Pty) Ltd. (see Note 33.3).

The nominal values of the derivative financial instruments were as follows:

	Remaining term nominal amounts					
	under 1 year		over 1 year		Total	
in € million	2020	2019	2020	2019	2020	2019
Interest rate futures						
Swaps	-	-	920.0	920.0	920.0	920.0
Forward exchange transactions	**-20.4**	**-80.1**	**-5.8**	**-5.8**	**-26.2**	**-86.0**
Average EUR:USD forward rate	*1.22*	*1.14*	*1.23*	*1.17*	-	-
Average EUR:GBP forward rate	*0.90*	*0.85*	-	-	-	-

The fair values of derivative financial instruments were as follows:

	Assets		Liabilities	
	Dec. 31,		Dec. 31,	
in € million	2020	2019	2020	2019
Foreign exchange contracts				
Cashflow Hedges	0.4	0.1	-	-
not designated in a hedging relationship	5.0	5.4	0.8	1.4
Interest rate derivatives				
Component of embedded derivative	-	50.9	-	-
Interest rate swaps	-	-	5.6	9.5
Total	**5.4**	**56.4**	**6.4**	**10.9**

36.3. Disclosures on hedge accounting

The development of hedging instruments for foreign exchange risks recorded in other comprehensive income as of December 31, 2020/2019, is as follows:

in € million	Equity attributable to owners of HENSOLDT AG	Non-controlling interests	Total
As of Jan. 1, 2019	**-3.4**	**-0.2**	**-3.7**
Unrealized valuation gains (+) and losses (-)	-1.4	-0.1	-1.6
Reclassification to consolidated income/loss	1.1	0.1	1.2
Deferred taxes on unrealized valuation gains	-0.3	-0.0	-0.3
Change	**-0.7**	**-0.0**	**-0.7**
As of Dec. 31, 2019	**-4.1**	**-0.3**	**-4.4**
Unrealized valuation gains (+) and losses (-)	-1.7	-0.6	-2.3
Reclassification to consolidated income/loss	0.9	0.1	0.9
Deferred taxes on unrealized valuation gains	0.3	0.1	0.4
Change	**-0.6**	**-0.4**	**-1.0**
As of Dec. 31, 2020	**-4.7**	**-0.7**	**-5.5**

The carrying amount of the derivatives used as hedging instruments is €0.4 million (PY: €0.1 million) and is shown within other financial assets. In the fiscal year, an amount of €0.9 million (PY: €1.0 million) from due cash flow hedges was reclassified from equity primarily to revenue. There were no material inefficiencies from hedging relationships in both 2020 and 2019.

The nominal value of derivative financial instruments used as hedging instruments amounts to €0.4 million (PY: €0.5 million) and has a maturity of less than one year.

36.4. Net gains or net losses

The following net gains or net losses on measurement of the financial assets and financial liabilities were recognized in profit or loss in 2020 and 2019.

	Fiscal year	
in € million	2020	2019
Financial assets or liabilities at fair value through profit or loss	-45.8	56.1
Financial assets at amortized costs	-4.3	-1.3
Financial liabilities at amortized costs	-63.5	-59.6
Net gains or net losses	**-113.6**	**-4.8**

36.5. Impairment losses

The following impairment losses on financial assets were recognized in profit or loss in 2020 and 2019:

in € million	Category	2020	2019
Impairment losses for:			
Trade receivables and contract assets (Stage 1 and 2)	AC	0.9	0.9
Trade receivables and contract assets (Stage 3)	AC	2.9	4.6
Impairment losses (gross) on financial assets and contract assets		**3.8**	**5.5**
Reversals of impairment losses		-1.6	-1.4
Impairment losses (net) on financial assets and contract assets		**2.3**	**4.1**

VII. Additional comments

37. Auditor's fee and services

The HENSOLDT Group, its subsidiaries and other companies included in the consolidated financial statements recognized the following expenses for the fees and services of KPMG AG for the fiscal years 2020 and 2019:

	Parent company		Subsidiaries		Total	
	Fiscal year		Fiscal year		Fiscal year	
in € million	2020	2019	2020	2019	2020	2019
Audit services	0.5	0.3	0.5	0.5	1.0	0.8
Other assurance services	0.5	-	0.2	0.2	0.7	0.2
Tax advisory services	0.2	-	0.1	0.1	0.3	0.1
Other services	0.1	-	0.8	0.6	0.9	0.6
Total	**1.3**	**0.3**	**1.6**	**1.4**	**2.9**	**1.7**

The fees for the audit services provided by KPMG AG were mainly related to the audit of the consolidated financial statements of the Group and the annual financial statements together with the combined management report, the management report of HENSOLDT AG as well as the annual reports of its subsidiaries including statutory extensions of the engagement.

Fees for the other assurance services mainly relate to the issuance of comfort letters and other contractually agreed upon assurance services in conjunction with the Company's IPO like the review of the Company's interim financial statement.

Furthermore, tax advisory services were provided in connection with business acquisitions. In addition, KPMG AG provided other quality assurance services in connection with the IPO and consulting services in connection with financial due diligence (buyer´s side).

38. Future payment obligations

There were purchase commitments especially for inventories and services in the amount of €658.7 million as of December 31, 2020 (PY: €253.5 million).

39. Events after the reporting date

For information on acquisitions after the balance sheet date, please refer to Note II.7.1

The Executive Board and the Supervisory Board propose the distribution of a dividend of €0.13 per share to holders entitled to dividends. This corresponds to an expected total payment of around €13.7 million. The payment of the proposed dividend is subject to the approval of the Annual General Meeting.

There were no other significant events after the reporting date.

HENSOLDT AG

Management

Thomas Müller	Axel Salzmann	Peter Fieser

HENSOLDT Group

Taufkirchen, District of Munich

Combined Management Report

for the year ended December 31, 2020

Content

I. Group fundamentals

1. Business model

The HENSOLDT Group (the “Group”, “HENSOLDT”) is a high-tech pioneer and specialized provider of defense and security sensor solutions, with a portfolio focus on high-performance sensors in the fields of radars, electronic warfare, avionics and optronics. The product portfolio as of December 31, 2020, included a variety of products with a lifecycle of ten years or more. HENSOLDT is constantly striving to increase and improve the current product offering through its own developments, industrial cooperation and acquisitions, in order to increase competitiveness and expand into new markets.

2. Organization and group structure

2.1. Legal structure

The HENSOLDT Group consists of HENSOLDT AG (the “Company”) with statutory seat in Taufkirchen, Germany (registered office: Willy-Messerschmitt-Str. 3, 82024 Taufkirchen, Germany, under file no. HRB 258711, Munich Local Court) and its subsidiaries. With registration in the commercial register on August 17, 2020, HENSOLDT GmbH was converted into HENSOLDT AG.

The consolidated financial statements include the financial statements of HENSOLDT AG and the financial statements of all significant subsidiaries directly and indirectly controlled by HENSOLDT AG. 32 entities (PY: 32) were fully consolidated. One entity was included in the Group using the equity method.

In preparation for the initial public offering (“IPO”) in the third quarter of 2020, the transformation of the legal form of HENSOLDT GmbH into a stock corporation (AG) was executed. The reporting for HENSOLDT AG is included in the Combined Management Report in chapter “X HENSOLDT AG”.

2.2. Locations and employees

HENSOLDT’s headquarters are located in Taufkirchen near Munich, an important innovation center of the defense industry in Germany. In addition, business activities in Germany are conducted in Ulm, Oberkochen and Pforzheim in particular. Other locations in Germany include Wetzlar, Immenstaad and Kiel. As of December 31, 2020, of the 5,605 (PY: 5,461) employees of HENSOLDT, among them 430 (PY: 410) trainees, interns etc., approx. 4,100 (PY: 4,000) were employed in Germany. HENSOLDT’s larger locations outside Germany are mainly located in France, South Africa and the UK.

2.3. Operating segments

The HENSOLDT Group’s segmentation corresponds to its internal steering, controlling and reporting structures. In accordance with IFRS 8, HENSOLDT has identified the reportable segments Sensors and Optronics.

Sensors segment

The Sensors segment provides system solutions and comprises the three divisions Radar, Identification Friend or Foe (“IFF”) & Data Communications (“COMMS”), Spectrum Dominance & Airborne Solutions, and Customer Services, as well as Others/Elimination. The solutions of the Radar, IFF & COMMS and the Spectrum Dominance & Airborne Solutions divisions are complementary in the value chain, resulting in interdependencies between the two such as shared engineering and operations. As an aftersales division, the Customer Services division is positioned further down the value chain and largely dependent on the primary business of the other two divisions of the Sensors segment.

Radar, IFF & COMMS

Within the Radar, IFF & COMMS division, the Group develops and manufactures mobile and stationary radar and IFF systems used for surveillance, reconnaissance, air traffic control (ATC) and air defense. These systems are deployed on various platforms, including the Eurofighter, the German Navy's Frigate 125 and the US Navy's Littoral Combat Ship. The Radar, IFF & COMMS division also includes systems for establishing secure data connections for air, sea and land platforms.

Spectrum Dominance & Airborne Solutions

The Spectrum Dominance & Airborne Solutions division includes electronic systems for the acquisition and evaluation of radar and radio signals and jammers, which are used, for example, to protect convoys or individual vehicles against improvised explosive devices. In addition to applications on the electromagnetic spectrum for land, sea and air applications, the product range is being extended to include defensive cyber-solutions. Furthermore, the Group offers electronic self-protection systems integrating missile, laser and radar warning sensors with countermeasures for air, sea and ground platforms and provides military and civil avionics systems such as situational awareness systems, mission computers and flight data recorders. Systems from the Spectrum Dominance & Airborne Solutions division are used in fighter aircraft such as the Eurofighter and Tornado, the Airbus A400M transport aircraft and various helicopter models.

Customer Services

The Customer Services division encompasses a range of customer support and service activities, as well as maintenance over the entire lifecycle of the platforms and systems developed in the other two divisions of the Sensors segment. Simulation solutions, training courses and special services are also offered within this division.

Others/Elimination includes others, mainly comprising components for anti-aircraft missile defense systems, funded military studies and funding projects, and the elimination of intra-segment revenue between the three divisions of the Sensors segment.

Optronics segment

The Optronics segment comprises optronics and optical and precision instruments for military, security and civil applications that can be used on land, in water and in the air. On land, the product range includes rifle scopes, sights, laser rangefinders, night vision devices, and thermal imaging cameras that assist snipers and infantry soldiers with observation and target acquisition. In addition, devices for surveillance and target acquisition are offered for armored vehicles. For use at sea, submarine periscopes, optronic mast systems and other electro-optical systems are offered. In the air, the product portfolio includes stabilized sensor platforms with image stabilizers for helicopters, manned fixed-wing aircraft and drones, which support their surveillance and target acquisition. HENSOLDT also offers mobile and stationary surveillance solutions for security applications, as well as special equipment for industrial and space applications within this segment. Further, support and services for Optronics products forms part of the Optronics segment.

3. Goals and Strategies

The long-term goal for HENSOLDT is to become Europe's leading, platform-independent provider of defense and security sensor solutions with global reach. To achieve this, HENSOLDT developed a comprehensive strategic framework to promote its growth and business improvement strategy. The framework consists of the following five key components: innovation, customer, continuous improvement, strategic acquisitions and business culture.

3.1. Innovation

The development of high-performance sensor electronics is at the core of the HENSOLDT DNA. The technology portfolio is developed by nearly 1,900 engineers in all divisions at all locations. The widespread experience among the engineers paired with their long tenure at HENSOLDT play a key role in the quality and consistency of the research and development ("R&D") efforts and the products and solutions the Group develops. HENSOLDT develops products and technologies for specific customer platforms and further invests in the product portfolio, leading to greater independence from specific customers and platforms. Compared to 2017, HENSOLDT increased self-funded R&D expenditure (including R&D costs and capitalized development costs) by 75.5 % in the fiscal year. In 2020, self-funded R&D expenditure for HENSOLDT was €87.2 million.

The combination of existing and newly developed technologies enables HENSOLDT to address additional markets and customer segments. An example is the Xpeller counter-UAV system, which combines know-how and products from across the HENSOLDT Group and can be used as multi-sensor fusion system against modern threats posed by unmanned aircraft and for the protection of airports, critical infrastructures or events. Another example for HENSOLDT's innovative capacity is the production of the world's first 3D-printed circuit board with ten layers in cooperation with the business partner Nano Dimension in 2020.

3.2. Customer

It is HENSOLDT's goal to become a long-term partner for its customers. In order to achieve this, the Company focuses on two pillars: the bundling of technologies into comprehensive solutions for its customers, and the creation and maintenance of customer intimacy through its global sales force and service stations.

In addition to the focus on offering long-term platform integration, HENSOLDT follows a dedicated regional strategy, building on customer intimacy created through the global sales network to grow the geographically addressable market.

For the Company's home country Germany, the long-term growth strategy is focused on positioning HENSOLDT on new European programs and capturing the anticipated increases in defense spending and, simultaneously, the shift to electronic content in such spending. The Company aims to leverage its status as a supplier of sensitive technologies and to secure the inclusion in platforms through partnerships with leading defense contractors.

The export strategy is centered on leveraging home country technologies for worldwide distribution. The Company aims to position itself in the most attractive markets by creating local proximity, increasing international business operations, and building local partnerships to support sales campaigns.

In order to achieve the goal of developing customer relationships domestically and abroad, HENSOLDT built up a sales organization which as of December 31, 2020, had around 100 FTEs distributed among the sales centers in Europe, the Middle East, Asia-Pacific, Africa, North America and Latin America.

3.3. Continuous Improvement

Driven by a culture of continuous improvement, HENSOLDT aims to create further value through enhanced project execution.

Since the carve-out from Airbus, the Company launched an extensive program under the name “HENSOLDT GO!” which has already delivered a number of improvements to date and continues to drive operational progress. In the area of continuous improvements HENSOLDT already almost optimized the operation and development efficiency as well as the procurement organization. In the future the Company intends to focus on enhancing production, further boosting development efficiency, and improving supply chain management. In the area of central functions HENSOLDT was already able to increase the efficiency of the general administrative functions.

3.4. Strategic Acquisitions

HENSOLDT uses acquisitions to speed up growth and has a clear M&A strategy to identify the right targets, which follows four key aspects:

- Accessing new and disruptive technologies, especially in the areas of artificial intelligence (AI), data fusion and analytics, autonomous capabilities, as well as intelligence and cyber.
- Strengthening the focus regions and entering into new markets, particularly in Europe, Asia-Pacific and North America.
- Expanding the product portfolio, especially solution offerings, connectivity and communication, lower-end security products and other sensor capabilities complimentary to the existing portfolio.
- Increasing corporate value and scale from consolidation by leveraging HENSOLDT’s current position in Germany and joining forces with partners in Europe.

HENSOLDT has made a number of acquisitions since its carve-out from Airbus, each with a unique strategic rationale. Since 2018, the following acquisitions have been made:

- The largest acquisition thus far – the Nexeya Group – not only provided an addition to the product portfolio through its test and integration services, but also access to the French regional market.
- The reason for acquiring HENSOLDT Australia Pty Ltd (formerly: IE Asia-Pacific Pty Ltd) was predominantly a regional expansion to Australia and the expansion of the product portfolio by offering local customer support services.
- The purchase of two business units (ATM and Defence Division) of Tellumat Proprietary Limited not only enabled a South African expansion and access to new regional markets but also strengthened the technology portfolio, specifically for radar offerings in South African locations.
- The acquisition of SAIL LABS Technology GmbH in the first quarter of 2021 supplements the existing capabilities in signal reconnaissance with the increasingly important segment of open source intelligence.

3.5. Corporate Culture

HENSOLDT strives for a culture of mutual success, which is predominantly characterized by the diversity of its employees. Overarching cooperation between all stakeholders, paired with demand for excellence, personal responsibility and innovation spirit create the entrepreneurship, which lays the foundation for continued success.

Other key aspects of the corporate culture are the responsible treatment of employees, protection of natural resources and integrity of management. An extensive description of these topics can be found in the separate sustainability report. The sustainability report for the fiscal year 2020 is published simultaneously with the annual report and can then be found on the HENSOLDT website.

4. Financial performance indicators

HENSOLDT uses certain key performance indicators ("KPIs") to measure performance, identify trends and make strategic decisions. Besides revenue, the most important KPIs are order intake and adjusted EBITDA[1]. In addition, HENSOLDT uses two more non-IFRS performance indicators, the adjusted pre-tax unlevered free cash flow[2] and the adjusted EBIT[3], as well as one additional operating metric (besides order intake), the order backlog as performance indicator. In the first half of 2020, the adjusted pre-tax unlevered free cash flow was added to the steering system. In connection with the IPO, the importance of adjusted EBITDA has increased, which is also reflected accordingly in the financial reporting.

Adjusted EBITDA is used as a key indicator of the economic performance of the Group, in particular to illustrate the non-recurring effects on the operating results from acquisitions and other non-recurring effects. In addition, non-financial performance indicators are partly used to manage the Group. To this end, starting in the fiscal year 2021, an additional remuneration element geared towards long-term, sustainable success of the HENSOLDT Group will be included in the management remuneration (see chapter V. "Non-financial group statement").

Performance Indicators

	Fiscal year		
€ million	2020	2019	% Change
Revenues	1,206.9	1,114.2	8.3%
Adjusted EBITDA	219.3	215.6	1.7%
Adjusted EBIT	167.2	160.8	4.0%
Adjusted pre-tax unlevered free cash flow	196.4	74.9	162.2%
Order intake	2,541.3	1,040.0	144.3%
Order backlog	3,424.0	2,202.3	55.5%

5. Research and Development

Research and development in the HENSOLDT Group comprises both product-specific developments and general research and development activities that concentrate on basic research and product innovation.

R&D costs amounted to €25.1 million in fiscal year 2020 (PY: €31.0 million). This corresponds to 2.1 % of revenue (PY: 2.8 %). This does not include capitalized development costs of €62.1 million in the reporting year (PY: €55.1 million), with the increase being in particular due to air traffic control and naval & ground radar programs within the Sensors segment and land, sea and air programs within the Optronics segment. This reflects a capitalization rate of 71.2 % (PY: 64.0 %) in terms of total research and

[1] Defined as EBIT adjusted for depreciation and amortization (including effects on earnings from purchase price allocations), as well as certain non-recurring effects relating to transaction costs, separation costs, and other non-recurring effects.
[2] Defined as free cash flow adjusted for non-recurring effects as well as interest, tax and M&A activities. The free cash flow is defined as sum of the cash flows from operating and investing activities as reported in the consolidated statement of cash flows.
[3] Defined as EBIT adjusted for certain non-recurring effects relating to transaction costs, separation costs, and other non-recurring effects.

development spend of €87.2 million (PY: €86.1 million). Amortization of capitalized development costs amounted to €9.0 million in the fiscal year (PY: €9.7 million).

6. HENSOLDT on the capital market

The IPO of HENSOLDT AG in 2020 represented an important milestone in the Company's history.

In the preparation for the IPO, the CEO and CFO held talks with many institutional investors as part of a virtual roadshow. During this process, HENSOLDT was supported by BofA Securities, J.P. Morgan, KKR Capital Markets, as well as Deutsche Bank, which operated as Joint Global Coordinators and Joint Bookrunners. Citigroup, COMMERZBANK, UniCredit Bank AG and Crédit Agricole CIB were mandated as further Joint Bookrunners. Mizuho International plc accompanied the transaction as Co-Lead-Manager. The role of the Designated Sponsor was taken over by J.P Morgan.

On September 23, 2020, the final allotment price for the shares of HENSOLDT AG was set at €12.00 per share and a total of 33,333,333 bearer shares with no par value (plus additional shares to cover potential over-allotments) were placed to investors. On September 25, 2020, trading in the Prime Standard of the Frankfurt Stock Exchange commenced. Starting with an opening price of €12.00 at XETRA, the share price of HENSOLDT AG rose to €14.70 (December 15, 2020) over the course of the year 2020 and closed at €13.95 on the last trading day of the year. At end of trading on December 30, 2020, HENSOLDT AG had a market capitalization of almost €1.5 billion.

Development of the share price

With the inclusion of HENSOLDT AG in the SDAX, the small-cap index of the Frankfurt Stock Exchange, the Company's successful growth was recognized on the trading floor and beyond. The announcement of the exercise of the German federal government's acquisition right for 25.1 % of the shares of HENSOLDT AG currently still held by KKR is further proof of the great confidence in the capabilities of HENSOLDT and its role as central supplier of key technologies for the security and defense sector. Thus, the Company gains further visibility on the capital market and, with the Federal Republic of Germany, obtains a strong long-term oriented cornerstone shareholder.

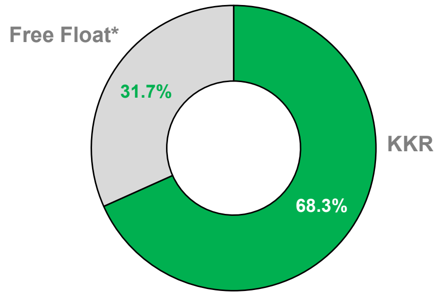
Shareholder structure

Square Lux Holding II S.à r.l., a KKR company, held approximately 68.3 % of the shares of HENSOLDT AG as of December 31, 2020. Thus the free float of shares was at 31.7 %.

On December 17, 2020, the Federal Republic of Germany announced that it would exercise the granted acquisition right for 25.1 % of the shares – the acquisition shall take place in 2021.

On September 30, 2020, HENSOLDT AG was informed by means of a voting rights notification that CI Investments Inc. exceeded the 3 % voting rights notification threshold on September 30, 2020.

Shareholders structure of HENSOLDT AG as of December 31, 2020



* Free Float includes all shares that are not held by major shareholders (share of more than 5 % in the share capital) (definition of Deutsche Börse AG).

Analyst Coverage

At the end of 2020, the following well-known national and international banks and local research houses were monitoring and evaluating the HENSOLDT stock:

- Bank of America Securities
- KEPLER CHEUVREUX / UniCredit
- COMMERZBANK
- Citigroup
- Deutsche Bank
- J.P. Morgan
- Warburg Research

All seven analysts issued a buy recommendation at the start of their coverage. This remained unchanged until the end of 2020. Based on existing inquiries, it can be assumed that further analysts will initiate coverage in 2021.

Investor Relations – Communication with the capital market

HENSOLDT strives to maintain a transparent and continuous dialogue with the capital market. Therefore, it is an important concern of HENSOLDT to constantly deepen the relationship with investors, analysts and financial journalists through individual meetings, telephone calls, roadshows, conferences as well as Company visits (if possible) and to expand the confidence of capital market participants in the Company. In the fiscal year 2020, the Management Board held an analyst call following the publication of the 9-month financial figures and presented the recent developments of the Company, the current business performance and the growth prospects to institutional investors and analysts.

In addition, 14 virtual investor and analyst meetings were held following the publication of the financial figures for the third quarter. In order to meet the requirements of the capital market, another focus was on establishing the necessary structures and processes in the area of investor relations.

Basic information and key data on HENSOLDT shares in 2020

ISIN:	DE000HAG0005
WKN:	HAG000
Symbol:	HAG
Stock exchange listing:	Frankfurter Stock Exchange
Stock exchange segment:	Regulated market (Prime Standard)
Index:	SDAX
Designated Sponsor:	J.P. Morgan
Number of shares:	105,000,000

Share type:	Bearer shares without par value (no par value shares)
Highest share price in Xetra-trading in €:	14.70
Lowest share price in Xetra-trading in €:	9.71
Closing share price in Xetra-trading (December, 30 2020) in €:	13.95
Market capitalization (December 30, 2020) in €:	1.465 billion
Free float (December 31, 2020):	31.7 %

II. Economic report

1. Economic conditions

1.1. General economic conditions

In its press release on the economic situation in Germany in January 2021, the German federal government published a price-adjusted German GDP decline of 5.0 % for 2020. This signaled a strong hit by the 2020 coronavirus crisis on the German economy after ten successive years of expansion (Source: Federal Statistical Office, January 14, 2021). This was predominantly driven by a reduction in private spending and investments, while the increase in public spending had a stabilizing effect. Simultaneously, the coronavirus SARS-CoV-2 (“COVID-19”) pandemic negatively impacted the labor market, with employee salaries declining to a significantly lesser extent than corporate and property income. The COVID-19 pandemic had a considerable impact on foreign trade and caused the first reduction in exports and imports since 2009.

Value creation declined in almost all parts of the economy. The production industry (excluding construction), in particular, as well as the service industry experienced significant declines, whereas the construction industry actually reported an increase in value added. This led the German economy into a deep recession. There are first indicators, however, that the German economy was hit less severely by the lockdown toward the end of 2020 when compared with the spring lockdown. The impact of tightened COVID-19 measures as well as the governmental support measures will be key decisive factors for the future economic development. However, in an international comparison, the German economy seems to have fared relatively well throughout the crisis (Source: Federal Statistical Office, January 14, 2021).

The International Monetary Fund’s (“IMF”) World Economic Outlook from January 2021 projects the global economy to grow by 5.5 % in 2021 (2020: -3.5 %), an increase of 0.3 percentage points compared to the October 2020 forecast (Source: World Economic Outlook (“WEO”), January 2021).

According to the IMF, the global economy is slowly recovering from the effects of the COVID-19 pandemic, although renewed lockdowns to protect the population are having a decelerating effect. The speed of recovery will vary considerably from country to country. In this context, economic data released after the October 2020 forecast suggest that economic activity in the second half of 2020 will be, on average, stronger than forecast in all regions. GDP results for the third quarter were mostly positively or in line with expectations. Private consumption showed the strongest recovery, while investments – with the exception of China – recovered relatively slowly.

The downturn triggered by the COVID-19 pandemic differs significantly from past recessions. In contrast to previous crises, a more pronounced decline in the service sector than in manufacturing is apparent for 2020 (Source: WEO, October 2020). In 2020, global trade is expected to contract by over 9.6 % and fall back on a level seen during the 2009 global financial crisis. However, in line with the recovery of the global economy, world trade volume is forecast to grow by around 8.1 % in 2021 before slowing to 6.3 % in 2022 (Source: WEO, January 2021).

After the recovery in 2021, global growth is expected to stabilize at around 3.5 % in the medium term. This implies only limited progress in achieving pre-pandemic forecasts, both for the industrialized countries and for emerging and developing countries. While growth in the USA is expected to be at 5.1 % in 2021 (2020: -3.4 %), the eurozone expects an increase of 4.2 % in 2021 (2020: -7.2 %). Recovery in China has been faster than expected, which is why growth is expected to increase to 8.1 % in 2021 (2020: 2.3 %). The uncertainties in these forecasts are unusually high due to the ongoing pandemic (Source: WEO, January 2021).

1.2. Conditions in the defense and security sector

The global security situation remains tense, which is also reflected in increasing defense spending worldwide. Developments in Germany, Europe and other NATO members are particularly relevant for HENSOLDT. In principle, NATO members continue to work to achieve the goals formulated at the NATO Summit in Wales in 2014. An important aspect is the declaration of intent to move toward a defense spending of 2.0 % of GDP. This goal was reaffirmed by the NATO foreign ministers' statement on the occasion of NATO's 70th anniversary in April 2019. The economic consequences caused by the COVID-19 pandemic, however, put pressure on national budgets for defense. Because effects on budget planning generally occur with some delay, many NATO members have not seen immediate negative effects on defense spending in 2020. These effects are expected from 2021 onwards.

In 2017, Germany and France agreed on intensive cooperation for defense projects. They are jointly developing several platforms, such as the Future Combat Air System ("FCAS") (together with Spain), the Main Ground Combat System ("MGCS"), and the Maritime Airborne Warfare System ("MAWS"). Germany and France committed to the development of the FCAS in April 2018, with Spain joining in 2019. In February 2020, with the award of an initial framework contract, the three countries officially launched the demonstrator phase of the FCAS, which is expected to culminate in the development of the first test aircraft by 2026. The technology maturation phase, which comprises the development of demonstrators, is expected to last until about 2026, with expected first orders and start of production thereafter. As part of the FCAS, an unmanned weapon carrier is expected to be developed from the mid-2020s onwards. From 2040 onwards, this is supposed to successively take over all offensive and defensive air operations. HENSOLDT as consortium leader, together with Diehl Defence, ESG and Rohde & Schwarz, is part of the Future Combat Mission System (FCMS) consortium, which has assumed joint responsibility for the complex topic of the networked use of sensors and effectors in the FCAS project (Source: Report of the Federal Ministry of Defense (BMVg) on armament matters, December 2020).

The binational agreement between France and Germany on arms exports was adopted in 2019 and has already been partially implemented. The implementation of joint regulations on the export of defense equipment through industrial cooperation is still pending. The agreement is one aspect of the "Aachen Treaty" signed in 2019. According to the provisions of the treaty, both countries also intend to develop a joint strategic framework in respect of military deployment and drive the consolidation of the European defense industry. To this end, a new Franco-German defense and security council is to be established which shall meet regularly and steer collaboration.

For HENSOLDT, bilateral and multilateral cooperation projects offer a long-term strategic perspective in terms of product development and high-volume procurements.

2. Business development

Over the past few months, HENSOLDT has monitored the situation around the COVID-19 pandemic at all sites with the objective of protecting the health and well-being of all employees, customers, partners as well as securing the business. The local business continuity management teams have reviewed and updated their plans accordingly to enable maximum resilience of business activities. Key processes were tested and changed if necessary to not only ensure ongoing operations but also minimize the spread of the virus. As part of the COVID-19 action plan, HENSOLDT has decided to fully draw the previously unused revolving credit facility ("RCF").

So far, despite short-term plant closures, the COVID-19 pandemic has not significantly influenced HENSOLDT's business as a provider of defense and security electronics. Apart from delays and postponements in the project business, there have been neither formal cancellations of large orders from defense sector customers nor significant effects on the order backlog or future prospects in the defense sector due to the pandemic.

HENSOLDT AG successfully completed its IPO in the third quarter of 2020. In preparation of the IPO, the share capital was increased in August 2020 by €70.0 million from the capital reserve and the legal form was changed from HENSOLDT GmbH, a limited liability company, to a stock corporation (AG). The issue of new shares led to a gross increase in equity by €300.0 million. The proceeds from the primary offering were used to strengthen the capitalization of, and to deleverage, the HENSOLDT Group. In connection with the IPO, HENSOLDT replaced its existing debt financing with a new facilities agreement comprising a new term loan of €600.0 million and a new revolving credit facility of €350.0 million, which has been still fully drawn.

Overall, HENSOLDT Group's business operations were marked by ongoing profitable developments in 2020. During the reporting year, HENSOLDT won a number of major contracts, in particular large orders of €1.5 billion for the joint development and production of the Eurofighter Common Radar System Mk1. Revenue saw a significant rise of 8.3 % (€1,206.9 million; PY: €1,114.2 million), which was mainly attributable to the acquisition of Nexeya in October 2019 and revenue from the Eurofighter Common Radar System Mk1. Adjusted EBITDA improved by 1.7 % (€219.3 million; PY: €215.6 million). To a large extent, this resulted from an improved gross profit due to higher revenue as well as decreased development costs not eligible for capitalization. These effects were, however, partly neutralized by higher functional costs.

3. Assets, liabilities, financial position and financial performance

3.1. Financial Performance

Order intake, revenue and order backlog

	Order intake			Revenues			Order backlog		
	Fiscal year			Fiscal year			Dec. 31,	Dec. 31,	
in € million	2020	2019	% Change	2020	2019	% Change	2020	2019	% Change
Sensors	2,238.1	657.5	>200%	923.6	837.1	10.3%	2,825.5	1,567.8	80.2%
Optronics	308.3	383.3	-19.6%	288.1	277.4	3.9%	600.0	634.5	-5.4%
Elimination / Transversal / Others	-5.1	-0.8		-4.8	-0.3		-1.5	-	
HENSOLDT	**2,541.3**	**1,040.0**	**144.3%**	**1,206.9**	**1,114.2**	**8.3%**	**3,424.0**	**2,202.3**	**55.5%**

Order intake

Despite delays and postponements in project business due to the COVID-19 pandemic, order intake at a Group level increased significantly, mainly as a result of the strong increase in order intake in the Sensors segment.

Growth within the Sensors segment was mainly driven by major orders worth over €1.5 billion for the Eurofighter Common Radar System Mk1. Within the Sensors segment, 78.5 % (PY: 26.8 %) was attributable to the Radar, IFF & COMMS division. The Spectrum Dominance & Airborne Solutions division accounted for 10.6 % (PY: 45.0 %) of order intake and 10.6 % (PY: 28.0 %) was attributable to the Customer Services division.

The overall decrease in order intake within the Optronics segment compared to the previous year resulted from lower order intake in the Naval and Ground Based Systems product lines, which was only partially offset by higher order intake in the South African company. The decrease seen in the Naval product line is mainly due to some significant orders which had been won in the previous year.

Revenue

Revenue increased significantly, primarily due to the acquisition of the Nexeya business in October 2019 and the revenue generated by the Eurofighter Common Radar System Mk1. This was offset to a limited extent by delays and postponements of order intake due to the COVID-19 pandemic.

The growth within the Sensors segment was mainly driven by the Radar, IFF & COMMS and the Customer Services divisions. Within the Sensors segment, the Radar, IFF & COMMS division contributed 42.8 % (PY: 43.2 %) and the Spectrum Dominance & Airborne Solutions division contributed 27.4 % (PY: 33.0 %) to revenue. The rise in revenue within the Radar, IFF & COMMS division is predominantly the result of higher revenue with Eurofighter radars and was partially offset by lower revenue in the Surveillance Radars and Air Traffic Control product lines. There has been a slight decline of revenue in the Spectrum Dominance & Airborne Solutions division in the fiscal year. The Customer Services division was responsible for 29.4 % (PY: 23.0 %) of revenue with the acquisition of the Nexeya Group sontributing an amount in the mid €60 million range to this increase.

In the Optronics segment, the growth in the Industrial Commercial Solutions and Aerospace & Protection product lines was partially offset by lower revenue in the Naval product line and the South African subsidiary.

Order backlog

The order backlog at Group level rose sharply driven by high order intake in Sensors segment.

Within the Sensors segment, 72.5 % (PY: 45.9 %) of order backlog was attributable to the Radar, IFF & COMMS division. The increase compared to the previous year was mainly caused by the order intake for the Eurofighter Common Radar System Mk1. 14.9 % (PY: 28.6 %) was attributed to the Spectrum Dominance & Airborne Solutions division and 12.1 % (PY: 23.7 %) was attributable to the Customer Services division.

Despite a book-to-bill ratio of more than 1, the Optronics segment saw an overall decrease on account of an order being cancelled because export clearance had unexpectedly not been granted.

Earnings[4]

	Profit			Profit margin	
	Fiscal year			Fiscal year	
in € million	2020	2019	% Change	2020	2019
Sensors	156.2	162.5	-3.8%	16.9%	19.4%
Optronics	65.6	54.3	20.9%	22.8%	19.6%
Elimination / Transversal / Others	-2.5	-1.2			
Adjusted EBITDA	**219.3**	**215.6**	**1.7%**	**18.2%**	**19.3%**
Depreciation and amortization	-120.8	-133.8			
Non-recurring effects	-30.0	-19.7			
Earnings before finance result and income taxes (EBIT)	**68.5**	**62.1**	**10.3%**	**5.7%**	**5.6%**
Finance result	-143.7	-26.5			
Income taxes	10.7	-27.4			
Group result	**-64.5**	**8.2**	**>-200%**		
Earnings per share					
Basic and diluted earnings per share (EUR)	-0.75	0.07			

Adjusted EBITDA

Adjusted EBITDA increased slightly compared to the previous year, mainly as a result of improved gross profit due to higher revenue and lower development costs not eligible for capitalization. These effects were partly offset by higher functional costs.

The slight decrease in adjusted EBITDA in the Sensors segment is predominantly due to a declining gross margin because of lower project margins for pass-through revenue. In addition, there was an increase in functional costs mainly due to the acquisition of the Nexeya group in October of the previous year, higher bid budgets and the costs of the global sales organization being fully included for the first time. Those effects were partially offset by lower development costs not eligible for capitalization.

The increase in adjusted EBITDA in the Optronics segment compared to the prior year can largely be explained by the improved gross margin due to higher revenue and efficient project management.

[4] The profit margins are calculated in relation to the corresponding revenue.

Earnings before interest and tax (EBIT)

Lower amortization of intangible assets led to an overall decrease in amortization. The non-recurring effects[5] included in the EBIT increased due to higher other non-recurring effects in administration costs, which mainly resulted from preparations for the IPO.

Group result

The lower earnings and increased expenses in the financial result are mainly caused by a change in fair value of a derivative embedded in the Term Loan repaid on September 30, 2020, which was recognized in the income statement under interest expense in accordance with IFRS 9, in the amount of €50.9 million (PY: interest income of €54.2 million) . Further, there were expenses due to the premature repayment of the replaced long-term loan in the amount of €27.9 million. The figures of the previous year included interest payments for former shareholder loans, while no such payments were recognized in the reporting year.

In the reporting year, income of €10.7 million (PY: expenses of €27.4 million) was recognized under income taxes. This includes a current income tax expense of €9.4 million (PY: €8.8 million) and an effect from deferred tax income of €20.1 million (PY: expenses of €18.6 million). The deferred tax income for the current year relates to the change in temporary differences amounting to €12.4 million and the utilization of deferred tax assets for loss and interest carryforwards in the amount of €7.7 million.

Earnings per Share

Earnings per share decreased from €0.07[6] in the previous year to €-0.75, predominantly due to a decline in the financial result and an increase in non-recurring effects.

The Management Board intends to propose to the Supervisory Board the distribution of a dividend of €0.13 per share to shareholders entitled to such dividends. This corresponds to an expected total payment of around €13.7 million. Payment of the proposed dividend is subject to approval by the shareholders' meeting.

Overall Assessment

The Management Board assessed the overall economic performance as positive. Despite the temporarily challenging environment due to the COVID-19 pandemic, the revised but still ambitious targets[7] for sales and order intake were achieved. Due to the achieved increase in business volume and the consistent implementation of efficiency improvement measures, adjusted EBITDA fully met the revised expectations.[8]

[5] Includes transaction costs, separation costs and other non-recurring effects.
[6] Calculated on the basis of the number of shares at the time of the change of the legal form of HENSOLDT AG
[7] In the first half of the year, the planning for the reporting year was revised to take account of the business and economic environment including the impact of the COVID-19 pandemic. In addition, adjusted EBITDA replaced adjusted EBIT as one of the most important KPIs.
[8] Regarding adjusted EBIT, a slight increase was achieved compared to the previous year.

3.2. Asset position

in € million	Dec. 31, 2020	Dec. 31, 2019	% Change
Non-current assets	1,313.4	1,392.6	-5.7%
therein: Goodwill	*637.2*	*637.2*	*0.0%*
therein: Intangible assets	*386.2*	*403.3*	*-4.2%*
therein: Property, plant and equipment	*103.1*	*92.9*	*10.9%*
therein: Right-of-use assets	*143.5*	*154.9*	*-7.3%*
therein: Non-current other financial assets	*1.0*	*53.2*	*-98.2%*
Current assets	1,634.2	1,063.1	53.7%
therein: Inventories	*403.7*	*411.1*	*-1.8%*
therein: Contract assets	*204.4*	*165.9*	*23.2%*
therein: Trade receivables	*282.0*	*290.8*	*-3.0%*
therein: Other current assets	*78.7*	*46.1*	*70.8%*
therein: Cash and cash equivalents	*645.5*	*137.4*	*>200%*
Total assets	**2,947.6**	**2,455.7**	**20.0%**

As of December 31, 2020, assets increased by 20.0 % to €2,947.6 million. The rise resulted from the increase in current assets by €571.1 million or 53.7 %, but was partly compensated by the decrease in non-current assets by €79.2 million or 5.7 %.

This decrease from €1,392.6 million as of December 31, 2019, to €1,313.4 million as of December 31, 2020, was mainly due to the derecognition of the derivative embedded in the replaced long-term loan in the amount of €50.9 million, which had previously been reported under other non-current financial assets. Intangible assets decreased mainly due to the amortization of assets from acquisitions and capitalized development costs in the amount of €79.5 million (PY: €91.5 million), which was partially offset by the capitalization of development costs in 2020 in the amount of €62.1 million (PY: €55.1 million). The increase in property, plant and equipment resulted, in particular, from higher investments in technical equipment and machinery, of €16.7 million (PY: €8.8 million), and other equipment, factory and office equipment of €7.6 million (previous year: €6.4 million), and was partially offset by depreciation.

In contrast to non-current assets, current assets increased by €571.1 million in 2020, from €1,063.1 million as of December 31, 2019, to €1,634.2 million as of December 31, 2020. This rise resulted primarily from the increase in cash and cash equivalents by €508.1 million, mainly from the precautionary utilization of the full revolving credit facility in the amount of €350.0 million and also from the positive cash flow from operating activities. The increase in contract assets by €38.5 million to €204.4 million as of December 31, 2020 resulted primarily from the provision of services prior to invoicing for some major projects. Current other assets increased from €46.1 million as of December 31, 2019 to €78.7 million as of December 31, 2020, mainly due to higher advance payments made.

The Management Board assesses the asset position of the HENSOLDT Group as positive. The liquidity position was further strengthened by the positive cash flow.

3.3. Financial position

Basic principles of financial management

HENSOLDT's financial management is focused on guaranteeing financial stability, flexibility and especially liquidity of the Group at all times. This includes capital structure management and financing of the HENSOLDT Group, the cash and liquidity management and the monitoring and controlling of market price risks, such as exchange rate and interest rate risks. The financing structure of the HENSOLDT Group enables it to maintain financial room for maneuver in order to seize of business and investment opportunities.

Capital structure

In connection with the IPO, HENSOLDT replaced its existing debt financing with a new credit facility agreement consisting of a term loan amounting to €600.0 million and a revolving credit facility amounting to €350.0 million, which was fully drawn as of the reporting date.

The availability and conditions of the long-term syndicated loan are tied to the compliance with a financial covenant, which refers to the ratio of net debt to adjusted EBITDA as defined in the Senior Financing Agreement. In 2020, these conditions were met at all times. In case of a breach, the financing partners are entitled to terminate the syndicated loan. There are no indications at the moment that the covenant will not be complied with in full in the near future. The loan agreement that was replaced was also tied to a financial covenant, which was complied with throughout the entire term.

in € million	Dec. 31, 2020	Dec. 31, 2019	% Change
Equity, total	346.8	154.8	124.0%
therein: Share capital / capital reserve	*701.8*	*406.7*	*72.5%*
therein: Other reserve	*-86.3*	*-49.8*	*73.4%*
therein: Retained earnings	*-281.6*	*-215.8*	*30.5%*
Non-current liabilities	1,257.1	1,517.9	-17.2%
therein: Non-current provisions	*482.6*	*413.6*	*16.7%*
therein: Non-current financing liabilities	*601.3*	*887.7*	*-32.3%*
therein: Non-current lease liabilities	*140.3*	*147.5*	*-4.9%*
Current liabilities	1,343.7	783.0	71.6%
therein: Current provisions	*193.6*	*185.1*	*4.6%*
therein: Current financing liabilities	*363.3*	*11.3*	*>200%*
therein: Current contract liabilities	*416.8*	*317.1*	*31.4%*
therein: Trade payables	*164.0*	*168.8*	*-2.8%*
therein: Other current financial liabilities	*97.8*	*20.5*	*>200%*
Total equity and liabilities	**2,947.6**	**2,455.7**	**20.0%**

As of December 31, 2020, liabilities increased by €491.9 million or 20.0 % to €2,947.6 million compared to €2,455.7 million as of December 31, 2019.

This increase was primarily due to an increase in current liabilities by €560.7 million to €1,343.7 million as of December 31, 2020. The main reason for this increase was primarily the utilization of the full revolving credit facility with a nominal amount of €350.0 million. In addition, current contract liabilities increased by €99.7 million mainly due to higher invoicing and additional advance payments received for some major projects. Current other financial liabilities resulted from the fact that the collection of payments to be collected by the factoring company in connection with factoring contracts were not yet due at the reporting date.

Equity increased by €192.0 million from €154.8 million as of December 31, 2019, to €346.8 million as of December 31, 2020. This increase mainly resulted from the proceeds from the IPO of €300.0 million less €4.9 million in transaction costs, which cannot be offset. Other reserves decreased by €36.5 million mainly due to the remeasurement of pension plans. The consolidated loss in the reporting period of €64.5 million also reduced equity.

In contrast, non-current liabilities decreased by €260.8 million, from €1,517.9 million as of December 31, 2019 to €1,257.1 million as of December 31,2020, which is mainly attributable to the reduction in non-current financing liabilities in the course of the refinancing through the IPO proceeds. Of the non-current financing liabilities with banks, €591.6 million related to a term loan. Non-current provisions increased by €69.0 million in the reporting period, primarily due to the increase in pension provisions.

Investment and liquidity analysis

	Fiscal year		
in € million	2020	2019	Change
Cash flows from operating activities	196.9	83.2	113.7
therein: Contract balances	*61.4*	*-89.4*	*150.8*
therein: Trade receivables	*5.3*	*56.4*	*-51.1*
Cash flows from investing activities	-95.0	-165.6	70.6
therein: Acquisition/addition of intangible assets and property, plant and equipment	*-97.4*	*-80.5*	*-16.9*
therein: Acquisition or subsidiaries net of cash acquired	*6.4*	*-83.8*	*90.2*
Free cash flow	**101.9**	**-82.4**	**184.3**
Non-recurring effects[9]	50.4	15.2	35.2
Interest[10], income tax[11] and M&A-activities[12]	44.1	142.1	-98.0
Adjusted pre-tax unlevered free cash flow	**196.4**	**74.9**	**121.5**
Cash flows from financing activities	**411.0**	**-9.1**	**420.1**
therein: Proceeds from / Repayment of financial liabilities (syndicated loan)	*30.0*	*2.4*	*27.6*
therein: Increase of other financial liabilities	*97.1*	*0.0*	*97.1*
therein: Issue of shares	*300.0*	*-*	*300.0*
Cash and cash equivalents	**645.5**	**137.4**	**508.1**

Free cash flow

The improvement in cash flow from operating activities was primarily due to an increase in contract liabilities mainly due to advance payments received in 2020, while these declined sharply in 2019. This was partially offset by an increase in contract assets after a reduction in the previous years and a lower reduction in trade receivables.

The decrease of the negative cash flow from investing activities is mainly due to high payments made for the acquisition of subsidiaries in the previous year. The decrease was partially compensated by higher investments in property, plant and equipment and intangible assets.

Investments include capital expenditure used to acquire, upgrade and maintain physical assets such as property, plant and equipment as well as intangible assets, such as software or licenses. In addition, capital expenditure includes development costs that were capitalized as internally generated intangible assets. The increase in capital expenditure is mainly due to higher investments in technical equipment and machinery and higher capitalized development costs (see chapter I.5 “Research and development” in the combined management report).

Adjusted pre-tax unlevered free cash flow

The increase in non-recurring effects[9] was mainly caused by higher other non-recurring effects, especially from the preparation for the IPO. The decrease in interest payments[10], income tax[11] and M&A activities[12] was primarily a result of high payments made for the acquisition of subsidiaries in the previous year.

Cash flow from financing activities

The increase in cash flow from financing activities was largely due to the drawing of the full revolving credit facility, while there was no such drawing in the period for comparison. The proceeds from the IPO were used to reduce the non-current financing liabilities in the course of the refinancing. Further cash inflows resulted from factoring agreements, for which payments for collection by the factoring company were not yet due at the reporting date.

Cash and cash equivalents

As of December 31, 2020, cash and cash equivalents were exclusively composed of bank balances amounting to €645.5 million. The increase compared with the previous year resulted primarily from the precautionary use of the full revolving credit facility and the positive cash flow from operating activities.

Overall Assessment

Overall the Management Board assesses the financial situation as positive. The proceeds from the IPO further strengthened the capital structure and improved the debt-to-equity ratio of the HENSOLDT-Group. The liquidity of the Group was ensured at all times during the fiscal year.

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[9] Includes transaction costs, separation costs and other non-recurring effects.

[10] Defined as “Interest paid” as reported in the consolidated cash flow statement.

[11] Defined as “Income tax payments / refunds as reported in the consolidated cash flow statement.

[12] Defined as sum of “Share of profit in entities accounted for using to the equity method”, “Acquisition of associates, other investments and other non-current investments, ” “Disposal of associates, other investments and other non-current investmentsv (only in the reporting year), “Proceeds from sale of intangible assets and property, plant and equipment”, “Acquisition of subsidiaries net of acquired cash” and “Other cash flows from investing activities” as reported in the consolidated statement of cash flow.

III. Forecast

1. Development of overall economic conditions

The IMF expects a decline in the global economic output of 3.5 % in 2020, an improvement of 0.9 percentage points compared to the October 2020 forecast, due to stronger dynamics in the second half of 2020.

For 2021, the IMF forecasts a global economic growth of 5.5 %. This forecast, which has been revised upwards by 0.3 percentage points compared to the October 2020 forecast, reflects the expectation of an economic recovery later in 2020 triggered by vaccinations and additional financial support in some major economies. The additional fiscal measures announced in late 2020, particularly in the U.S. and Japan, are expected to further support the global economy in the years 2021-22. The speed of recovery will, however, vary widely depending on the country (Source: WEO, January 2021).

For the euro area, the IMF projects significantly stronger growth than in previous years of 4.2 % on average, based on the low 2020 baseline. Compared with the last forecast, there was a downgrade of 1.0 percentage points, reflecting the observed slowdown in economic activity toward the end of 2020, which is expected to continue into early 2021 because of rising infections and renewed lockdowns. For 2022, the IMF expects a growth of 3.6 % on average.

The uncertainty surrounding these forecasts is unusually high because they are based on health and economic factors that are by nature difficult to predict. Although new restrictions and increases in infections (particularly in Europe) suggest that growth may be weaker than projected in early 2021, other factors pull the distribution of risk in the opposite direction. Continued public health and economic policy efforts are needed to limit the lingering damage from the sharp declines in 2020 and to ensure a sustainable recovery. In addition, the situation requires strong multilateral cooperation from the global community (source: WEO, January 2021).

Apart from the pandemic, the agreement reached in December on the terms of the United Kingdom’s withdrawal from the European Union removed a key risk (i.e., a “no-deal Brexit”). The agreement negotiated between the EU and the United Kingdom entered into force on January 1, 2021 on a provisional basis. The approval of the European Parliament is currently still outstanding for the agreement to become legally binding. Among other things, the agreement establishes a comprehensive economic partnership and is essentially based on a free trade agreement, without tariffs or quotas and thus averts significant trade barriers.

2. Development in the defense and security sector

On the basis of supplementary budgets, the German budget for defense in 2020 was €45.2 billion (Source: BMVG, Verteidigungshaushalt 2020). Compared to 2019, the budget increased by €1.8 billion, which corresponds to 4.2 %. This positive trend continues in 2021 and the budget for defense is set to increase even further to €46.93 billion. Overall, €12.2 billion are planned for investment expenditure. This includes, in particular, the joint developments FCAS and MGCS and the planned submarine design to be realized together with Norway along with missiles (Source: BMVG, November 2020). The German government explained to NATO its two-stage approach to achieving the two-percent goal. Until 2024, 1.5 % of the GDP is supposed to go toward the budget for defense and until 2031 this is supposed to increase to 2.0 % of GDP. The Federal Minister of Defense, Annegret Kramp-Karrenbauer publicly affirmed Germany’s commitment to work toward the two-percent goal and, in this context, even demanded that investments should clearly surpass this threshold (Source: Neue Zürcher Zeitung, December 2020).

Germany had taken over the presidency of the EU Council for the second half of 2020, which was characterized by the global pandemic and its health-related, social and economic consequences. The reaction to the COVID-19 pandemic also became a defense policy focus. Furthermore, the first collective threat analysis was carried out as part of the Strategic Compass and an agreement for regulation regarding third state involvement in PESCO projects (Permanent Structured Cooperation) was reached (Source: Rückschau auf die deutsche EU-Ratspräsidentschaft aus Sicht des BMVg, December 2020).

From 2021 onwards, research and development projects in the defense industry are supposed to be supported by €7.9 billion in aid from the European Defence Industrial Development Programme (EDIDP). Like the perennial financial framework of the EU, the EDIDP shall apply for seven years (2021-2027) (Source: Euractive, December 2020).

With regard to Great Britain and the Brexit, Germany confirmed ongoing integration of United Kingdom in the European security architecture and the establishment of an E3-format with France, United Kingdom and Germany. In August 2020, the first formal meeting of this format took place, to consult about the crises in the immediate vicinity, the partial reorientation of the USA as well as the consequences of the COVID-19 pandemic (Source: BMVg, August 2020).

In France, defense spending continues to rise according to the military planning act for 2019-2025. This law determines that the budget for defense is set to increase by €1.7 billion annually until 2022 and by €3 billion annually from 2022 until 2025 in order to achieve the two-percent goal set out by NATO by 2025. In 2021, the budget for defense will be €39.2 billion, which corresponds to an increase of €1.7 billion from 2020. Within this budget, France spends 26.5 % on major procurement and on research and development (Source: Ministry for Europe and Foreign Affairs, December 2020).

In November 2020, the government of the United Kingdom announced that military spending will be increased gradually by an additional £16.5 billion over the course of the next four years. Currently, the budget for defense amounts to approximately £40 billion (2020) (Source: Deutsche Welle/Defense News, November 2020).

How defense spending develops in Eastern European countries remains to be seen due to the consequences of the COVID-19 pandemic, although all NATO members in Eastern Europe and South-Eastern Europe as well as the Baltic states continue to aim at reaching the goal set in Wales and securing the safety of NATO’s eastern border and the airspace above the Baltic area.

After significant growth in previous years, it remains to be seen what the development in the Asia Pacific region as well as the BRIC countries will be. The export environment for defense and security goods, particularly in non-European customer countries, is currently subject to a restrictive export approval policy.

3. Outlook

In the operational planning for the Group, the Management Board expects a significant growth in revenue for 2021 for both segments, in particular, due to the high order backlog. Furthermore, management expects a moderate increase in order intake in the Sensors segment for 2021, given the current developments in the defense and security industry. A strong increase in order intake is expected for 2021 in the Optronics segment.

Adjusted EBITDA is anticipated to increase significantly in 2021, whereby declining earnings effects are assumed from the adjustment items purchase price allocation and other non-recurring effects. The expected increase in adjusted EBITDA will mainly be driven by the Sensors segment.

This expectation does not account for possible implications from additional waves of infection or further lockdowns in connection with the global COVID-19 pandemic.

The forecast strongly depends on the conditions mentioned in the opportunities and risks report and, besides the macroeconomic developments described above, is based on the multi-year business plan of the Group. This forecasts a US dollar exchange rate of $1.20/€1.00 and an inflation rate of 2.0 % for the planning period. Furthermore, a 3.0 % increase in personnel costs is forecasted for Germany and a 2.0 % increase for France and Great Britain. In addition, the forecast volumes for revenue and order intake highly depend on the reliability and stability of the political framework.

HENSOLDT plans to achieve insignificant total revenue and order intake attributable to end-customers and business customers in the UK for 2021 to 2023. In view of the negotiated comprehensive economic partnership as part of the Brexit agreement negotiated between the EU and the United Kingdom, HENSOLDT expects only marginal effects regarding the administrative effort for imports and exports.

Overall, the Management Board is confident that HENSOLDT can build on the strong 2020 fiscal year and expects another positive development for 2021.

IV. Opportunities and risks report

1. Risk report

1.1. Basic principles of the HENSOLDT risk management

At the HENSOLDT Group, measures and systems have been implemented with the objective to allow an early identification of risks, which is the basis for a timely initiation of adequate counter-measures. The same applies to consistently seizing opportunities as they arise.

To support transparent risk and opportunity management, the HENSOLDT Group identifies, manages and reports all risks and opportunities on a segment specific-basis and thus differentiates between the two segments, Sensors and Optronics.

1.2. Risk management system

The risk management system, applicable to the entire HENSOLDT Group, considers relevant legal requirements and is based on generally accepted principles set out in external frameworks and standards, such as COSO. The HENSOLDT risk management system represents an integral part of the systems and instruments, which the HENSOLDT Management Board is using for a value- and success-oriented corporate management. The central objective is the early and systematic identification, assessment and management of significant risks. For this purpose, valid procedures and methods, which are applicable for all entities, are defined on HENSOLDT Group level. The overall responsibility for the risk management system lies with the Head of “Internal Audit, Risk Management & ICS”. The HENSOLDT risk management team permanently monitors the HENSOLDT risk management system to support a continuous improvement process. The Group policy “Enterprise Risk Management (ERM)” issued by the Management Board defines the methodical and organizational standards dealing with risks and opportunities. No changes were made to the risk management system in 2020.

The operational and IT-based risk management process takes the risks of all entities into account and consists of the following steps:

- Making assumptions and setting goals,
- Determining roles and responsibilities,
- Identifying risks and opportunities,
- Assessing the impact of these identified risks and opportunities,
- Responding in the form of implementing appropriate measures,
- Monitoring the effectiveness of these response measures, and
- Regular preparation of risk management reports.

For the identification and assessment of risks, the responsible persons in the various Group companies and departments have to follow the predefined procedures of the ERM team.

For the assessment of risks and opportunities on a Group level, HENSOLDT is using a predefined evaluation matrix, which includes the following levels of probability and impact.

Probability [%]	Min	Max	Risk matrix (p.26)
Very unlikely	0.00 %	4.99 %	Low
Unlikely	5.00 %	24.99 %	Low
Possible	25.00 %	49.99 %	Medium
Likely	50.00 %	74.99 %	High
Very likely	75.00 %	100.00 %	High

Impact on group level [€ million]	Min	Max	Risk matrix (p.26)
Low	0.000	0.999	Low
Medium	1.000	1.999	Medium
High	2.000	4.999	High
Very high	5.000	9.999	High
Critical	10.000	200.000	Critical

As a benchmark for assessing the financial impact of risk, adjusted EBIT is used at a group level. The basis for the subsequent impact assessment of (operative) risks on a project level is defined by the respective overall project volume or budget . Following the risks and opportunities assessment, the risk or opportunity owner defines respective countermeasures or measures to support the realization of opportunities. The HENSOLDT risk management system provides four response action strategies for risks as well as for opportunities. Related to risk management, these strategies are avoidance of the risk, transfer of the risks to third parties such as insurer, mitigation of the risk and acceptance of the risk. Accordingly, the strategies for opportunity management are, first, the exploitation of the opportunity; second, the allocation of the opportunity to parties or entities that are more likely to realize the opportunity; third, the enhancement of the opportunity by increasing the likelihood and/or the impact of it; and fourth, the acceptance of the fact that the opportunity cannot be realized.

For the reporting of risks, the heads of the central departments of the HENSOLDT Group and the ERM point of contact in each legal entity are responsible for providing their risk portfolio to the ERM Officer at the group level in time for the quarterly risk reporting. Besides, the site managers have to provide their risk information related to health and safety also in time for the reporting.

The ERM Officer prepares the quarterly ERM report for the Management Board and the Supervisory Board by consolidating the received information. For operative risks and if the likelihood is below 50.0 %, risk contingencies are recognized. If the likelihood exceeds 50.0 %, the accountable risks are added to the expected costs but are not weighted for purposes of risk reporting. However, these risks above 50.0 % are included in the existing risk reporting for monitoring purposes.

1.3. Accounting-related internal controls and risk management

Risks related to Group accounting include – amongst other things – the incomplete, invalid or inaccurate processing of financial data leading to misstatements in the financial reporting. To mitigate these risks, the management of HENSOLDT has implemented a number of measures and controls. These are part of the internal control system over financial reporting, which is monitored on a regular basis and subject to a continuous improvement process. Key elements of controls over financial reporting are diverse to cover the variety of risks related to Group accounting effectively.

To set binding guidelines and internal regulations in the context of preparing the monthly, quarterly and annual Group financials, respective accounting policies and manuals are in place, which have to be adhered to by any member of staff involved in accounting and closing processes. In addition, every legal entity uses a uniform Group chart of accounts.

For the preparation of the financial reporting, HENSOLDT has issued detailed instructions on how and when to prepare and submit reporting packages to ensure a consistent quality over all reporting entities. Preparer and reviewer of these reporting packages are different persons to support an adequate segregation of duties.

Such segregation of duties is also constant practice within the accounting department and its various functions. Here, for example, master data maintenance is separated from transaction processing on the basis of a 4-eyes-principle. In addition, accounting personnel regularly perform a reconciliation of the most critical general ledger accounts with the respective sub-ledger accounts.

HENSOLDT management has installed procedures for a monthly review of the financials based on predefined key performance indicators, and thus ensures a reconciliation of the actuals with planning data.

External auditors audit the HENSOLDT Group financial reporting per year-end. This audit is performed according to the existing and relevant regulations and accounting standards. Because of the listing, the half-year financial statements are also subject to a review by external auditors. Further, the financial statements are reviewed and signed off by the management and presented to the respective statutory bodies.

IT applications and tools that are used for preparing the financial statements as well as the underlying infrastructure are secured against unauthorized access, unauthorized system changes and loss of data.

1.4. Risks

To support the identification and the management of risks and opportunities, the HENSOLDT Group has defined risk groups and risk categories. Risk groups are operative and functional risks, whereas the latter includes the two subgroups of risks related to strategy & planning and compliance risks. This categorization of risks and opportunities is applied in the same way for the two segments Sensors and Optronics.

Under functional risks for the HENSOLDT Group, all those risks that are not directly project-related are summarized. Risk categories within the group of functional risks such as strategic risks and compliance risks are independent from HENSOLDT's operational activities.

Operative risks refer to operational activities in particular in the context of HENSOLDT's project business. HENSOLDT has defined further sub-categories of operative risks; these are project specific.

FUNCTIONAL RISKS AND OPPORTUNITIES
Strategic risks and opportunities (Economy and competition)
Strategy (incl. Brexit)
M&A
Controlling
Compliance risks and opportunities
Compliance/Corruption
Data protection
Export control
Health, safety, environment

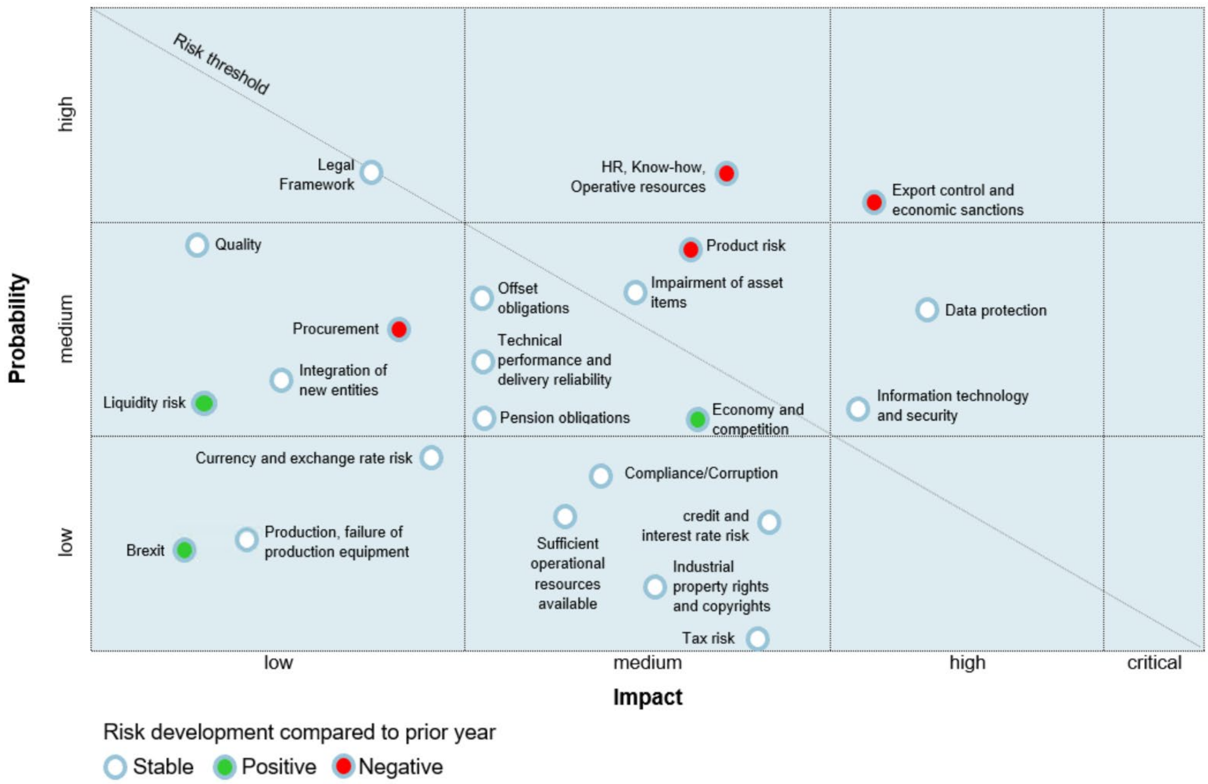
OPERATIVE RISKS AND OPPORTUNITIES
Construction/Technology
HR
Information management/Security
Legal
Operational quality
Procurement
IP rights
Production/Product risk
Sale/Offset obligations

FINANCIAL RISKS AND OPPORTUNITIES
Currency and exchange rate risks
Credit and interest rate risks
Liquidity risks
Impairment of assets
Taxes

As risks and opportunities can be both functional and operative, HENSOLDT is not always in a position to assign them to only one group of risks. Risks or opportunities that have been identified as functional can also be relevant for specific projects and therefore need to be assessed and managed with respect to these projects, e.g. by implementing measures on operational level. Vice versa, operative risks might require an assessment and management on a segment, entity or even Group level. Therefore, and to avoid a duplication of risks, the management of both functional and operative risks follows the same procedures of the HENSOLDT Group risk management system as described above.

Functional Risks

Functional risks cover risks related to strategy and planning as well as compliance risks. The subgroup strategy and planning covers any risks that have an impact on the strategic goals of the HENSOLDT Group, such as reputation and brand risks or risks resulting from market and industry changes and developments. The markets in which HENSOLDT is operating are highly regulated, which results in compliance risks.



Risks related to strategy & planning

For both segments, risks arising from the global economic cycle cannot be averted permanently. A change of the legal, regulatory or economic environment might affect revenue and adjusted EBIT of the segments and therefore of the HENSOLDT Group as a whole. International conflicts and political developments around the world, among other things, affect HENSOLDT's international sales and supply chains, cause more complexity and create additional barriers. Because of globalization as well as increasing intensity of competition, market risks are on the rise. Geopolitical developments also contribute in a significant way to market risks for HENSOLDT. Thus, fluctuations of prices, units and margins can occur.

To anticipate and mitigate negative consequences due to such new circumstances, the program "HENSOLDT GO!" was initiated. This focuses on five long-term, strategic policies:

- Innovation
- Customer
- Continuous improvement
- Strategic acquisitions
- Corporate culture

Improvement measures of this program include strengthening the distribution network, expanding the global partner network, increasing operating efficiency and optimization, a market-oriented expansion of the product portfolio and review of efficiency in the support functions such as HR, finance and communication. In 2020, significant increases in operating efficiency could already be achieved. In the second phase of this program, "Wave 2", further saving potentials shall be realized in the next two years, 2021 and 2022.

Innovation and technical progress in the industry are fundamental for the expansion into new markets and customer groups. The HENSOLDT Group therefore considers R&D as being fundamental for its business and market opportunities and is substantially investing in this area. By expanding the service business, additional revenue potential can be realized in the framework of project management and execution.

Although being a leading provider of defense and civil technology with a profound growth in size and know how in recent years, the HENSOLDT Group is constantly facing competitive risks. In Germany, its key market, HENSOLDT competes for contracts with a number of international competitors purely on market terms, which is not always the case for procurements on certain competitors' domestic markets and therefore may result in competitive challenges for HENSOLDT. While the small and mid-sized competitors are typically specialized in certain market niches, HENSOLDT also competes with large defense companies, which might have more resources, and may therefore be better positioned to develop and market new products and take advantage of economies of scale. An additional aspect to consider are national promotion programs and political support, which could put competitors in a better position.

These risks can be addressed through inorganic growth within the boundaries of competition law. HENSOLDT management is constantly evaluating, whether – and if so, how – the acquisition of leading technology providers or even competitors can positively contribute to addressing these competitive risks. However, such acquisition and integration of organizations into the existing HENSOLDT structure leads to additional risks that have to be managed adequately.

Towards the end of the Brexit transition period, the EU and the UK have reached a comprehensive trade agreement in December 2020. The agreement is provisionally effective from January 1, 2021 onwards and will become permanently effective upon approval by the European Parliament. Due to the comprehensive economic partnership of the EU with the UK negotiated in the agreement, HENSOLDT only expects marginal effects on the administrative effort for imports and exports.

Risks related to compliance

As an internationally operating enterprise, the HENSOLDT Group is subject to a range of compliance requirements in all countries in which it operates or sells its products and in particular to the ongoing changes in the legal framework relevant to the Group's business activities. Breaches of compliance can have a number of severe consequences for HENSOLDT, such as damages in reputation, loss of customers, exclusions from orders, sanctions, disgorgement of profits, compensation for damages as well as civil and criminal prosecution. The financial expenditure of compliance breaches, should they occur despite all precautionary measures, on consolidated results is difficult to gauge and is highly dependent on individual circumstances. The assurance of compliance with relevant legal requirements as well as internal rules is therefore a key principle for HENSOLDT, even though the risk posed by individual exceptions can never be fully eliminated. In view of the industry and the markets in which HENSOLDT operates, the avoidance or control of risks concerning corruption, competition law, export controls, economic sanctions and data protection are in focus. To address these risks, the HENSOLDT Group has set up a compliance organization that ensures the lawful conduct of the Company and its employees through a compliance management system, as well as an appropriate response to potential or actual violations of external and internal rules. All business units of HENSOLDT are thus responsible for compliance with applicable laws and regulations in the course of their work. All suspicions of compliance breaches are investigated and HENSOLDT cooperates fully with the authorities involved. Should a breach occur despite the measures that were put in place, all parties involved will have to deal with consequences and the processes will be reviewed.

HENSOLDT has implemented a number of preventive measures to identify currently relevant laws and regulations on an ongoing bases and ensure they are taken into account in all decisions and operative processes. One of these measures is the regular compliance risk assessment across the group. With the risk assessment, systemic and Company-specific compliance risks can be identified, rated and necessary measures can be taken. In relation to this, there are regular training and Q&A sessions (in English and German). HENSOLDT also issued standards for the Company and all employees for the most important ethical questions and compliance issues in its directive “Standards of Business Conduct”. All employees receive regular training on this. To further minimize compliance risks, HENSOLDT introduced processes and procedures (e.g., for dealing with third parties, including sales representatives, gifts and invitations as well as memberships and donations, processes for regulating export controls and international sanctions).

In connection with the current compliance directive, HENSOLDT employees are obliged to promptly report all compliance violations to their supervisors, their contacts in the HENSOLDT compliance team, the head of the compliance department or any other employee of the HENSOLDT compliance team. In addition, employees have the option of anonymously reporting violations to the “OpenLine” (anonymous telephone and email hotline).

Data protection risks

HENSOLDT has implemented a data protection management system across the Group, which is particularly intended to ensure a uniform level of data protection while taking into account the General Data Protection Regulation (GDPR) introduced by the EU. The goal is to enable a sustainable data-based business model as well as to ensure a responsible treatment of data in the interest of customers and employees. A variety of measures are developed and implemented in order to achieve the goals mentioned above. The focus is on a continuous improvement of the data protection managements system. For this, HENSOLDT adheres to a risk-based approach. Specific data protection risks may exist based on the GDPR, depending on the severity and culpability of an individual incident, with an amount of up to 4 % of the HENSOLDT Group’s global annual revenue per incident. To avoid such data protection incidents, HENSOLDT sensitizes its employees for a responsible handling of data and the new challenges of data-based business models. The legal department continuously updates the regulatory requirements and integrity standards for the data protection management system. As a result, HENSOLDT wants to offer its employees and customers as well as other stakeholders new services alongside safe processing of data. HENSOLDT offers an operational framework for the treatment of data for all employees of the Group. This includes defined fundamental principles for data processing, such as transparency, autonomy and data security. Both market specific and regional differences are considered in the application of those fundamental principles. The goal of implementing suitable processes and systems is to enable an efficient and effective way of secure and powerful data processing. Ongoing monitoring of the effectiveness is part of this system as well. Data protection officers are appointed in accordance with the legal requirements. All employees are trained in data protection.

Operative risks

Each project has a variety of inherent operative risks. Following the HENSOLDT risk management procedures, project management has to complete a risk assessment for each project prior to entering into any legally binding agreement with a partner or customer.

The HENSOLDT Group has to manage complex and long-running projects with demanding technical and volume requirements. Due to various uncertainties regarding calculations, unexpected technical problems or underestimated levels of complexity, which could have an impact on the adherence to the agreed-upon delivery dates, there are a number of risks to take into account. In addition, failure to meet its offset obligations may result in penalties and have a negative effect on project margins. Utilizing experienced employees, technical know-how, and professional project, quality and contract management, these risks can be minimized but not totally avoided.

As a company dependent on the sales of innovative and complex technological products to a relatively small number of customers, the success of the two segments of the HENSOLDT Group depends on the ability to attract and retain highly qualified engineering personnel for both segments, as well as skilled sales people and capable management. Since it is a competitive market environment, HENSOLDT needs to outbid its competitors by offering a more attractive work environment.

As much of the business is project-related, this requires the Company to continuously adjust research and development and production capacities. For this purpose, HENSOLDT employs certain measures such as flexible working hours, temporary workers, and the alignment of the production network to production volume.

The HENSOLDT Group has initiated a number of measures to be regarded as an attractive employer. For example, it is offering a mobile work environment as part of the Group agreement for all German sites, childcare during school holidays or an incentive program based on BONAGO employee cards. Against the background of the current labor market situation, HENSOLDT expects increased challenges in the future with regard to attracting and retaining highly qualified employees.

In the area of operational quality, the HENSOLDT Group is required to perform with the highest standards. Due to the complex and advanced nature of its products, there are technological challenges that arise in conjunction with the development and manufacturing of new products. In order to maintain high quality standards for its products, the HENSOLDT Group implemented a number of quality assurance measures such as an enhanced customer review and feedback process, single quality points of contact for “A-parts” and joined problem solving with suppliers. Other measures in this area are dynamic sampling as part of the incoming goods inspection or an improved first sample inspection for so-called “B-parts”. Product quality is also significantly dependent on properly functioning production facilities. Risks related to production, such as failure of production facilities or a decrease in performance of production facilities are addressed through an ongoing improvement process for production “HotSpots” and continuous improvement workshops. These measures are expected to increase production effectiveness and efficiency and to reduce production time as well as production cost. An adequate product quality reduces the risk of increased refunds to customers due to product liability and product warranty agreements.

For both segments, the procurement of raw materials, components and other modules is exposed to risks regarding delivery shortfalls or delays, supply bottlenecks, quality issues and price increases. A variety of different materials at low volumes characterizes the supply chain. In addition, these materials are also used in other industries, which is why the HENSOLDT Group only purchases small fractions of the suppliers’ total output. The HENSOLDT Group also procures highly customized products, which are only available from a small number of suppliers or even only from a single source. To mitigate these procurement risks, a number of measures are in place: suppliers are involved in projects at an early stage, preferred suppliers are specified and, moreover, suppliers are selected on the basis of fact- and competition-oriented factors. There is also a management system in place for supplier relationships.

As a company in the security and defense industry, HENSOLDT is particularly prone to attempted cyberattacks as well as the misappropriation or compromise of its IP or other confidential (project-related) information, including that of its customers. To mitigate this risk, several measures, including employee awareness campaigns and trainings, have been initiated. Furthermore, the HENSOLDT Group implemented cyber security measures including a dedicated cybersecurity team and budget, security monitoring, a Group-wide security operations team, penetration testing, and regular internal IT audits.

Financial risks

In the context of ensuring Group-internal and external financing, the HENSOLDT Group is exposed to a range of financial risks. Above all, these are currency and exchange rate risks, interest rate risks, liquidity risks, risks related to pension plans and risks of impairment of assets.

Financial risks can have negative effects on the profitability, financial position and cash flows of the HENSOLDT Group. The probability of occurrence and the possible impact of these risks and opportunities is considered as shown in the matrix above.

The Treasury department is centrally responsible for the management of the HENSOLDT Group's financing and liquidity and sets out guidelines in this function. These include primarily ensuring external Group financing at all times, coordinating financing needs within Group entities and monitoring compliance with corresponding internal and external requirements, such as covenants of loan agreements.

Currency and exchange rate risks

As a globally operating company, the HENSOLDT Group is exposed to risks and opportunities related to fluctuations in currency and exchange rates. While the reporting currency is the Euro, some of the consolidated subsidiaries report in foreign currencies. The results of operations are therefore affected by exchange rate fluctuations; in particular the rates of the U.S. Dollar, South African Rand and British Pound to the Euro. The income and cost risks resulting from currency fluctuations are limited by purchases and sales in corresponding foreign currencies as well as forward exchange transactions. Hedging contracts are concluded centrally for each foreign exchange rate risk resulting from various customer or supplier contracts. Corresponding foreign exchange forward and swap contracts are concluded with banks for the respective Group entities.

Credit and interest rate risks

To secure the cash requirements of the Group's business operation, the HENSOLDT Group uses interest-rate-sensitive financial instruments. The interest rate risks associated with these instruments are mitigated by way of interest rate hedges. The aim of interest rate management is to limit the impact of interest rates on the financial performance as well as on assets and liabilities of the Group.

In conjunction with the IPO in the third quarter of 2020, HENSOLDT replaced its existing debt financing with a new credit facility agreement, consisting, among others, of a new term loan amounting to €600.0 million (nominal value). The long-term syndicated loan is tied to compliance with a financial covenant. In the event of a breach, the financing partners are authorized to terminate the syndicated loan. There are no indications that the covenant cannot be fully complied with in the foreseeable future.

Liquidity risks

The liquidity of the HENSOLDT Group is dependent on its credit rating. Liquidity risk is the risk that a company may be unable to meet short-term financial demands. This usually occurs due to the inability to convert a security or asset into cash without loss of capital and/or income in the process. Risk and opportunities related to liquidity arise in connection with potential downgrades or upgrades of credit ratings by the rating agencies.

In 2020, the IPO proceeds were used by the HENSOLDT Group to improve liquidity and reduce debt. To ensure the liquidity of the Group, the Company replaced the existing revolving credit facility with a new revolving credit facility amounting to €350.0 million in the context of the IPO. In order to plan the required utilization of this facility, there is a comprehensive process in place for planning future liquidity requirements and thus to adequately cover the associated risk. At the end of December 2020, the revolving credit facility was drawn in full as a precautionary measure as part of the COVID-19 action plan.

Risks related to pension plans

The HENSOLDT Group has certain obligations with respect to defined benefit plans for employees in Germany. Under these plans, HENSOLDT is required to ensure specific retirement, invalidity, and survivor's benefits levels for employees participating in the plans. The plans are partly financed through contractual trust arrangements (“CTAs”). The calculation of expected liabilities arising from defined benefit plans is based on actuarial estimates and demographic and financial assumptions. The HENSOLDT Group is obliged to fund the CTAs only with respect to the employee-funded part of the pension plan. The HENSOLDT Group expects to make significant contributions in the future, in particular if the CTAs funding status deteriorates due to the developments of their assets or defined benefit obligations. The funding status of existing pension plans could be affected both by a change in actuarial assumptions, including the discount rate, and by changes in the financial markets or a change in the composition of invested assets. Opportunities and risks arise depending on changes in these parameters.

Risks of impairment of assets

The carrying amounts of individual assets are exposed to risks related to changing market and business conditions and thus to changes in fair values as well. Necessary impairments could have a significant negative non-cash impact on earnings and affect the balance sheet ratios. The intangible assets of the Group mainly consist of technology, customer relationships, order backlog, the brand, and capitalized development costs. Under the International Financial Reporting Standards as applicable in the EU (“IFRS”), HENSOLDT is required to annually test the recorded goodwill and intangible assets with indefinite useful lives, such as its brand, for impairment and to assess the carrying values of other intangible assets when impairment indicators exist. All relevant risks were assessed during the preparation of the consolidated financial statements and have been taken into account accordingly.

Tax Risks

Due to the international nature of its business, HENSOLDT is subject to taxation in several countries and is therefore exposed to tax risks. As a result, HENSOLDT is subject to numerous different legal requirements and tax audits. Possible changes in legislation as well as jurisdiction and differing legal interpretations by the tax authorities – especially in the area of cross-border transactions – may be subject to considerable uncertainty. In the course of tax audits, different assessments of facts may lead to additional claims by the responsible tax authorities. In addition, changes in tax legislation or interpretation as well as new jurisdiction may result in additional taxes for HENSOLDT and adversely affect the effective tax rate and the carrying amount of deferred tax assets or liabilities. Furthermore, tax risks may arise in connection with the expiration of tax loss carryforwards or from changes in the legal and tax structure of HENSOLDT. Particularly, certain Group companies of HENSOLDT are part of tax groups or tax consolidation systems. It can therefore not be ruled out that the companies concerned will be held liable for unpaid taxes of the members of such tax consolidation systems pursuant to law or contract. Additional taxes, interest and penalties may arise for HENSOLDT from a restructuring, other corporate actions or the non-recognition of tax consolidation options (e.g. by tax authorities or a tax court).

COVID-19

In the last months, HENSOLDT has tracked the situation around the COVID-19 pandemic at all sites to protect the health and well-being of all employees, customers, partners as well as the business itself. The local business continuity management teams have reviewed and updated their plans to enable maximum resilience of business activities. Key processes were tested and changed where necessary to not only ensure ongoing operations but also minimize the spread of the virus. So far, the COVID-19 pandemic has not significantly affected the business of HENSOLDT as a supplier of defense and security electronics. With the exception of delays and postponements in project business and of order intakes, there have been no formal cancellations of large orders from defense sector customers nor other significant effects on the order backlog or future prospects for the defense sector caused by the COVID-19 pandemic. Potential effects of further waves of infection and lockdowns due to the global COVID-19 pandemic have not yet been considered.

1.5. Overall risk assessment

HENSOLDT is not aware of any single or aggregated risk that could endanger the continuity of its business operations. The Management Board assesses the overall risk situation of the HENSOLDT Group as unchanged compared to the prior year.

2. Opportunity report

2.1. Opportunities

In line with its categorization of risks, HENSOLDT Group has defined the same groups and categories for the identification and management of opportunities for the segments Sensors and Optronics. HENSOLDT Group has summarized all single reported opportunities below.

Functional opportunities

The business policy is designed to ensure a long-term and economically sustainable future of the HENSOLDT Group. New opportunities shall be recognized systematically and at an early stage.

As a high-tech pioneer in the area of defense and security electronics, the HENSOLDT Group is a market leader for civil and military sensor solutions. The HENSOLDT Group operates in a highly regulated industry that is affected by international conflicts and political developments. For the HENSOLDT Group, the most important development in the recent past has been the increase in defense spending by NATO member countries. Throughout these countries, political pressure to spend at least 2.0 % of the national GDP on defense rises. As a result, the German government decided to increase its defense budget significantly by 2031. Even though the approvals concerning the exports of armaments rose, the HENSOLDT Group is still subject to the restrictive German approval policy.

From the year 2017 to 2020, the German government's defense equipment expenditure was the most significant driver for revenue. The fact that military budgets in Germany and allied NATO countries are expected to increase in the nearer future is highly relevant for the business of the HENSOLDT Group. Germany is one of the leading participants and decision-makers for major European and other international defense projects. When the political environment in Germany supports military spending, it not only directly affects HENSOLDT's project business, it also indirectly results in business prospects with respect to such projects. Due to the long-term nature of military projects, such commitments to increase budgets should ensure cash flows for many years.

Additional opportunities for the Sensors and Optronics segments result from the integration of newly acquired or formed Group companies. This could result in synergies, for instance through the centralization of functions.

Currently the main aim of HENSOLDT is to generate additional business volume. To achieve this, the Management Board, among other things, initiated the aforementioned program "HENSOLDT GO!".

Operative opportunities

The Group benefits from long-term experience on the highly regulated and complex market of defense and non-defense applications. In addition to its civil and military sensor solutions, HENSOLDT also develops new products for data management, robotics and cyber security by crosslinking existing expertise with software solutions. HENSOLDT pursues the goal to become Europeans leading, platform-independent provider of defense and security sensor solutions with global reach. Diversification of its products is considered key to increasing opportunities in this context.

As a consequence, the HENSOLDT Group started expanding its product offering, for example, through surveillance and protection solutions utilized for a number of high-profile events. This allows the entry into new markets, which may both facilitate future growth as well a diversification of risks.

Within the defense applications, the Group currently expands its customer services, including for example technical assistance, commissioning and installment. These services can lead to an increase in profitability and – at the same time – a decrease of risks concerning fluctuations of future cash flows.

The HENSOLDT Group has been successfully developing customer-specific solutions. These unique and highly technical products may have been costly initially (e.g. due to expensive special production facilities) but now they can impede market entry of new competitors.

The HENSOLDT Group has co-operations with many renowned universities and research institutes, mainly in Germany, for nearly all early-stage technological developments in the radar and optronics sectors. Through this intense collaboration between the universities and research institutes, the HENSOLDT Group lays the foundation for maximizing its opportunities as an innovative organization. Both segments take advantage of this.

2.2. Overall opportunity assessment

The most significant opportunities for the HENSOLDT Group result from the current increase in defense budgets. This is supported by the further diversification of the product range and the expansion of the service business as well as HENSOLDT’s ability to act as a leading innovator within its industry.

V. Non-financial group statement

Sustainability (Environment Social Governance or “ESG”) is an important topic for HENSOLDT, which is continuously expanded. The protection of natural resources, the responsible treatment of employees as well as a corporate governance with integrity have been the key aspects of the company’s culture since the start. HENSOLDT has set itself goals and entered into obligations to protect the planet, strengthen society, develop the potential of its employees, and to maintain and promote a corporate culture of integrity. Those goals are also anchored in the sustainability strategy of the Company.

This year, HENSOLDT issues a sustainability report, which will be compliant with the requirements for capital market-oriented companies, which describes the sustainability-related activities of HENSOLDT and extensively deals with the Company’s influence on the environment and society. For this purpose, current initiatives and relevant KPIs, especially, regarding relevant topic areas will be included and a forecast for future measures and initiatives will be given. Currently, business integrity as well as health and safety were identified as central topics. Other key areas for the Company are product responsibility, the potential and development of employees as well as diversity within the Company.

The sustainability report contains the non-financial declaration pursuant to sections 315b und 315c of the German Commercial Code (HGB). The sustainability report for the fiscal year 2020 is published simultaneously with the annual report and can be found on HENSOLDT’s website.

VI. Remuneration report

The remuneration report for the fiscal year 2020 has been prepared in accordance with the commercial law provisions valid until December 31, 2019, which pursuant to Article 83 (1) sentence 2 of the Introductory Act to the German Commercial Code (EGHGB) are still applicable. In accordance with the remuneration systems for the members of the Management Board and the members of the Supervisory Board, which the shareholders' meeting of HENSOLDT AG will resolve to approve in 2021, it explains the main elements of the remuneration systems for the Management Board and the Supervisory Board of HENSOLDT AG and reports on the amount of remuneration granted to the individual members of the Management Board and the Supervisory Board for the fiscal year 2020. The remuneration report already takes into account various requirements arising from section 162 of the German Stock Corporation Act (AktG) which is to be applied in the future.

HENSOLDT AG was formed by change of legal form of HENSOLDT GmbH registered with the commercial register on August 17, 2020. On September 25, 2020, the shares of HENSOLDT AG were listed for the first time on the Frankfurt Stock Exchange. In the fiscal year 2020 the current members of the Management Board, Thomas Müller, Axel Salzmann and Peter Fieser were initially employed on the basis of Managing Director service contract by the HENSOLDT Holding GmbH. In the context of the change of legal form they were appointed as members of the Management Board of HENSOLDT AG. They were also appointed as Managing Directors of HENSOLDT GmbH.

In the context of the change of legal form, the remuneration system was adapted to the needs of a listed company. The following principles were decisive in this adjustment:

- Alignment of the remuneration of the Management Board with the strategic objectives of the HENSOLDT Group and to support long-term financial and sustainable performance.
- Focus on further growth as well as the profitability of the Company.
- Orientation of the remuneration system on sustainability criteria and consideration of the variety of stakeholder interests, in particular, through the introduction of diversity and environmental targets.
- Performance orientation of variable remuneration components.
- Harmonization of the remuneration structure: Targets set for the Management Board regarding the development of the Company as a whole are applied accordingly to broader employee groups and in particular to executive staff.
- Ensuring the competitiveness of the remuneration system.

1. Principles of Management Board remuneration

The structure of the remuneration and the amounts paid to the members of the Management Board are determined and regularly reviewed by the Supervisory Board. In the review, the assessment criteria recommended in recommendations G.2, G.3 and G.5 of the German Corporate Governance Code as amended on December 16, 2019 ("GCGC") are applied and the requirements pursuant to section 87 AktG are implemented.

The recommendation G.4 of the GCGC has not been complied with yet.

2. Overview of the remuneration system

For the revision of the remuneration system and the review the level of remuneration, an independent external expert was consulted. The benchmark used for a market comparison is based on a German peer group of listed companies of comparable size with a focus on industrial, mechanical engineering and automotive suppliers, as well as listed companies of comparable size from the information technology sector.[13]

The remuneration of the members of the Management Board is based on their area of responsibility, individual performance, the performance of the Management Board as a whole, and the economic and financial situation and success of the HENSOLDT Group. The compensation paid to the members of Management Board is appropriate, performance-related and in line with market conditions.

The Management Board service agreements replaced the Managing Director employment agreements with the HENSOLDT Holding GmbH at the time of the appointment of the previous Managing Directors as Management Board members.

As a rule, the remuneration for the period prior to the change of legal form (pre-form change phase) is based on the remuneration conditions in accordance with the service contracts of the previous Managing Directors of the HENSOLDT Holding GmbH.

In contrast, the remuneration for the period after the change of legal form (post-form change phase) is based on new remuneration conditions, which besides a short-term remuneration component (STI) provide for a long-term variable remuneration component (LTI). The introduction of the LTI as a remuneration component is aimed at aligning the incentives through the remuneration of the Management Board members with the long-term developments and successes of the HENSOLDT Group. In the new remuneration system, the variable remuneration resulting from the achievement of long-term targets exceeds the share resulting from short-term targets.

In the event of entry or withdrawal of the members of the Management Board during the year, all remuneration is calculated pro rata temporis.

3. Remuneration components of the Management Board

3.1. Fixed remuneration components

Basic remuneration

The members of the Management Board receive a fixed annual base remuneration for their services from the Company, payable in twelve equal installments.

In the reporting period the basic remuneration amounted to:

- for Mr. Müller €600,000 (gross) p.a. within the pre-form change phase and €600,000 (gross) p.a. within the post-form change phase
- for Mr. Salzmann €600,000 (gross) p.a. within the pre-form change phase and €600,000 (gross) p.a. within the post-form change phase
- for Mr. Fieser €300,000 (gross) p.a. within the pre-form change phase and €400,000 (gross) p.a. within the post-form change phase

Additional benefits

The members of the Management Board are also granted additional benefits. These mainly comprise a company car, employer contributions to private and statutory health insurance, continued payment of wages in the event of incapacity for work due to illness or death, preventive health checks at the Com-

[13] The following 15 businesses were included in the peer group benchmarking: Brenntag, Dürr, Fraport, GEA, KION, Knorr-Bremse, MTU Aero Engines, Nemetscheck, Osram, Rational, Rheinmetall, Siltronic, Software, TeamViewer, Varta.

pany’s expense, group accident insurance, term life insurance, reimbursement of home travel expenses,[14] and a housing cost subsidy for a secondary residence[15]. The additional benefits are limited to a maximum amount in accordance with section 7 of the Management Board Service Agreement (within the post-form change phase).

Pension benefits

For the duration of the Managing Director service contract (pre-form change phase) and respectively the Management Board service contract (post-form change phase), the Management Board members are entitled to participate in the pension plan “P3 – personal pension plan for managers and executives” (or a comparable successor plan) in its currently valid version. The annual contribution is 1.75 % of the eligible remuneration plus 14 % of the proportion of the remuneration which exceeds the contribution assessment limit in the statutory pension insurance (§§ 159, 275a SGB VI, as applicable) applicable to the employee at the time the contribution is provided.

3.2. Variable Remuneration

In addition to the fixed basic remuneration, the members of the Management Board receive an STI annual bonus depending on the annual performance and an additional LTI bonus relating to the long-term, sustainable success of the HENSOLDT-Group from the first fiscal year beginning in the post-from change phase (i.e., starting from the fiscal year 2021) in accordance with the applicable compensation regulations.

Subsequent changes to the target values or reference parameters for the STI bonus and the LTI bonus are generally excluded. The Supervisory Board does, however, have the option of taking appropriate account of extraordinary developments when assessing targets.

STI annual bonus

The members of the Management Board have the opportunity to receive an STI annual bonus depending on the annual performance of the Company. The STI annual bonus is rewarding the achievements of the short- to medium-term business objectives of the HENSOLDT-Group. The corresponding target values are approved by the Supervisory Board as part of the determination of the annual budget. The STI annual bonus is payable within thirty workdays after the approval of the consolidated financial statements for the past fiscal year.

For the fiscal year 2020 an annual target bonus was set, which depends on the achievement of certain equally weighted financial targets of the HENSOLDT Group (based on the target values for: adjusted free cash flow, adjusted EBITDA and order intake). The target achievement of the STI annual bonus for the reporting year is based on the performance targets for the 2020 annual bonus applicable under the original Managing Director service contracts (in conjunction with the applicable bonus plan thereunder).

Effective from January 1, 2021, the STI annual bonus is measured by the three equally weighted STI-bonus components: free cash flow, EBITDA and annual revenue, which are determined on a consolidated basis for the HENSOLDT Group.

The target bonus for 100 % target achievement amounts to:

- for Mr. Müller €600,000 (gross) p.a. within the reporting period and €550,000 (gross) p.a. from fiscal year 2021
- for Mr. Salzmann €550,000 (gross) p.a. within the reporting period and €500,000 (gross) p.a. from fiscal year 2021

[14] This only concerns the Management Board member Axel Salzmann.
[15] This only concerns the Management Board member Axel Salzmann.

* for Mr. Fieser €300,000 (gross) p.a. within the reporting period and €300,000 (gross) p.a. from fiscal year 2021

Terms of payment of the STI in the fiscal year 2020:

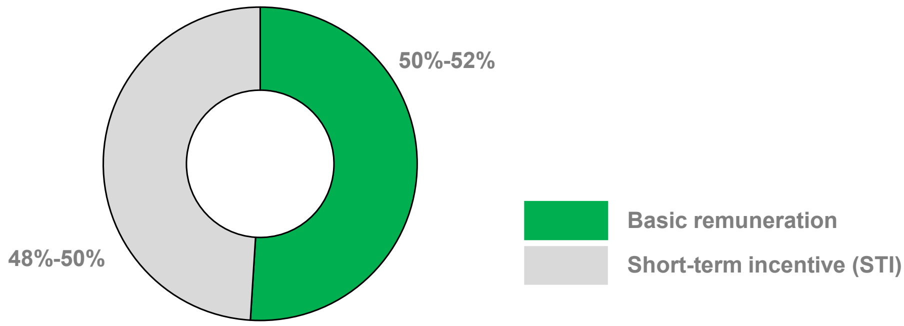
Bonus component	weighting	Disbursement % of target value <80% of target value	>80% and <100% of target value*	target value	>100% and <120% of target value*	>120% of target value**
adjusted Free Cash Flow	33%	0%	linear reduction in the ratio 1:5	100%	linear increase in the ratio 1:2.5	150%*
adjusted EBITDA	33%	0%	linear reduction in the ratio 1:5	100%	linear increase in the ratio 1:2.5	150%*
Order Intake	33%	0%	linear reduction in the ratio 1:5	100%	linear increase in the ratios 1:2.5	150%*

* If the respective target value for an STI bonus component is not reached, the respective bonus component is reduced on a straight-line basis in the ratio 1:5. If one target value for an STI bonus component is exceeded, the respective bonus component increases on a straight-line basis in the ratio 1:2,5.

** The linear increase in the bonus component only occurs if a target value of more than 80 % for all three STI bonus components has been achieved.

The relative proportion of the STI annual bonus varies between the different positions within the Management Board and is based on a contractually agreed target value of 90-100 % of the basic remuneration.

The targeted direct remuneration granted to all Management Board members in the reporting period therefore comprises basic remuneration and variable remuneration as follows:



In the case of premature termination of the employment relationship for a material reason within the meaning of section 626 of the German Civil Code (BGB) for which the Management Board member is responsible the entitlement of the Management Board member to any STI annual bonus shall expire.

Apart from that in the event of a termination of the contract during the year, the Management Board member's outstanding claims to an STI annual bonus attributable to the period up to termination of the contract will be paid out in installments in accordance with the agreed targets and comparison parameters and the defined due date.

Long-Term Incentive

The Management Board members participate starting with the first fiscal year beginning in the post-form change phase (fiscal year 2021) in the respective applicable LTI bonus. Each fiscal year a new evaluation period (Performance Period) begins, in accordance with the terms and conditions of the applicable LTI bonus, after which the achievement of certain predefined targets is measured. The first LTI bonus applies for the fiscal year 2021 with the performance period 2021 - 2024.

At the beginning of the respective four-year evaluation period of an LTI bonus tranche, the Supervisory Board shall determine at its reasonable discretion the terms and conditions for each LTI bonus component and the corresponding target values of the relevant bonus tranche. Unless the Supervisory Board resolves to redefine the LTI terms, the conditions of the current LTI bonus will apply to the respective next performance period.

The terms of the currently applicable LTI bonus provide for the assignment of virtual shares (Performance Share Units) at the beginning of each fiscal year within the performance period from 2021 - 2024. The initially allocated Tranche of Performance Share Units serves as measurement parameter for the subsequent determination of any LTI bonus payout amount, taking into account the performance measurement/ target achievement after the end of the four-year assessment period. At the beginning of the respective measurement period, the Management Board member receives a number of virtual shares ('stock rights') calculated by dividing the target amount of the LTI target bonus by the average price of the shares of HENSOLDT AG.

The assignment value (target amount) amounts to €650,000 for Mr. Müller, €600,000 for Mr. Salzmann and €400,000 for Mr. Fieser.

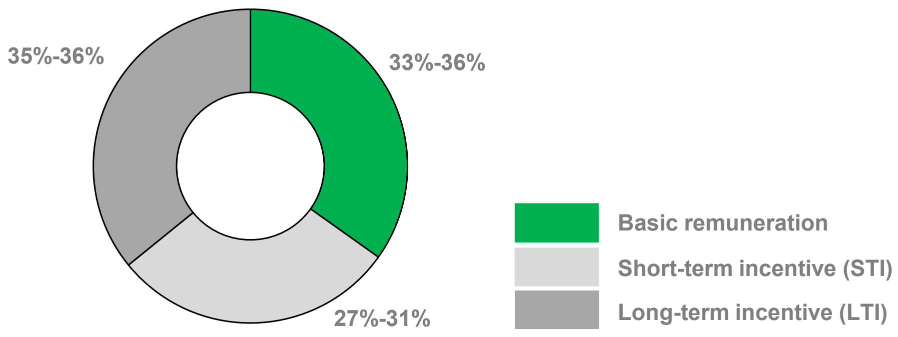
At the end of the respective measurement period, an overall target achievement level is determined for the performance targets set by the Supervisory Board before the start of the performance period.

On the basis of the currently applicable conditions of the LTI bonus the final number of performance share units is determined at the end of the performance period by multiplying the initial number of performance share units with the overall target achievement. The overall degree of target achievement is determined from the degree of target achievement of the individual targets set by the Supervisory Board for the respective performance period. As part of the LTI bonus for the performance period 2021 - 2024 the targets include at least (i) one target relating to the share price/ share return, (ii) one long-term financial target and (iii) one sustainable target.

The LTI bonus to be paid out as a cash entitlement is determined by multiplying the final number of performance share units with the average closing price of the shares of HENSOLDT AG. If the share price remains unchanged and the target achievement equals 100% (without intervention of clawback offenses) the payout amount of the LTI bonus would thus equal the initial assignment value. As a rule, the maximum payout amount of a LTI tranche can (before consideration of clawback offenses) not exceed 200% of the LTI target value.

The relative share of the LTI bonus varies between the position of the Management Board members and is based on the contractually agreed target value of 100%-110% of the basic remuneration.

The target direct remuneration intended in the future remuneration system for the average of all Management Board members will thus comprise basic remuneration and variable remuneration as follows:



Clawback

The STI annual bonus and the LTI bonus are subject to clawback conditions as from the IPO onwards. This means the Company has a claim against the Management Board member for repayment of the STI annual bonus and LTI bonus paid out if, after payment of the STI annual bonus and LTI bonus, it turns out that objectively incorrect audited and approved consolidated financial statements and/or management report, which requires subsequent correction, was used in calculating the amount of the bonus payment. In this respect the fault of the Management Board member is not important – or if the Management Board member has breached his duties to the Company in a grossly negligent manner, in particular his compliance duties.

The Supervisory Board decides on the amount of the repayment claim at its due discretion. Variable remuneration amounts already paid out can be reclaimed if a clawback event occurs. The claim for repayment also exists if the Management Board appointment and/or the service contract with the Management Board member has already ended at the time the claim for repayment becomes due.

3.3. Maximum remuneration

The remuneration of the Management Board members consisting of the basic annual remuneration, the STI annual bonus and the LTI bonus as well as additional benefits and pension contributions according to the Management Board service agreements amounts to a maximum of:

- for Mr. Müller €3.5 Million (gross) p.a.
- for Mr. Salzmann €3.3 Million (gross) p.a. and
- for Mr. Fieser €2.5 Million (gross) p.a.

3.4. Shares retention program

The members of the Management Board are obliged to hold shares of HENSOLDT AG for the duration of their appointment as a member of the Management Board, whereby this obligation must be fulfilled for the first time latest four years after the initial appointment as a member of the Management Board. The share retention program is designed to support the Company's equity story and incentivize the members of the Management Board to increase the value of the Company in the interest of the shareholders.

The share retention obligation is determined based on the (gross) basic annual remuneration and amounts for the chairman of the Management Board to 150 %, for the CFO 120 % and for all other ordinary members of the Management Board 100 % of the basic annual remuneration.

Until the end of the Management Board service agreement the Management Board member must not transfer, assign, pledge or otherwise dispose or undertake to dispose in any other way HENSOLDT AG shares held under the share retention program. From the end of the Management Board service agreement on, the Management Board member can sell each year up to 50 % of the HENSOLDT AG shares held.

3.5. Benefits in the event of premature termination of employment

In the event of premature termination of the appointment, the Management Board members are entitled to a severance payment. The severance payment is limited to two years' remuneration and is reduced on a pro rata temporis basis if the remaining term of the Management Board service contract is less than two years. The amount of the annual remuneration is determined by the sum of the annual basic remuneration and the STI target value for the last full fiscal year before the end of the Management Board service agreement. Any claims of the Management Board member to the LTI bonus shall remain unaffected by the severance payment.

A deviating regulation applies for the early termination of the Management Board service agreement due to permanent incapacity to work. In this case the Management Board member receives a severance payment in the amount of one annual basic remuneration, which is reduced on a pro rata temporis basis if the remaining term of the Management Board service agreement is less than one year. If the Management Board activity ends prematurely due to the death of the Management Board member, the heirs are entitled to 1/12 of the annual basic remuneration for the month in which the Management Board service agreement ends as well as for the six following months, but at the longest until the end of the contractual term stipulated in the Management Board service agreement.

In the event of an effective extraordinary termination of the Management Board service agreement for a material cause by the Company or in the event of resignation by the Management Board member without a material cause, the Management Board member does not receive a severance payment.

The Management Board members are subject to a post-contractual non-competition clause for a period of one year. During this period the Management Board member is entitled to a compensation of monthly 50 % (gross) of the proportional annual basic remuneration most recently received by the Management Board member on a monthly basis. The compensation is paid at the end of each month. The severance payment will be offset in the full amount against the entitlement.

A so-called “Change-of-Control” clause, which means a special right of termination in the event of a change of control, existed only within the previous Managing Director employment contracts of the HENSOLDT Holding GmbH. Such a special right of termination is not part of the Management Board service agreements concluded in September 2020.

4. Remuneration of the Supervisory Board

Within the pre-form change phase at HENSOLDT GmbH there was no shareholder resolution about the remuneration of the Supervisory Board members. After the effectiveness of the form change, the remuneration of the Supervisory Board members is based on section 12 of the articles of association of HENSOLDT AG.

According to the articles of association, the fixed annual remuneration of each Supervisory Board member amounts to €40,000 after the change of the legal form. The chairman of the Supervisory Board receives twice the amount, thus €80,000, the vice Chairman receives one and a half times this amount, thus €60,000. For their work on the Executive Committee, Nominating Committee, Audit Committee, Compliance Committee, the members receive additional fixed compensation amounting to €10,000. The Chairpersons of these Committees receive €15,000 each.

The maximum remuneration for Supervisory Board members is provided for in section 12 (3) in the articles of association and amounts to twice the amount of the annual remuneration of the Supervisory Board members according to section 12 (1) in the articles of association. Supervisory Board members who are members of the Supervisory Board or a Committee or are Chairperson of a committee for only part of the fiscal year, receive a remuneration which is lower in proportion to the time served.

The Company reimburses the members of the Supervisory Board for expenses incurred in the performance of their duties, including any value-added tax payable on the reimbursement of expenses.

5. Individual disclosure of the remuneration granted or paid to the Management Board in the fiscal year 2020

Grants awarded for the reporting period – Group (January 1 to December 31, 2020)

	Thomas Müller* CEO				Axel Salzmann* CFO				Peter Fieser* CHRO			
	Fiscal year				Fiscal year				Fiscal year			
in €	2020	2020(min)	2020(max)	2019	2020	2020(min)	2020(max)	2019	2020	2020(min)	2020(max)	2019
Annual basic remuneration	600,000	600,000	600,000	600,000	600,000	600,000	600,000	600,000	339.288**	339,288	339,288	300,000
Additional benefits	37,707	37,707	37,707	44,002	138,627	138,627	138,627	140,952	36,614	36,614	36,614	51,914
Total	**637,707**	**637,707**	**637,707**	**644,002**	**738,627**	**738,627**	**738,627**	**740,952**	**375,902**	**375,902**	**375,902**	**351,914**
STI annual bonus	600,000	-	900,000	600,000	550,000	-	825,000	550,000	300,000	-	450,000	300,000
LTI bonus	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Total	**1,237,707**	**637,707**	**1,537,707**	**1,244,002**	**1,288,627**	**738,627**	**1,563,627**	**1,290,952**	**675,902**	**375,902**	**825,902**	**651,914**
Pension expense	174,127	174,127	174,127	177,744	166,252	166,252	166,252	169,869	98,418	98,418	98,418	83,244
Total remuneration	**1,411,834**	**811,834**	**1,711,834**	**1,421,746**	**1,454,878**	**904,878**	**1,729,878**	**1,460,821**	**774,319**	**474,319**	**924,319**	**735,158**

* The holder of the position was appointed as Managing Director of HENSOLDT GmbH by shareholder resolution from October 28, 2019, and was previously employed by HENSOLDT Holding GmbH (former parent Company of the group).

** The annual basic remuneration of Peter Fieser increased from €300,000 to €400,000 effective from August 17, 2020. This results in an annual average of €339,288.

Inflow in the reporting period – Group (January 1 to December 31, 2020)

	Thomas Müller* CEO		Axel Salzmann* CFO		Peter Fieser* CHRO	
	Fiscal year		Fiscal year		Fiscal year	
in €	2020	2019	2020	2019	2020	2019
Annual basic remuneration	600,000	600,000	600,000	600,000	339,286	300,000
Additional benefits	37,707	44,002	138,627	140,952	36,614	51,914
Total	**637,707**	**644,002**	**738,627**	**740,952**	**375,900**	**351,914**
STI annual bonus	450,000	660,000	412,500	605,000	225,000	302,500
LTI bonus	n/a	n/a	n/a	n/a	n/a	n/a
Others	-	-	-	-	-	-
Total	**1,087,707**	**1,304,002**	**1,151,127**	**1,345,952**	**600,900**	**654,414**
Pension expense	174,127	177,744	166,252	169,869	98,418	83,244
Total remuneration	**1,261,834**	**1,481,746**	**1,317,378**	**1,515,821**	**699,317**	**737,658**

* The holder of the position was appointed as Managing Director of HENSOLDT GmbH by shareholder resolution from October 28, 2019 and was previously employed by HENSOLDT Holding GmbH (former parent Company of the group).

Total grants by the Company according to HGB – Group (January 1 to December 31, 2020)

	Thomas Müller* CEO		Axel Salzmann* CFO		Peter Fieser* CHRO	
	Fiscal year		Fiscal year		Fiscal year	
in €	2020	2019	2020	2019	2020	2019
Fixed remuneration	600,000	600,000	600,000	600,000	339,286	300,000
Additional benefits	37,707	44,002	138,627	140,952	36,614	51,914
Total	**637,707**	**644,002**	**738,627**	**740,952**	**375,900**	**351,914**
Variable remuneration	600,000	450,000	550,000	412,500	300,000	302,500
Total variable remuneration	**600,000**	**450,000**	**550,000**	**412,500**	**300,000**	**225,000**
Pension expenses	174,127	177,744	166,252	169,869	98,418	83,244
Total remuneration	**1,411,834**	**1,271,746**	**1,454,878**	**1,323,321**	**774,317**	**660,158**

* The entry date corresponds to the beginning of the appointment as Managing Director of the same Company. The holder of the position was appointed as Management Board member by resolution on August 11, 2020, in the course of the change of legal form and became member of the Management Board upon registration of the change of legal form on August 17, 2020.

Grants awarded for the reporting period – HENSOLDT AG (August 17 to December 31, 2020)

	Thomas Müller* CEO				Axel Salzmann* CFO				Peter Fieser* CHRO			
	from August 17, 2020				from August 17, 2020				from August 17, 2020			
in €	2020	2020(min)	2020(max)	2019	2020	2020(min)	2020(max)	2019	2020	2020(min)	2020(max)	2019
Basic remuneration, pro rata**	235,710	235,710	235,710	n/a	235,710	235,710	235,710	n/a	157,140	157,140	157,140	n/a
Additional benefits	12,820	12,820	12.820***	n/a	47,324	47,324	47.324***	n/a	9,293	9,293	9.293***	n/a
Total	**248,530**	**248,530**	**248,530**	**n/a**	**283,034**	**283,034**	**283,034**	**n/a**	**166,433**	**166,433**	**166,433**	**n/a**
STI annual bonus, pro rata	235,710	-	353,565	n/a	216,068	-	324,101	n/a	117,855	-	176,783	n/a
LTI bonus	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Total	**484,240**	**248,530**	**602,095**	**n/a**	**499,101**	**283,034**	**607,135**	**n/a**	**284,288**	**166,433**	**343,216**	**n/a**
Pension expense	67,909	67,909	67,909	n/a	64,838	64,838	64,838	n/a	38,383	38,383	38,383	n/a
Total remuneration	**552,150**	**316,440**	**670,004**	**n/a**	**563,940**	**347,872**	**671,973**	**n/a**	**322,671**	**204,816**	**381,598**	**n/a**

* The entry date corresponds to the beginning of the appointment as Managing Director of the same Company. The holder of the position was appointed as Management Board member by resolution on August 11, 2020, in the course of the change of legal form and became member of the Management Board upon registration of the change of legal form on August 17, 2020.

** The daily pro rata billing is based on the number of tax days.

*** The additional benefits are limited in accordance with Article 7.1 of the Management Board service agreement.

Inflow in the reporting period – HENSOLDT AG (August 17 to December 31, 2020)

	Thomas Müller* CEO		Axel Salzmann* CFO		Peter Fieser* CHRO	
	from August 17, 2020		from August 17, 2020		from August 17, 2020	
in €	2020	2019	2020	2019	2020	2019
Annual basic remuneration	235,714	n/a	235,714	n/a	157,143	n/a
Additional benefits	12,820	n/a	47,324	n/a	9,293	n/a
Total	**248,535**	**n/a**	**283,038**	**n/a**	**166,436**	**n/a**
STI annual bonus	-	n/a	-	n/a	-	n/a
LTI bonus	n/a	n/a	n/a	n/a	n/a	n/a
Others	-	n/a	-	n/a	-	n/a
Total	**248,535**	**n/a**	**283,038**	**n/a**	**166,436**	**n/a**
Pension expense	67,909	n/a	64,838	n/a	38,383	n/a
Total remuneration	**316,444**	**n/a**	**347,876**	**n/a**	**204,819**	**n/a**

* The entry date corresponds to the beginning of the appointment as Managing Director of the same Company. The holder of the position was appointed as Management Board member by resolution on August 11, 2020, in the course of the change of legal form and became member of the Management Board upon registration of the change of legal form on August 17, 2020.

Total grants by the Company according to HGB – HENSOLDT AG (August 17 to December 31, 2020)

	Thomas Müller* CEO		Axel Salzmann* CFO		Peter Fieser* CHRO	
	from August 17, 2020		from August 17, 2020		from August 17, 2020	
in €	2020	2019	2020	2019	2020	2019
Fixed remuneration	235,714	n/a	235,714	n/a	157,143	n/a
Additional benefits	12,820	n/a	47,324	n/a	9,293	n/a
Total	**248,535**	**n/a**	**283,038**	**n/a**	**166,436**	**n/a**
Variable remuneration	235,710	n/a	216,068	n/a	117,855	n/a
Total variable remuneration	**235,710**	**n/a**	**216,068**	**n/a**	**117,855**	**n/a**
Pension expenses	67,909	n/a	64,838	n/a	38,383	n/a
Total remuneration	**552,154**	**n/a**	**563,944**	**n/a**	**322,674**	**n/a**

* The entry date corresponds to the beginning of the appointment as Managing Director of the same Company. The holder of the position was appointed as Management Board member by resolution on August 11, 2020, in the course of the change of legal form and became member of the Management Board upon registration of the change of legal form on August 17, 2020.

6. Individual disclosure of the remuneration for the Supervisory Board in the fiscal year 2020

Calculation for the remuneration of the Supervisory Board at the level of HENSOLDT Holding GmbH (January 1 to August 16, 2020)

	Until August 16, 2020		
in €	Total 2020	Fixed remuneration	Committee remuneration
Johannes Huth	33,333	26,667	6,667
Christian Ollig	-	-	-
Claire Wellby	26,667	26,667	-
Prof. Wolfgang Ischinger	33,333	26,667	6,667
Ingrid Jägering	33,333	26,667	6,667
Prof. Burkhard Schwenker	33,333	26,667	6,667
Armin Maier-Junker	33,333	26,667	6,667
Winfried Fetzer	33,333	26,667	6,667
Thomas Hoepfner	33,333	26,667	6,667
Peter Härtle	8,333	6,667	1,667
Dr. Frank Döngi	25,000	20,000	5,000
Jürgen Bühl	33,333	26,667	6,667
Julia Wahl	33,333	26,667	6,667

Calculation for the remuneration of the Supervisory Board at the level of HENSOLDT AG (August 17 to December 31, 2020)

	from August 17, 2020		
in €	Total 2020	Fixed remuneration	Committee remuneration
Johannes Huth	45,833	33,333	12,500
Christian Ollig	-	-	-
Claire Wellby	16,667	16,667	-
Prof. Wolfgang Ischinger	25,000	16,667	8,333
Ingrid Jägering	27,083	16,667	10,417
Prof. Burkhard Schwenker	22,917	16,667	6,250
Armin Maier-Junker	29,167	25,000	4,167
Winfried Fetzer	20,833	16,667	4,167
Marion Koch	20,833	16,667	4,167
Frank Döngi	20,833	16,667	4,167
Jürgen Bühl	20,833	16,667	4,167
Julia Wahl	20,833	16,667	4,167

VII. Takeover-relevant information and explanatory report

The takeover-relevant information and the explanatory report for the fiscal year 2020 are made in accordance with section 289a (1) and section 315a (1) HGB, in each case in the version applicable to this report pursuant article 83 (1) sentence 2 EGHGB.

1. Composition of share capital

As of December 31, 2020, the share capital of HENSOLDT AG amounts to €105.0 million and is divided into 105,000,000 ordinary bearer shares (no-par value shares). The shares are fully paid up. All shares carry the same rights and obligations. The rights and obligations of shareholders arise in detail from the provisions of the German Stock Corporation Act (AktG), in particular sections 12, 53a et seqq., 118 et seqq. and 186 AktG.

2. Restrictions on voting rights or transfer of shares

Each share grants one vote at the shareholders' meeting and is decisive for the shareholders' share in the company's profit. Excluded from this are treasury shares held by the Company, which do not entitle the company to any rights pursuant to section 71b AktG. In the cases of section 136 AktG, the voting rights from the relevant shares are excluded by law. Violations against the notification requirements according to section 33 (1), section 38 (1) and section 39 (1) German Securities Trading Act (WpHG) can lead to a situation where rights arising from shares and also voting rights are at least temporarily suspended according to section 44 WpHG.

The German Federal Ministry for Economic Affairs and Energy ("BMWi") may examine the direct or indirect acquisition of shares in the Company by a foreign acquirer if, following the acquisition, the acquirer will directly or indirectly hold 10 % or more of the voting rights in the Company. According to the provisions in sections 60 et seqq. of the Foreign Trade and Payments Ordinance, the intended acquisition must be notified in writing to the BMWi, which will only approve the acquisition if it does not conflict with any essential security interests of the Federal Republic of Germany. If section 60 of the Foreign Trade and Payments Ordinance is not applicable, the BMWi may nevertheless prohibit or restrict the acquisition if this would endanger public order or security in Germany or in another EU member state (cross-sectoral examination).

In the course of the IPO of HENSOLDT AG, Square Lux Holding II S.à r.l. entered into a lock-up obligation vis-à-vis the syndicate banks for the shares held by it or its affiliates for a period of six months from the date of the IPO on September 25, 2020. Certain transactions are excluded from this.

In connection with article 19 (11) of the Regulation (EU) No. 596/2014 (Market Abuse Regulation) and on the basis of internal rules for members of the Management Board and Supervisory Board, several restrictions exist for the purchase and sale of shares of HENSOLDT AG, in particular in the temporal context with the publication of financials, as well as holding obligations in connection with the compensation of the Management Board.

Otherwise, the Management Board is not aware of any agreements by shareholders of HENSOLDT AG containing restrictions for the exertion of voting rights or the transfer of shares.

3. Shareholdings exceeding 10.0 % of the voting rights

To the Company's knowledge, the following direct or indirect shareholdings in the voting capital of HENSOLDT AG exceeding 10.0 % of the voting rights existed as of the balance sheet date:

- With voting rights notifications dated September 28, 2020, KKR Management LLP, Wilmington, Delaware, United States of America, and KKR SP Limited, George Town, Grand Cayman, Cayman Islands, as persons subject to the reporting requirements pursuant to section 40 WpHG, each reported that 66,666,666 voting rights were indirectly attributed to them. In relation to the share capital of HENSOLDT AG, which is divided into 105,000,000 shares, this represents a share of approximately 63.5 % of the voting rights. The voting rights are, in each case, held directly by Square Lux Holding II S.à r.l. as shareholder.
- Further, KKR Management LLP, Wilmington, Delaware, United States of America, and KKR SP Limited, George Town, Grand Cayman, Cayman Islands, as persons subject to the reporting requirements pursuant to section 40 WpHG, each reported, in the voting rights notifications of September 28, 2020, an instrument also attributable to them relating to the acquisition of a total of 5,000,000 voting rights with a term until November 5, 2020. In relation to the share capital of HENSOLDT AG, which is divided into 105,000,000 shares, this represents a share of approximately 4.8 % of the voting rights.
- With voting rights notification dated September 30, 2020, the Federal Republic of Germany, Berlin, reported an acquisition right relating to a total of 26,355,000 shares and, thus, voting rights with an exercise period from October 1, 2020 to December 31, 2020. In relation to the share capital of HENSOLDT AG, which is divided into 105,000,000 shares, this corresponds to a share of 25.1 % of the voting rights. On December 17, 2020, the Federal Republic of Germany announced its intention to acquire 25.1 % of the shares in HENSOLDT AGfrom Square Lux Holding II S.à r.l. in exercise of this acquisition right (execution expected in 2021).

Other direct or indirect shareholdings in the Company's capital exceeding 10.0 % of voting rights have not been reported to the Company nor has the Company become aware of any such shareholdings in any other way.

4. Shares with special rights of control

Shares with special rights of control do not exist.

However, the Federal Republic of Germany (represented by the Federal Ministry of Defense together with the Federal Ministry for Economic Affairs and Energy or the corresponding ministry succeeding it in the respective function) is entitled, as soon as and for as long as it is a shareholder of the Company, to appoint one of the members attributable to the shareholders to the Supervisory Board. As long as Square Lux Holding II S.à r.l., Luxemburg is a shareholder of the Company, the right of delegation of the Federal Republic of Germany described above exists as a joint right of delegation of the Federal Republic of Germany and Square Lux Holding II S.à r.l. The Federal Republic of Germany furthermore has the right to delegate one further member attributable to the shareholders to the Supervisory Board, as long as the Federal Republic of Germany directly or indirectly holds shares amounting to at least 25.1 % of the Company's share capital. Further details of this right of delegation, including further modalities of exercise, can be found in section 8 (2) of the articles of association of the Company.

5. Type of voting rights control if employees have an interest in the capital and do not exercise their control rights directly

There are no stock option programs under which control rights are not exercised directly. Employees who hold shares of HENSOLDT AG exercise their control rights in the same way as other shareholders in accordance with legal requirements and the articles of association.

6. Legal requirements and provisions of the articles of association concerning the appointment and dismissal of members of the Management Board and amendments to the articles of association

The appointment and dismissal of members of the Management Board are governed by sections 84 and 85 AktG as well as section 31 of the German Codetermination Act (MitbestG). Pursuant to section 6 (1) of the articles of association, the Management Board shall consist of at least two members, the number of members of the Management Board shall be determined by the Supervisory Board. The articles of association also stipulate that the Supervisory Board may appoint a member of the Management Board as chairman of the Management Board.

Pursuant to sections 119 (1) no. 6 and 179 AktG, any amendment of the articles of association requires a resolution of the shareholders' meeting The authority to make amendments that only affect the wording is delegated to the Supervisory Board according to section 10 (9) of the articles of association. Further, the Supervisory Board has been authorized by resolutions of the shareholders' meeting to amend section 4 of the articles of association in accordance with the respective utilization of Conditional Capital 2020/I and, in the event of non-utilization after the expiry of the authorization period or the expiry of the exercise and fulfillment periods, and in accordance with the utilization of Authorized Capital 2020/I.

According to section 179 (2) AktG, resolutions of the shareholders' meeting amending the articles of association require a majority of at least three quarters of the share capital represented when the resolution is adopted, unless the articles of association stipulate a different capital majority. Section 16 (2) of the articles of association of HENSOLDT AG stipulates a different capital majority in this respect. Accordingly, unless otherwise stipulated by the articles of association or by law, resolutions of the annual shareholders' meeting are adopted by a simple majority of the votes cast and, if a capital majority is also required, by a simple majority of the share capital represented when the resolution is adopted. However, the majority pursuant to section 16 (2) of the articles of association does not apply in particular to a change in the Company's business purpose, since in this respect only a larger capital majority may be specified in the articles of association according to section 179 (2) sentence 2 AktG. The capital majorities of at least three quarters of the share capital represented at the time thef resolution is adopted, which are required by law for an amendment to the articles of association in addition to the simple majority of votes, also remain unaffected. This applies in particular to resolutions on the creation of conditional capital, section 193 (1) sentence 1 AktG, the creation of authorized capital, section 202 (2) sentence 2 AktG, a capital increase from company funds, section 207 (2) sentence 1 AktG, reductions of share capital, section 222 (1) sentence 1 AktG as well as section 229 (3) AktG, and the redemption of shares, section 237 (2) sentence 1 AktG.

7. Authority of the Management Board to issue or repurchase shares

7.1. Conditional capital

By resolution of the shareholders' meeting on August 18, 2020, the Management Board was authorized, subject to the approval of the Supervisory Board, to issue bearer or registered bonds with warrants and/or convertible bonds, profit participation rights and/or participating bonds, or a combination of these instruments for a total nominal amount of up to €500 million, with or without limited term, on one or more occasions up to August 11, 2025, in return for contributions in cash or in kind and to grant or impose option rights or obligations on the holders or creditors of bonds with warrants or participatory certificates with warrants or participating bonds with warrants, or grant or impose conversion rights or obligations on the holders of convertible bonds or participatory certificates with warrants or convertible participating bonds, in respect of bearer shares with no par value of the Company representing a pro rata amount of the share capital of up to €16.0 million in total, in accordance with the respective terms and conditions of these bonds.

The bonds may be issued in euros or in the legal currency of a member country of the Organization for Economic Cooperation and Development (”OECD”), limited to the equivalent value in euros. They may also be issued by a subordinated Group company of the Company;in this case, the Management Board is authorized subject to the approval of the Supervisory Board to assume the guarantee for the bonds on behalf of the Company and to grant or impose option or conversion rights or obligations on the holders in respect of bearer shares with no par value of the Company. Further details are contained in the authorization resolution.

The shareholders are generally entitled to a subscription right to the bonds. Insofar as the shareholders are not enabled to subscribe directly to the bonds, the shareholders shall be granted the statutory subscription right in such a way that the bonds are taken over by a credit institution or a syndicate of credit institutions with the obligation to offer them to the shareholders for subscription. If the bonds are issued by a subordinated Group company, the Company must ensure that the statutory subscription right is granted to the Company's shareholders in accordance with the preceding sentence.

However, the Management Board is authorized, subject to the approval of the Supervisory Board, to exclude fractional amounts resulting from the subscription ratio from the shareholder’s subscription right and also to exclude the subscription right to the extent necessary to grant holders of previously granted option or conversion rights as well as imposed option or conversion obligations a subscription right to the extent to which they would be entitled as shareholders after exercising the option or conversion rights or upon fulfillment of the option or conversion obligation.

The Management Board is also authorized, subject to the approval of the Supervisory Board, to fully exclude subscription rights of shareholders to bonds issued in return for cash contributions which are issued with option or conversion rights or option or conversion obligations, provided that the Management Board, after due examination, is of the opinion that the issue price of the bond is not significantly lower than its hypothetical market value calculated in accordance with recognized methods, in particular financial mathematics methods. However, this authorization to exclude subscription rights only applies to bonds issued with option or conversion rights or option or conversion obligations, with an option or conversion right or an option or conversion obligation on shares with a pro rata amount of the share capital which in total may not exceed 10.0 % of the share capital, either at the time this authorization becomes effective or – if this value is lower – at the time it is exercised. Shares sold or issued under exclusion of subscription rights pursuant to section 186 (3) sentence 4 AktG during the term of this authorization up to the issue of the bonds with option or conversion rights or option or conversion obligations without subscription rights pursuant to section 186 (3) sentence 4 AktG shall count towards the aforementioned 10.0 % limit.

Insofar as profit participation rights or participating bonds are issued without conversion rights or conversion obligations or option rights or option obligations, the Management Board is authorized, subject to the approval of the Supervisory Board, to exclude the shareholders’ subscription rights altogether if these profit participation rights or participating bonds have bond-like features, i.e. do not confer any membership rights in the Company, do not grant any participation in liquidation proceeds and the amount of interest is not calculated on the basis of the amount of net income for the year, of the net retained profits or of the dividend. In this case the interest rate and the issue amount of the profit participation rights or participating bonds must correspond to the current market conditions at the time of issue.

The Management Board is also authorized, subject to the approval of the Supervisory Board, to exclude shareholders’ subscription rights to bonds issued against contributions in kind with option or conversion rights or option or conversion obligations, in particular in the case of the acquisition of companies, parts of companies, equity interests in companies or other assets, including rights and receivables, or in connection with business combinations.

In order to grant shares to the holders or creditors of the aforementioned instruments, the share capital of HENSOLDT AG is conditionally increased by up to €16.0 million, divided into up to 16,000,000 new bearer shares with no par value (Conditional Capital 2020/1). Further details of the Conditional Capital 2020/I can be found in section 4 (4) of the articles of association.

7.2. Authorized capital

The Management Board is authorized, subject to the approval of the Supervisory Board, to increase the share capital on or before August 11, 2025, on one or more occasions by in total up to €36.0 million by issuing new bearer shares with no par value in return for contributions in cash or in kind (Authorized Capital 2020/I).

When shares are issued from Authorized Capital 2020/I, shareholders must generally be granted subscription rights. However, the Management Board is authorized, in each case subject to the approval of the Supervisory Board, to exclude subscription rights of shareholders on one or more occasions in each of the following cases:

- in order to exclude fractional amounts from shareholders' subscription rights in the event of capital increases against cash contributions or contributions in kind;
- to the extent necessary to grant subscription rights to the new bearer shares with no par value to holders or creditors of option or conversion rights granted or option or obligations imposed by the Company or by its direct or indirect affiliated companies in the scope to which they would be entitled as shareholders after exercising the option or conversion right or after fulfilling the option or conversion obligation as shareholders;
- insofar as the capital increase takes place against contributions in kind, in particular in the case of the acquisition of companies, parts of companies, participations in companies or other assets, including rights and receivables, or in the context of mergers;
- for the purpose of issuing shares to employees of the Company and employees and members of the management of subordinated Group companies, with regard to employees also in compliance with the requirements of section 204 (3) AktG;
- in the case of capital increases against cash contributions, if the subscription price for which the new bearer shares with no par value are issued does not significantly fall short of the market price at the time of final determination of the amount for which the shares are issued, which should be as close as possible to the placement of the bearer shares with no par value (simplified exclusion of subscription rights in accordance with section 186 (3) sentence 4 AktG).The shares issued under exclusion of subscription right in accordance with section 186 (3) sentence 4 AktG may not exceed a total of 10.0 % of the share capital existing at the time when the resolution on the creation of this authorization is adopted or – if this value is lower – at the time when the resolution on the initial exercise of this authorization. The upper limit of 10.0 % of the share capital shall be reduced by the prorated amount of the share capital attributable to those shares issued or sold during the period of effectiveness of this authorization under the exclusion of subscription right in direct or analogous application of section 186 (3) sentence 4 AktG. Furthermore, this limit is decreased by shares that have been or may be issued in order to satisfy option or conversion rights or obligations, if the option or conversion rights or obligations were granted or imposed under exclusion of the subscription rights in accordance with section 186 (3) sentence 4 AktG during the period of effectiveness of this authorization.

In accordance with section 186 (5) AktG, the new shares may also be subscribed by a credit institution or a companyoperating in accordance with section 53 (1) sentence 1 or section 53b (1) sentence 1 or

(7) of the German Banking Act (KWG) with the obligation to offer them to the shareholders for subscription (indirect subscription right).

The Management Board is authorized, subject to the approval of the Supervisory Board, to determine the further details of the capital increase and the conditions for the issuance of shares.

7.3. Share buyback

By resolution of the shareholders' meeting on August 18, 2020, the Management Board was also authorized until August 11, 2025 to acquire treasury shares of the Company up to a total of 10.0 % of the Company's share capital existing at the time the resolution is adopted or – if one of these values is lower – at the time this authorization becomes effective or at the time this authorization is exercised. The authorization may be exercised, in each case individually or jointly, by the Company or also by subordinated Group companies of the Company or by third parties for the account of the Company or its subordinated Group companies. The authorization to acquire and use treasury shares may be exercised in full or in part, once or several times.

At the discretion of the Management Board, the shares may be purchased on the stock exchange or by means of a public purchase offer or a public invitation to shareholders to submit an offer for sale.

- If treasury shares are purchased on the stock exchange, the purchase price paid by the Company (excluding incidental costs) may not be more than 10.0 % higher or lower than the price of the Company's shares determined by the opening auction on the trading day in the Xetra trading system (or a comparable successor system) on the Frankfurt Stock Exchange.
- If the shares are purchased by means of a public offer to buy or a public invitation to submit an offer to sell, the purchase or selling price offered or the limits of the purchase or selling price range per share (excluding incidental costs) may not be more than 10.0 % higher or lower than the average closing price in the Xetra trading system (or a comparable successor system) on the Frankfurt Stock Exchange on the three trading days prior to the date of the public announcement of the offer or the public invitation to submit an offer to sell. If there is a significant deviation in the relevant price after publication of a purchase offer, the offer may be adjusted. In this case, the average price of the three stock exchange trading days prior to the day of publication of any adjustment shall be taken as the basis; the 10.0 % limit for oversubscription or undersubscription shall be applied to this amount. If the offer to purchase is oversubscribed or, in the case of an invitation to submit an offer to sell, not all of several equivalent offers can be accepted, acceptance must be in proportion to the shares tendered (tender ratios). In addition, shares may be rounded down to avoid fractional amounts.

The authorization may be exercised for any legally permissible purpose, in particular in pursuit of one or more of the purposes set out below, excluding shareholders' subscription rights in accordance with the following provisions, and may be exercised individually or jointly by the Company or a subordinated Group company or by third parties for the account of the Company or a subordinated Group company.

- The Management Board is authorized, subject to the approval of the Supervisory Board, to sell the treasury shares acquired on the basis of the authorization granted at the shareholders' meeting on August 18, 2020, also in a way other than via the stock exchange or by means of an offer to all shareholders, provided that the sale is for cash and at a price which is not significantly lower than the stock market price of shares in the Company at the time of the sale (simplified exclusion of subscription rights pursuant to section 186 (3) sentence 4 AktG). The shares sold on the basis of this authorization may not exceed a total of 10.0 % of the share capital, either at the time the resolution is adopted by the shareholders' meeting or at the time this authorization is exercised. The maximum limit of 10.0 % of the share capital shall be reduced by the pro rata amount of the share capital attributable to those shares issued during the term of this authorization with exclusion of subscription rights in direct or analogous application of section 186 (3) sentence 4 AktG. Furthermore, this limit shall be reduced by shares issued or issuable to service option or conversion rights, provided that the bonds were issued during the term of this authorization under exclusion of subscription rights in accordance with section 186 (3) sentence 4 AktG.

- The Management Board is authorized, subject to the approval of the Supervisory Board, to transfer the treasury shares acquired on the basis of the authorization granted by the shareholders' meeting on August 18, 2020 to third parties in return for contributions in kind, in particular in connection with the acquisition of companies, parts of companies, or equity interests in companies, or in connection with business combinations, as well as in connection with the acquisition of other assets, including rights and receivables.
- The Management Board is authorized, subject to the approval of the Supervisory Board, to use the treasury shares acquired on the basis of the authorization granted by the Annual shareholders' meeting on August 18, 2020 to fulfill obligations arising from conversion or option rights or conversion obligations from convertible bonds or bonds with warrants or profit participation rights or income bonds (or combinations of these instruments) issued by the Company or its subordinated Group companies which grant a conversion or option right or stipulate a conversion or option obligation.
- The Management Board is authorized, subject to the approval of the Supervisory Board, to use the treasury shares acquired on the basis of the authorization granted by the shareholders' meeting on August 18, 2020 to grant holders of convertible bonds or bonds with warrants or profit participation rights or participating bonds (or combinations of these instruments) issued by the Company or its subordinated Group companies, which grant a conversion or option right or stipulate a conversion or option obligation, treasury shares to the extent that they would be entitled to a subscription right to shares of the Company after exercising the conversion or option right or after fulfillment of the conversion or option obligation.
- The Management Board is authorized to offer for purchase the treasury shares acquired on the basis of the authorization granted by the shareholders' meeting on August 18, 2020 to persons who are or were employed by the Company or one of its affiliated companies (employee shares).

In addition, in the event of a sale of treasury shares by means of an offer to all shareholders, the Management Board may with the approval of the Supervisory Board exclude shareholders' subscription rights for fractional amounts.

In addition, treasury shares acquired on the basis of the authorization granted by the shareholders' meeting on August 18, 2020 may be retired without any further resolution by the shareholders' meeting. The retirement generally leads to a capital reduction. In derogation of this, the Management Board may determine that the share capital shall remain unchanged and instead the retirement shall increase the proportion of the share capital represented by the remaining shares in accordance with section 8 (3) AktG. In this case, the Management Board is authorized to adjust the number of shares stated in the articles of association.

The details of the authorization and particularly the limits of the possibility to exclude subscription rights and the offsetting modalities, are set out in the authorization resolution.

8. Significant agreements of the Company that are subject to a change of control due to a takeover bid

On September 7, 2020, HENSOLDT AG concluded a credit agreement with a number of lenders under which HENSOLDT AG expects to extend loans in the total amount €950.0 million. This credit agreement contains a so-called “change of control” clause, which is triggered if a person other that the person specified in the agreement directly or indirectly acquires more than 50.0 % of voting rights in HENSOLDT AG. In the case of a change of control, the loan may be called in for repayment immediately.

9. Compensation agreements concluded by the Company with members of the Management Board or employees in the event of a takeover bid

For the event of a change of control, HENSOLDT AG has not concluded any compensation agreements with its employees or with members of the Management Board or with managing directors or with employees of any direct or indirect subsidiaries.

VIII. Corporate governance statement

In this corporate governance statement, we report on the principles of corporate management and corporate management practices and on significant structures of our corporate governance for the past fiscal year in accordance with sections 289f and 315d HGB, each in the applicable version pursuant to section 83 (1) sentence 2 EGHGB. It also includes the Declaration of Conformity pursuant to section 161 AktG.

The corporate governance statement is part of the combined management report for HENSOLDT AG and the Group. In accordance with section 317 (2) sentence 6 HGB, the auditor's examination of the statements pursuant to section 289f (2) and (5) and § 315d HGB is limited to whether the statements have been made.

1. Fundamentals

HENSOLDT promotes the principles of good corporate governance in the sense of responsible, transparent corporate management and control aimed at increasing the value of the Company in the long term. This is a prerequisite for promoting the trust of national and international investors and financial markets, business partners, employees and the public in HENSOLDT. HENSOLDT bases its activities on the recommendations and suggestions of the German Corporate Governance Code ("Code").

2. Declaration of conformity pursuant to section 161 AktG as amended on December 16, 2019, published in the Federal Gazette on May 20, 2020

The Management Board and Supervisory Board of HENSOLDT AG were not subject to the obligation under section 161 AktG to issue a declaration of conformity with the Code throughout the entire fiscal year. With the admission of shares of HENSOLDT AG to the Frankfurt Stock Exchange on September 24, 2020, this obligation arose for the Management Board and the Supervisory Board. The Management Board and Supervisory Board issued the following declaration on the Code on March 5, 2021:

> "The Management Board and the Supervisory Board declare that since the admission of the shares of HENSOLDT AG, the Company has complied with the Government Commission on the German Corporate Governance Code in the version of December 16, 2019, published in the official section of the Federal Gazette (Bundesanzeiger) on May 20,2020, with the following exception:
>
> Until now, recommendation G.4 has not been complied with as the Supervisory Board will only deal with the remuneration topics in connection with the adoption of the proposed resolution on the remuneration system at the shareholders' meeting in 2021. The Supervisory Board intends to take recommendation G.4 into account. The Company will thus comply with all recommendations in the future.
>
> Taufkirchen, March 5, 2021
>
> **HENSOLDT AG**
>
> Management Board Supervisory Board"

The latest declaration of Conformity, as printed above, is available on the Company's website. Future declarations of conformity by the Company shall also be published there, and in the future, the respective declarations of conformity for the last five fiscal years will be available.

3. Disclosures on corporate governance practices

3.1. Principles

HENSOLDT is named after Moritz Hensoldt (1821-1903). He was a German pioneer in optics and precision engineering. He developed innovative technologies, which at the time revolutionized the possibilities in the fields of surveillance and reconnaissance. We still see his entrepreneurial spirit today as the key to fulfilling our mission for our customers. For this purpose, we have introduced four principles: “Collaboration” is the foundation of our culture, our most important principle. Therefore, our motto is “We are a team” - we can only innovate and succeed together. Motivated employees who take responsibility, who work together, who respect and trust each other, and who use their individual strengths to work for our Company are at the heart of a successful and well-functioning collaboration. “Continuous Improvement”, “Responsibility” and “Innovation” are the three other principles.

3.2. Suggestions of the Code

In the reporting period, HENSOLDT voluntarily complied with the suggestions of the Code with the following exceptions:

- At the time of this statement, it is unclear whether, in the event of a takeover bid, the Management Board would convene an extraordinary shareholders’ meeting at which the shareholders would discuss the takeover bid and, if necessary, decide on measures under company law (suggestion A.5). The Management Board would make this decision depending on the content of any takeover bid and the specific need for discussion and decision in each individual case, taking into account the expense of an extraordinary shareholders’ meeting.

3.3. Standards of Business Conduct

HENSOLDT is committed to the core values of integrity, quality, trust and innovation, thus securing tomorrow's success. Regardless in which business area HENSOLDT is active or which professional tasks HENSOLDT performs – HENSOLDT gains the trust of colleagues and stakeholders not only with what HENSOLDT does, but also with how HENSOLDT does it. “Doing the right thing” is not always easy, especially in the complex, international and highly regulated business environment in which HENSOLDT operates. The Standards of Business Conduct provide valuable guidance on key ethical and compliance issues and explain the mutual rights and obligations of employees and the HENSOLDT Group. As it is also important for HENSOLDT that the high standards regarding accountability are met by suppliers, HENSOLDT requires its suppliers to follow the same rules of conduct.

HENSOLDT's Standards of Business Conduct are available on the Company’s website.

3.4. Compliance

HENSOLDT’s compliance program aims to ensure the compatibility of its business activities with applicable law and regulations, but also with ethical principles, and to develop a culture of integrity. To achieve this, HENSOLDT developed and implemented a comprehensive compliance program specifically designed for the individual risk profile. If business proposals are submitted, which HENSOLDT believes involve compliance risks that are inconsistent with its values and zero-tolerance policy, we do not hesitate to reject these business opportunities.

HENSOLDT has implemented several compliance policies and procedures, including a counterparty due diligence directive, a gifts and hospitality directive, an investigation policy, a privacy policy and an offset compliance policy. One of the focal points of the compliance system is the prevention of corruption; to this end, HENSOLDT has developed an anti-corruption policy and has devoted particular attention and resources to dealing with the typical industry risk of engaging commercial agents and other third parties.

HENSOLDT's compliance process is further supported by the internal audit department, which is involved in conducting regular compliance-focused audits. HENSOLDT additionally conducts regular risk analysis to update risk assessments and improve compliance processes.

In addition, HENSOLDT has established a whistleblower system, which allows employees and external parties to report violations in person or anonymously via an “OpenLine” (anonymous telephone and e-mail hotline). HENSOLDT's compliance organization includes eleven employees as of December 31, 2020, and reports directly to the general counsel, who reports to the CEO. The Head of Compliance also reports regularly to the Compliance Committee of HENSOLDT's Supervisory Board. In addition to the Head of Compliance, eight Compliance Officers (full-time) are currently employed. Besides, there are compliance contacts in subordinate companies who report to the central compliance organization. Training courses are held both virtually and in person. For this purpose, IT tools are being used. These tools are used in particular as part of due diligence to screen potential business partners. The Management Board of HENSOLDT regularly communicates on the compliance organization via internal communication media.

Further information on the compliance organization can be found on the Company’s Website.

3.5. Risk and control management

Functioning control systems are an essential component of stable business processes. HENSOLDT’s Group-wide control systems are embedded in an overall concept, which, among other things, takes into account statutory regulations, the recommendations of the Code, international regulations and recommendations, and other company-specific guidelines. The responsible persons for the individual elements of the control system are in close contact with each other and with the Management Board and report regularly to the Supervisory Board or its committees. Similarly, the Group has a Group-wide risk management system in place, which describes and regulates functions, processes and responsibilities in a binding manner. Key features of the internal control and risk management system are explained in chapter “IV. Opportunities and risks report”.

3.6. Sustainability

HENSOLDT is aware of the special responsibility and knows the impact of the activities on society and the environment. HENSOLDT is committed to conducting its business sustainably and responsibly at all times. The Long Term Incentive bonus components for the Management Board members are among other criteria based on the achievement of the ESG targets “Diversity” and “Climate Impact”. Further information on sustainability (ESG) can be found in chapter V. “Non-financial group Statement” and on the Company’s website and further information on the Management Board remuneration and relevant target criteria in the chapter VI. “Remuneration report”.

3.7. Shareholders and shareholders’ meeting

The shareholders of HENSOLDT AG exercise their rights at the shareholders’ meeting. The shareholders’ meeting decides on all matters assigned to it by law, including the appropriation of profits, the discharge of the Management Board and the Supervisory Board, and the election of the auditor. The shareholders’ meeting also elects the Supervisory Board members representing the shareholders. By using electronic means of communication, especially the internet, the Management Board extends the possibilities for shareholders to follow the speeches of the Chairman of the Supervisory Board as well as of the members of the Management Board and enables shareholders to be represented by proxies designated by the Company when exercising their voting rights.

The reports, documents and information required by law for the shareholders’ meeting, including the annual report as well as the agenda for the shareholders’ meeting and any countermotions or election proposals from shareholders, which have to be made accessible, are available on the internet.

The first shareholders’ meeting after the IPO of HENSOLDT AG will take place on May 18, 2021. Due to the ongoing COVID-19 pandemic and the resulting uncertainty with regard to holding a meeting in person, the shareholders’ meeting will be held as a virtual meeting without the physical presence of shareholders or their representatives in order to protect employees and shareholders in accordance with applicable legal requirements.

3.8. Management Board and Supervisory Board Shareholdings

Pursuant to article 19 of Regulation (EU) No. 596/2014 on market abuse, members of the Management Board and the Supervisory Board as well as persons closely associated with them are legally obliged under certain circumstances to disclose transactions made in shares of HENSOLDT AG or in derivatives relating thereto or in other related financial instruments.

A process is established to properly disclose these transactions in the event of such notification. The reported transactions are available on HENSOLDT's website in the Corporate Governance section.

3.9. Corporate communication and transparency

Corporate Communications provides comprehensive and timely information. All mandatory publications are made available on HENSOLDT's website in the Investor Relations section. Numerous publications, for example ad hoc announcements, press releases and interim and annual reports, are issued in German and English. HENSOLDT organizes press conferences and conference calls on important occasions. The Management Board is responsible for HENSOLDT's communication with shareholders, shareholder associations, financial analysts, the media and the interested public on the Company's development and significant events. In addition, the Chairman of the Supervisory Board participates to an appropriate extent in investor meetings in close consultation with the Management Board, to the extent in which such meetings relate to the work and tasks of the Supervisory Board. The current financial calendar, which provides information on all significant publication and event dates, is also available on the website.

The Company’s statute, the rules of procedure of the Supervisory Board, as well as the report of the Supervisory Board, the Declaration of Conformity, and the Corporate Governance Report, each as of the 2020 fiscal year, are available on our website in the Corporate Governance section. A remuneration report on the last fiscal year pursuant to section 162 AktG and an auditor's report pursuant to section 162 AktG as well as the resolutions of the shareholders’ meeting on the remuneration of the Management Board and Supervisory Board have not yet been prepared or adopted in accordance with the applicable transitional regulations. A remuneration report containing further information on the remuneration system for the Management Board and the Supervisory Board as well as the individualized disclosure of the remuneration of the members of these Boards in the 2020 fiscal year is available under “VI. Remuneration report”. The remuneration resolutions for the Management Board and Supervisory Board will be on the agenda of the first annual shareholders’ meeting on May 18, 2021; the corresponding explanations on the remuneration systems required by law will be included in the notice of the annual shareholders’ meeting. Immediately after the annual shareholders’ meeting, the above-mentioned documents will also be available on the Company's website where they will remain publicly accessible in accordance with statutory requirements.

4. Working methods of Management Board and Supervisory Board

The actions of the Management Board and Supervisory Board of HENSOLDT AG are based on the principle of responsible corporate management and control (corporate governance). The cooperation between the two committees is characterized by mutual trust.

On the basis of section 90 AktG, the Management Board informs the Supervisory Board regularly, promptly, comprehensively and generally in text form about all issues of strategy, planning, business development, risk situation, risk management and compliance that are relevant to the Company. The Management Board discusses the status of strategy implementation with the Supervisory Board at regular intervals and addresses any deviations in the course of business from adopted plans and targets, including an explanation regarding the reasons. The Chairmen of the two boards meet regularly to discuss all relevant current issues, also at short notice and with regard to specific events.

4.1. Management Board of HENSOLDT AG

Working methods of the Management Board

The Management Board manages the Company on its own responsibility. In doing so, it is bound to the interests of the Company and committed to increasing the sustainable value of the Company. The board's main tasks include defining the Company's objectives and strategic direction, managing and monitoring the operating units, and establishing and monitoring an efficient risk management system. The Management Board is responsible for the preparation of the consolidated financial statements and the annual financial statements as well as the preparation of interim financial information of HENSOLDT AG. The Management Board is also responsible for ensuring compliance with legal requirements and official regulations.

The members of the Management Board are jointly responsible for the overall management of the Company and its direct and indirect subsidiaries within the meaning of section 290 HGB ("subsidiaries" and the Company together with its subsidiaries the "HENSOLDT-Group"). They work together as colleagues and inform each other on an ongoing basis about important measures and events within their respective areas of responsibility. Irrespective of the overall responsibility, each member of the Management Board is responsible for managing the area of responsibility assigned to them. As far as measures and transactions of one area of responsibility simultaneously affect another or several other areas of responsibility, the respective member of the Management Board must first reach agreement with the other member(s) involved. If no agreement can be reached, each member of the Management Board involved is obliged to bring about a resolution by the Management Board.

The current Management Board has three functional responsibilities, namely the position of Chief Executive Officer (CEO), Chief Financial Officer (CFO) and Chief Human Resources Officer (CHRO), with the CHRO also serving as Labor Director. The business allocation plan assigns specific business areas to the respective Management Board members; the business allocation plan is reviewed by the Supervisory Board in regular intervals and adjusted as necessary. At present, the CEO's portfolio includes responsibility for the division Radar, IFF & COMMS, the division Spectrum Dominance & Airborne Solutions, the Division Optronics and the Division Customer Services. The CEO is also responsible for Business Development and Sales, as well as Customer Support/Space, Operations/Productions (including R&D), Legal & Compliance, HENSOLDT France, as well as Strategic Programs and Strategy/M&A activities and PMI. The CFO is primarily responsible for the departments Finance & Controlling, Treasury, Investor Relations, Commercial & Offset, Internal Audit, as well as other related programs and tasks (Enterprise Risk Management, Information Management and "HENSOLDT GO!"). In addition to Human Resources, the CHRO is also responsible for Security and Corporate Social Responsibility, Facility Management and Health, Safety and Environment. Within their respective functional areas of responsibility, the members of the Management Board each have – relating to all parts of the Company – the authority to issue directives, the duty of supervision and the duty to coordinate, without prejudice to the continuing overall responsibility of the Management Board. This also applies towards the heads of entities with their own legal form and towards HENSOLDT-Group companies abroad, unless this is not legally permissible in individual cases.

The detailed structure of the work of the Management Board is determined by the rules of procedure, which is issued by the Supervisory Board; the Supervisory Board review the rules of procedure on a regular basis to determine whether any adjustments are required. These rules of procedure govern, among other things, matters reserved for a decision by the whole Management Board, special measures requiring the approval of the Supervisory Board as well as other procedural and resolution modalities. The Management Board meets regularly at Management Board meetings. These are convened by the Chairman of the Management Board, who coordinates the work of the Management Board. Any member of the Management Board may request the convening of a meeting. In accordance with the rules of procedure, the Management Board regularly adopts resolutions by a simple majority of the members participating in the resolution. In the event of a tie, the vote of the Chairman of the Management Board shall be decisive.

Composition of the Management Board

Pursuant to section 6 (1) of the statute, the Management Board of HENSOLDT AG consists of at least two persons. In the reporting period, the Management Board comprised three members: Thomas Müller as Chairman (CEO), Axel Salzmann as CFO and Peter Fieser as CHRO.

Further information on the composition as well as the CVs, term of appointment and areas of responsibility of the individual Management Board members can be found on the Company's website, as is information on other mandates held by members of the Management Board. In addition, the composition of the Management Board is presented in the Notes to the Consolidated Financial Statements.

The members of the Management Board are appointed by the Supervisory Board on the proposal of the Executive Committee. In any appointment decisions, the Supervisory Board takes into account diversity aspects such as age, gender, educational or professional background. In particular, the Supervisory Board aims to give appropriate consideration to women. The flexible age limit for members of the Management Board stipulates that members of the Management Board should generally not be older than 65. The flexible age limit is formulated in a soft way in order to retain a certain degree of flexibility to the Supervisory Board in its appointment decisions.

The current members of the Management Board were already part of the management of the HENSOLDT-Group prior to the IPO. It was intended not to make any changes to the proven composition of the management team in the context of the IPO. Therefore, both Thomas Müller and Axel Salzmann will be 66 years old at the currently scheduled end of their respective terms of appointment at September 20, 2024, which leads to a deviation from the standard age limit set for the Management Board. In future appointment decisions including the event of a possible expansion of the Management Board, the Supervisory Board will take the diversity aspects mentioned above into account in its decision-making and, will in consideration of the professional competencies of the candidates, strive for the most diverse possible composition of the Management Board.

For further information on the representation of women in the Boards, please refer to the chapter "4.4 Disclosure on the representation of women on the Management Board and Supervisory Board and at the top management levels of HENSOLDT AG".

As part of the succession planning for the Management Board, the Chairman of the Supervisory Board, who is also the Chairman of the Executive Committee, regularly discusses suitable internal candidates with the Management Board. In addition, the Executive Committee will also evaluate external candidates for Management Board positions as required and, if necessary, will seek the help of external service providers.

Management Board remuneration

Information on the remuneration and the remuneration system for the Management Board in the past fiscal year can be found in the chapter "VI. Remuneration report".

4.2. Supervisory Board of HENSOLDT AG

Working methods of the Supervisory Board

The Supervisory Board monitors and advises the Management Board in the management of the Company. It supports the Management Board in major business decisions and assists in matters of strategic importance. Measures requiring the approval of the Supervisory Board have been defined by the Supervisory Board in the rules of procedure for the Management Board. Furthermore, the Supervisory Board appoints the members of the Management Board, determines their total remuneration and reviews the consolidated and annual financial statements of HENSOLDT AG, the combined management report including the combined non-financial statement and the report of the Management Board on relations with affiliated companies (dependency report).

At least two Supervisory Board meetings are held each calendar half-year. Extraordinary meetings are held as required. The committees also hold regular meetings. The resolutions of the Supervisory Board require a majority of the votes cast, unless otherwise stipulated by law. If a vote results in a tie, each member of the Supervisory Board has the right to demand a new vote on the same matter. If this also results in a tie, the Chairman has two votes. In the past fiscal year, no issues were discussed which would have required a meeting of the Supervisory Board without the presence of the Management Board. However, insofar as the Executive Committee meets in the future or the Supervisory Board as a whole discusses in particular issues of personnel planning and remuneration and its self-assessment, it is planned to meet without the presence of the Management Board if necessary. The Supervisory Board has adopted rules of procedure for itself, which are published on the Company's website.

HENSOLDT considers the regularly review of the effectiveness of the Supervisory Board's work in accordance with recommendation D.13 of the Code as an important component of good corporate governance. In order to be able to cover a complete year of the activities of the supervisory board of a listed company for the corresponding self-evaluation, a self-evaluation shall be carried out for the first time in November 2021 or at the first meeting in 2022.

In principle, members of the Supervisory Board take responsibility for the training and continuing education measures required for their duties. If necessary, they are supported by the Company to an appropriate extent. To support the Supervisory Board in the induction of any new members, an induction process has been established in which the members of the Supervisory Board are familiarized with the main characteristics of HENSOLDT and its business activities as well as the legal requirements and internal processes relevant to their work on the Supervisory Board.

Details of the Supervisory Board's activities, including the number of meetings and information on the attendance of Supervisory Board members at meetings in the 2020 fiscal year, are provided within the “Report of the Supervisory Board”.

Composition of the Supervisory Board

The Supervisory Board has 12 members and, in accordance with the requirements of the German Codetermination Act (MitbestG), is composed of an equal number of shareholder and employee representatives. The rules of procedure of the Supervisory Board stipulate that the Supervisory Board shall be composed in such a way that its members as a whole possess the knowledge, skills and professional experience required to properly perform their duties and that the statutory gender quota is complied with.

In the fiscal year 2020, the Supervisory Board comprised the following members:

Johannes P. Huth Chairman of Supervisory Board Partner at KKR and Head of KKR EMEA	Member of the Supervisory Board since:	2017

Born 1960	Appointed until: 2025 **Memberships in other statutory supervisory boards in Germany** • Member of the Supervisory Board at HENSOLDT Holding GmbH* until third quarter of 2020 • Member of the Supervisory Board of Axel Springer SE **Memberships in other comparable domestic and foreign control bodies of commercial enterprises** • Member of the Board of Coty Inc. Based on the assessment of the Supervisory Board, the Supervisory Board member is independent of the Company and its Management Board.
Armin Maier-Junker Vice Chairman of Supervisory Board Chairman of the Works Council of HENSOLDT Sensors GmbH at the site in Ulm; Chairman of the Central Works Council of HENSOLDT Sensors GmbH and Chairman of the Groups Works Council Born 1962	Member of the Supervisory Board since: 2017 Appointed by the court until completion of the employee elections, which is expected in 2021 **Memberships in other statutory supervisory boards in Germany** • Member of the Supervisory Board of HENSOLDT Holding GmbH* until third quarter of 2020 • Member of the Supervisory Board of HENSOLDT Sensors GmbH* **Memberships in other comparable domestic and foreign control bodies of commercial enterprises** • None Employee representative
Jürgen Bühl Head of the Industry Policy Coordination department in the Management Board of IG Metall Born 1969	Member of the Supervisory Board since: 2017 Appointed by the court until completion of the employee elections, which is expected in 2021 **Memberships in other statutory supervisory boards in Germany** • Member of the Supervisory Board of HENSOLDT Sensors GmbH* from March 1, 2020 • Member of the Supervisory Board of HENSOLDT Holding GmbH* until third quarter of 2020 **Memberships in other comparable domestic and foreign control bodies of commercial enterprises** • None Employee representative

Dr. Frank Döngi Head of product line Airborne, Space & ISR Radars and of product line Eurofighter Radar of HENSOLDT Sensors GmbH; Born 1966	Member of the Supervisory Board since: 2020 Appointed by the court until completion of the employee elections, which is expected in 2021 **Memberships in other statutory supervisory boards in Germany** • Member of the Supervisory Board of HENSOLDT Holding GmbH* until third quarter of 2020 • Member of the Supervisory Board of HENSOLDT Sensors GmbH* from February 15, 2020 **Memberships in other comparable domestic and foreign control bodies of commercial enterprises** • None Employee representative
Winfried Fetzer Chairman of the Works Council of HENSOLDT Optronics GmbH in Oberkochen; Member of the Groups Works Council Born 1959	Member of the Supervisory Board since: 2017 (retired as of December 31, 2020) **Memberships in other statutory supervisory boards in Germany** • Member of the Supervisory Board of HENSOLDT Holding GmbH* until third quarter of 2020 • Member of the Supervisory Board of HENSOLDT Optronics GmbH* **Memberships in other comparable domestic and foreign control bodies of commercial enterprises** • None Employee representative
Prof. Wolfgang Ischinger Chairman of the Foundation Munich Security Conference; Senior Professor for security policy and diplomatic practice at the Hertie School of Governance in Berlin; Honorary professor at the University Tübingen Born 1946	Member of the Supervisory Board since: 2017 Appointed until: 2025 **Memberships in other statutory supervisory boards in Germany** • Member of the Supervisory Board of HENSOLDT Holding GmbH* until third quarter of 2020 **Memberships in other comparable domestic and foreign control bodies of commercial enterprises** • None Based on the assessment of the Supervisory Board, the Supervisory Board member is independent of the Company and its Management Board as well as of the controlling shareholder.

Ingrid Jägering Member of the Management Board, CFO and Labor Director at Leoni AG Born 1966	Member of the Supervisory Board since: 2017 Appointed until: 2025 **Memberships in other statutory supervisory boards in Germany** • Member of the Supervisory Board of HENSOLDT Holding GmbH* until third quarter of 2020 **Memberships in other comparable domestic and foreign control bodies of commercial enterprises** • Independent member of the Board of Directors of SAF Holland S.A. Based on the assessment of the Supervisory Board, the Supervisory Board member is independent of the Company and its Management Board as well as of the controlling shareholder.
Marion Koch Member of the Work Council of HENSOLDT Sensors GmbH at the site in Immenstaad and Member of the Group Work Council; Project Manager in the product line Airborne, Space & ISR Radars of HENSOLDT Sensors GmbH Born 1978	Member of the Supervisory Board since: 2020 Appointed by the court until completion of the employee elections, which is expected in 2021 **Memberships in other statutory supervisory boards in Germany** • None **Memberships in other comparable domestic and foreign control bodies of commercial enterprises** • None Employee representative
Christian Ollig Partner at KKR and Head of KKR in Germany, Executive Director of Traviata B.V. Born 1977	Member of the Supervisory Board since: 2017 Appointed until: 2025 **Memberships in other statutory supervisory boards in Germany** • Member of the Supervisory Board of HENSOLDT Holding GmbH* until third quarter of 2020 • Member of the Supervisory Board of ETL AG Steuerberatungsgesellschaft • Member of the Supervisory Board at Wella AG **Memberships in other comparable domestic and foreign control bodies of commercial enterprises** • Member of the Supervisory Board of Upfield Holdings B.V. Based on the assessment of the Supervisory Board, the Supervisory Board member is independent of the Company and its Management Board.

Prof. Dr. Burkhard Schwenker Senior Fellow of Roland Berger; Academic Co-Director of the HHL Center for Scenario-Planning Born 1958	Member of the Supervisory Board since: 2017 Appointed until: 2025 **Memberships in other statutory supervisory boards in Germany** • Member of the Supervisory of HENSOLDT Holding GmbH* until third quarter of 2020 • Member of the Supervisory Board of Hamburger Hafen and Logistik AG • Member of the Supervisory Board of Hamburger Sparkasse AG • Member of the Supervisory Board of Flughafen Hamburg GmbH • Member of the Supervisory Board of M.M. Warburg & Co. KGaA **Memberships in other comparable domestic and foreign control bodies of commercial enterprises** • Member of the Board of Directors of HASPA Finanzholding Based on the assessment of the Supervisory Board, the Supervisory Board member is independent of the Company and its Management Board as well as of the controlling shareholder.
Julia Wahl Personal assistant to the district manager of the IG Metall Baden-Württemberg Born 1987	Member of the Supervisory Board since: 2019 Appointed by the court until completion of the employee elections, which is expected in 2021 **Memberships in other statutory supervisory boards in Germany** • Member of the Supervisory Board of HENSOLDT Holding GmbH* until third quarter of 2020 • Member of the Supervisory Board of HENSOLDT Sensors GmbH* from January 15, 2019 **Memberships in other comparable domestic and foreign control bodies of commercial enterprises** • None Employee representative
Claire Wellby Member of the Private-Equity-Team of KKR, Vice President of the KKR Show Aggregator GP Limited Born 1988	Member of the Supervisory Board since: 2020 Appointed until: 2025 **Memberships in other statutory supervisory boards in Germany** • Member of the Supervisory Board of HENSOLDT Holding GmbH* until third quarter of 2020 • Member of the Supervisory Board of LEONINE Licensing AG **Memberships in other comparable domestic and foreign control bodies of commercial enterprises** • None Based on the assessment of the Supervisory Board, the Supervisory Board member is independent of the Company and its Management Board.

The term of appointment mentioned above is calculated on the basis of the first appointment to the Supervisory Board of the HENSOLDT Holding GmbH respectively HENSOLDT GmbH, which means before the change of the legal form of the Company into a public limited company (AG) as of August 17, 2020. Mandates within the HENSOLDT-Group are marked with a star (*). Winfried Fetzer resigned from the Supervisory Board as of December 31, 2020. As his successor, Ingo Zeeh (born 1983), a member of the Works Council of HENSOLDT Optronics GmbH. was appointed to the Supervisory Board by court order on January 15, 2021, for the remaining term of Winfried Fetzer.

In accordance with the rules of procedure, the Supervisory Board shall adopt a competence profile, which takes into account the recommendations of the Code and specifies concrete objectives for its composition. Based on the competence profile prepared by the Supervisory Board and in consideration of the areas of operation of the HENSOLDT Group, the essential competences in particular include, in-depth experience and knowledge in the management of an international company, in the area of digitalization and information technology, in the area of human resources management and recruitment, in accounting and financial reporting, in controlling/ risk management as well as in the area of corporate governance and compliance including the regulatory requirements relevant for HENSOLDT. In addition, the Supervisory Board shall have knowledge and experience in the area of international security policy. Besides the appropriate representation of all gender identities and age groups, proposals for elections to the Supervisory Board will also take into account different educational backgrounds and the most diverse possible cultural and regional origins of the members of the Supervisory Board.

The competence profile also provides rules on the independence of Supervisory Board members and on the limitation of other mandates held in line with the relevant recommendations and suggestions of the Code. A standard length of service of twelve years has been included. This competence profile is to be critically reviewed again after the first self-assessment of the Supervisory Board.

Based on its work up to date, the Supervisory Board has gained the impression that, on an overall basis, the competencies which are considered essential for the board’s work relating HENSOLDT AG and the HENSOLDT Group are represented on the Supervisory Board. The Supervisory Board members as a whole are familiar with the industry in which HENSOLDT operates. On the shareholder side in particular, a significant number of members have many years of international experience in the management of an internationally operating company, Corporate Governance and Compliance, and Human Resources issues. With the Chairwoman of the Audit Committee, Ingrid Jägering, at least one member of the Supervisory Board has proven expertise in the fields of accounting or auditing. In addition, the Chairman of the Supervisory Board as well as Mr. Ollig and Ms. Wellby have in-depth knowledge in this area. Several members have experience in implementing digital processes. Mr. Prof. Ischinger supports the Supervisory Board, in particular, with his in-depth knowledge of the international security policy. Mr. Prof. Dr. Schwenker also contributes considerable experience in the area of committee work and thus also governance. In addition, from the Supervisory Board's point of view, the employee side in particular ensures that the interests of numerous stakeholders are adequately taken into account within the work of the Supervisory Board.

The rules of procedure of the Supervisory Board contain a flexible provision on age limits. Accordingly, only persons who are not older than 70 should be proposed for election. This standard age limit is currently exceeded by only one Supervisory Board member, namely Mr. Prof. Ischinger, whose experience, skills and network are of considerable value to the Company. In this case, exceeding the standard age limit when proposing the election was and continues to be irrelevant from the Supervisory Board's point of view.

For further information on the representation of women in the Boards, please refer to the chapter ”4.4 Disclosure on the representation of women on the Management Board and Supervisory Board and at the top management levels of HENSOLDT AG”.

In future proposals to the shareholders’ meeting for the election of shareholder representatives, the Supervisory Board will take into account its competence profile and the objectives for the composition of the Supervisory Board, which are included in this profile, as well as diversity aspects. In addition, the Supervisory Board will take the time commitment of the proposed persons into account when making proposals to the shareholders' meeting for the election of shareholder representatives.

Prevention of conflicts of interest and independence

Each member of the Supervisory Board must disclose conflicts of interest to the Supervisory Board. Information about conflicts of interest that arose in the past fiscal year and their handling is provided in the "Report of the Supervisory Board".

The Supervisory Board assessed by taking into account the ownership structure of HENSOLDT AG, that an appropriate number of shareholder representatives are independent by definition of the Code. On the shareholder representative's side, the Supervisory Board considers Ingrid Jägering, Prof. Ischinger and Prof. Dr. Burkhard Schwenker to be independent of the Company, its Management Board and of the controlling shareholder, thus three of the total of six shareholder representatives. Consequently recommendation C.9 (1) of the Code is complied with.

The right of the Federal Republic of Germany to appoint a member of the Supervisory Board, as provided for in section 8 (2) of the statute, has not yet been exercised. Moreover, this does not generally affect the independence of a Supervisory Board member, according to the assessment of the Supervisory Board. On the one hand, the statute stipulates that such a Supervisory Board member may not be a civil servant or employee of the Federal Republic of Germany, another regional authority or an institution under public law. On the other hand, in the opinion of the Supervisory Board, the Federal Republic of Germany is not a controlling shareholder in line with the meaning of recommendation C.9 of the Code, as no control agreement has been concluded with the Federal Republic of Germany, nor does the Federal Republic of Germany hold an absolute majority of votes or any other sustainable majority at the shareholders' meeting.

With regard to recommendation C.9 of the Code, the Supervisory Board does not classify Johannes P. Huth, Christian Ollig and Claire Wellby as independent of the controlling shareholder, because of their status as partner or employees of Kohlberg Kravis Roberts & Co L.P. ("KKR") or companies affiliated with KKR. The Supervisory Board nevertheless assumes that the aforementioned Supervisory Board members are independent of the Management Board and the Company, recommendation C.7 of the Code. In this respect, the Supervisory Board assumes that the existing business relationships between the HENSOLDT-Group on the one hand and companies affiliated with KKR on the other hand were not material for either of the business partners in the past fiscal year.

Supervisory Board remuneration

Information about the remuneration system for the Supervisory Board and on the remuneration of the Supervisory Board in the past fiscal year can be found in chapter "VI. Remuneration report".

4.3. Committees of the Supervisory Board

To the extent permitted by law, the Supervisory Board may transfer some of its duties and rights to one of its committees. In particular, the Supervisory Board reserves the right, if necessary, to form a committee for confidentiality matters to deal with classified information. The committees are each responsible for the tasks assigned to them by resolution of the Supervisory Board or by the rules of procedure adopted by the Supervisory Board, which define these tasks in more detail. The Chairpersons of the committees shall report regularly to the Supervisory Board on the activities of the committees. The responsibilities of the Supervisory Board committees are set out in the rules of procedure for the Supervisory Board. The rules of procedure of the committees essentially correspond to those of the Supervisory Board in a plenary session.

In the reporting year, the Supervisory Board formed six permanent and one temporary committee. More details on the work of the committees in the reporting period, including the number of respective meetings and information on the attendance of committee members at meetings, can be found in the "Report of the Supervisory Board".

Executive Committee

The Executive Committee is composed of the Chairman of the Supervisory Board, his deputy and one further member from both the employee and shareholder sides. In the reporting period, Johannes P. Huth (chairman), Jürgen Bühl[16], Prof. Wolfgang Ischinger and Armin Maier-Junker[16] were members of the committee. The Executive Committee prepares proposals to the Supervisory Board for the appointment and dismissal of Management Board members and the extension of their mandates, the handling of service contracts with Management Board members, Management Board succession planning, and corporate governance issues. The Executive Committee is responsible for concluding, amending, extending and terminating service contracts with the members of the Management Board within the framework of the remuneration system determined by the Supervisory Board in a plenary session and the shareholders' meeting and within the targets set by the Supervisory Board in a plenary session for the variable remuneration of the individual Management Board members. In addition, the Executive Committee makes proposals to the Supervisory Board for resolutions on existing or anticipated conflicts of interest of members of the Management Board. Furthermore, the Executive Committee makes proposals for the approval of other contracts and transactions between the Company or a subsidiary of the Company on the one hand and a member of the Management Board or persons or companies related to a member of the Management Board on the other hand, unless the Committee for Related Party Transactions is responsible.

Audit Committee

The Audit Committee is composed of two shareholder representatives and two employee representatives. In the reporting period Ingrid Jägering (Chairwoman), Marion Koch[16], Christian Ollig and Julia Wahl[16] belonged to the committee. The Chairwoman of the Audit Committee, Ingrid Jägering, is independent in the assessment of the Supervisory Board. She has not been a member of the Management Board of HENSOLDT AG in the past, nor does she have any other personal or business relationship with HENSOLDT AG or its institutions, which could constitute a material and not only temporary conflict of interest. She is not simultaneously Chairwoman of the Supervisory Board and has expertise in the fields of accounting and auditing.

The Audit Committee is tasked with reviewing the financial statements and with monitoring the accounting process. In connection with the adoption of the annual financial statements by the Supervisory Board, the Audit Committee undertakes the preliminary review of the annual and consolidated financial statements, the combined management report of HENSOLDT AG and the Group, the sustainability report, the report of the Management Board on relations with affiliated companies (dependency report) and the proposal of the Management Board for the appropriation of balance sheet profit. In addition, the Audit Committee discusses significant changes in audit and accounting methods. The Audit Committee prepares the report of the Supervisory Board to the shareholders' meeting in accordance with section 171 (2) AktG.

The Audit Committee also reviews the effectiveness of the internal control system, the risk management system and the internal auditing system. For this purpose, the Committee discusses the principles of risk identification and risk management with the Management Board and deals with the Company's risk monitoring system. The Audit Committee monitors the Company's compliance with legal provisions, official regulations and the Company's internal policies, where these do not relate to transactions and regulations concerning anti-corruption, antitrust (competition law), data protection and export control, which are duties of the Compliance Committee of the Supervisory Board.

[16] Employee representative

The Audit Committee prepares the resolution proposal to the shareholders' meeting regarding the election of the auditor for the annual financial statements and the consolidated financial statements as well as any quarterly and half-yearly reports. The Audit Committee monitors the selection and the independence of the auditor. It also oversees the work of the auditor, including the additional services provided by the auditor.

Conciliation Committee

The Conciliation Committee consists of the chairman of the Supervisory Board as chairman of the committee, his deputy elected in accordance with the German Codetermination Act, and one additional representative for each shareholders and employees. In the reporting period Johannes P. Huth (Chairman), Jürgen Bühl[16], Armin Maier-Junker[Fehler! Textmarke nicht definiert.16] and Christian Ollig were members of the Committee. In the cases set out in section 31 (3) and (5) MitbestG, the Conciliation Committee shall submit proposals to the Supervisory Board for the appointment or withdrawal of the appointment of members of the Management Board.

Compliance Committee

The Compliance Committee is composed of two shareholder representatives and two employee representatives. In the reporting period, Prof. Dr. Burkhard Schwenker (chairman), Dr. Frank Doengi[16], Winfried Fetzer[16] and Christian Ollig were members of the Committee. The Compliance Committee's task is to monitor the Company's compliance with legal provisions, official regulations and internal Company policies relating to anti-corruption, antitrust (competition law), data protection and export control.

Related Party Transactions Committee

The Related Party Transactions Committee shall be composed of two shareholder representatives and two employee representatives, taking into account that the majority of the Committee shall be composed of members for which no concern of a conflict of interest exists due to their relationship with a related party. In the reporting period, Prof. Dr. Burkhard Schwenker (Chairman), Jürgen Bühl[16], Prof. Wolfgang Ischinger and Armin Maier-Junker[16] were members of the Committee. Task of the Related Party Transactions Committee is to monitor the Company's internal procedure for the ordinary course of business and the arm's length nature of related party transactions within the meaning of section 111a (1) AktG. Furthermore, the Committee is responsible for the approval of related party transactions in accordance with section 111b AktG. For such transactions, the decision-making authority of the committee takes precedence over the decision-making authority of other committees.

Nomination Committee

The Nomination Committee consists of up to four Supervisory Board members from the shareholder's side. In the reporting period, Johannes P. Huth (Chairman), Prof. Wolfgang Ischinger, Ingrid Jägering and Christian Ollig were members of the Committee. When appointing members to this committee, the Supervisory Board ensures an appropriate representation of women and men. The Nomination Committee proposes suitable candidates to the Supervisory Board for its election proposal to the shareholders' meeting. The Nomination Committee is also responsible for preparing a proposal for the competency profile, reviewing the existing competency profile, and recommending any adjustments.

IPO Committee

In the last fiscal year the Supervisory Board also formed a temporary IPO Committee from August 11, 2020, until October 31, 2020. Johannes P. Huth (Chairman), Jürgen Bühl[16], Armin Maier-Junker[16] and Christian Ollig were members of the Committee. The IPO Committee performed the duties and authorities of the Supervisory Board with regard to the preparation and implementation of the IPO. This in particular concerned tasks regarding the further implementation of the prospectus approval procedure and the preparation of the admission of the shares of HENSOLDT AG for trading as well as to the capital increase planned in this context and the agreements to be concluded with the accompanying issuing banks, as well as the Square Lux Holding II S.à r.l.

4.4. Disclosures on the representation of women in the Management Board and Supervisory Board and at the top management levels of HENSOLDT AG

Disclosures on the achievement of the legally required minimum quota for the Supervisory Board pursuant to section 96 (2) Sentence 1 AktG

The legally required gender quota of 30.0 % in accordance with section 96 (2) AktG applies to the Supervisory Board. To prevent possible unequal treatment of shareholder or employee representatives and to increase planning security in the respective election processes, the shareholder representatives on the Supervisory Board have objected to the overall fulfillment of the quota in accordance with section 96 (2) sentence 2 AktG. This means the shareholder side and the employee side must meet the minimum quota of 30.0 % for each gender separately. The shareholder and employee sides must therefore each include at least two women and at least two men.

In the reporting period, there were two women each on both the shareholder and employee sides. The legally required gender quota was therefore complied with in the past fiscal year.

Determination in accordance with § 111 (5) AktG

The Supervisory Board of HENSOLDT AG has set a target for the proportion of women on the Management Board in accordance with section 111 (5) AktG. When the target was first set, a minimum target of 25.0 % was set until the end of the first implementation period on August 11, 2025. The proportion of women on the Management Board was zero percent at the time the target was set for the first time.

Determination for the two management levels below the Management Board

In accordance with section 76 (4) AktG, the Management Board also sets targets for the proportion of women in the two management levels below the Management Board. As of the reporting date of December 31, 2020, HENSOLDT AG, as an individual entity, did not have any management levels below the Management Board. The determination of a target proportion has therefore not yet been made.

Even independently of setting targets for the proportion of women, the Management Board pays attention to diversity when filling management positions within the HENSOLDT Group, particularly with regard to the appropriate representation of all gender identities as well as the international experience and origin of employees.

IX. Final declaration on the dependency report

In the fiscal year 2020, HENSOLDT AG was a dependent Company of KKR Square Aggregator L.P., Canada and its subsidiaries within the meaning of section 312 AktG. The Management Board of HENSOLDT AG therefore prepared a dependency report according to section 312 (1) AktG, which contains the following final declaration:

“We declare that HENSOLDT AG, with regard to the legal transactions and measures listed in the report on relations with affiliated companies, according to the circumstances known to us at the time the legal transactions were carried out or the measures were taken or omitted, received appropriate consideration for each legal transaction and was not disadvantaged by the fact the measures were taken or omitted.”

X. HENSOLDT AG

The annual financial statements of HENSOLDT AG were prepared in accordance with the German Commercial Code (HGB) and the German Stock Corporation Act (AktG).

As of December 31, 2020, HENSOLDT AG was the parent Company of the HENSOLDT Group. With the entry in the commercial register on August 17, 2020, HENSOLDT GmbH was converted into HENSOLDT AG. HENSOLDT GmbH, Taufkirchen, District of Munich (until November 11, 2019: Blitz 19-320 GmbH, Munich) was founded with corporation agreement dated September 17, 2019 and was registered into the commercial register under file no. HRB 252143 at the Munich Local Court on October 16, 2019.

1. Financial Performance HENSOLDT AG

For the fiscal year 2020, the income statement for HENSOLDT AG was as follows. In the comparative column for 2019, figures shown are for the stub fiscal year of HENSOLDT GmbH from October 16 to December 31, 2019.

	Fiscal year		
in € million	2020	2019	% Change
Revenue	8.3	-	
Cost of sales	-8.5	-	
Gross profit	**-0.2**	**-**	
General administrative expenses	-33.6	-0.3	>-200%
Other operating income	5.3	-	
Other operating expenses	-6.0	-	
Operating result	**-34.5**	**-0.3**	**>-200%**
Financial result	-8.4	-	
Loss after taxes	**-42.9**	**-0.3**	**>-200%**
Loss carryforw ard	-0.3	-	
Withdraw al from the capital reserve	60.0	-	
Balance sheet profit / loss	**16.8**	**-0.3**	**>200%**

Revenue consists exclusively of internal onwards charging. The administrative expenses mainly include consulting fees in relation to the IPO and the refinancing as well as personnel costs. Other operating expenses mainly include costs for raising equity. Other operating income include onwards charging in relation to the IPO. The financial result consists predominantly of interest paid for the syndicated loan, bank commissions and fees as well as the interest expense from the revaluation of the pension provisions. The balance sheet profit resulted from the withdrawal from the capital reserve in the context of the preparation of the annual financial statements. As of December 31, 2020, HENSOLDT AG had five employees.

2. Asset and financial position HENSOLDT AG

The assets and financial positions of HENSOLDT AG on December 31, 2020, were as follows:

in € million	Dec. 31, 2020	Dec. 31, 2019	% Change
Property, plant and equipment	0.1	-	
Financial assets	2,670.0	1,650.0	61.8%
Fixed assets	**2,670.1**	**1,650.0**	**61.8%**
Receivables and other assets	125.9	-	
Cash and cash equivalents	188.0	0.0	>200%
Current assets	**313.9**	**0.0**	**>200%**
Prepaid expenses	9.1	-	
Total assets	**2,993.1**	**1,650.0**	**81.4%**
Share capital	105.0	10.0	>200%
Capital reserve	1,785.0	1,640.0	8.8%
Balance sheet profit / loss	16.8	-0.3	>200%
Equity	**1,906.8**	**1,649.7**	**15.6%**
Provisions	7.3	0.3	>200%
Liabilities	1,078.9	0.0	>200%
Total equity and liabilities	**2,993.1**	**1,650.0**	**81.4%**

The increase in financial assets resulted from a contribution into the capital reserve of HENSOLDT Holding GmbH, which in turn paid a contribution into the capital reserve of HENSOLDT Holding Germany GmbH in order to redeem the outstanding liabilities under the existing financing agreement. The receivables and other assets are mainly made up of receivables from cash pooling in the amount of €103.7 million as well as receivables from advance VAT declarations of tax group subsidiaries in the amount of €20.4 million. The improvement of cash and cash equivalents resulted mainly from the cash inflows from refinancing and the proceeds of the IPO and was partially reduced by the contribution to the capital reserve of HENSOLDT Holding GmbH. Prepaid expenses included the capitalized discounts in connection with the taking up of the loan.

As of December 31, 2020, the share capital of HENSOLDT AG amounted to €105.0 million, divided into 105.0 million ordinary bearer shares (no-par value shares). With the entry in the commercial register on August 17, 2020, HENSOLDT GmbH was converted into HENSOLDT AG. Prior to the conversion, the share capital of the Company was increased from €10.0 million by €70.0 million to €80.0 million from the Company's capital reserves by resolution of the shareholders on August 4, 2020 and entry in the commercial register on August 6, 2020 (capital increase from company funds).

At the time of conversion of HENSOLDT GmbH into HENSOLDT AG, the share capital of HENSOLDT GmbH amounted to €80.0 million. In the course of the IPO, the share capital of the Company was increased by an additional €25.0 million to €105.0 million based on the resolution of the shareholders' meeting on September 3, 2020 and with entry in the commercial register on September 24, 2020.

The exceeding amount of €275.0 million from the issuance of the 25.0 million new shares was allocated to the capital reserve. On September 24, 2020, all of the 105.0 million shares of HENSOLDT AG were admitted to trading on the Frankfurt Stock Exchange with admission to the sub-segment of the regulated market with additional post-admission obligations (Prime Standard), and trading commenced on the following day.

The previous year's figures relate to the share capital of HENSOLDT GmbH. HENSOLDT GmbH's share capital was fully paid in and amounted to €10.0 million as of December 31, 2019.

Loss after taxes for the fiscal year as of December 31, 2020 amounted to €42.9 million. In connection with the preparation of the annual financial statements, an amount of €60.0 million was withdrawn from the capital reserve and allocated to balance sheet profit.

The provisions referred predominantly to provisions for pensions obligations and provisions for personnel expenses. The liabilities mainly comprised liabilities to banks from the new syndicated loan consisting of a loan in the nominal amount of €600.0 million and a revolving credit facility amounting to €350.0 million, which was drawn in full on reporting date. Liabilities also included payables to affiliated companies in the amount of €100.4 million, mainly from cash pooling.

3. Opportunities and risks

The business development of HENSOLDT AG is subject to the same opportunities and risks as the HENSOLDT Group because of its role as a holding company. The most significant risks for the Company are the worsening of operative performances of subsidiaries and the associated impairment risk in the carrying amount of investments as well as liquidity and interest risks. HENSOLDT AG is not aware of an individual or aggregated risk, which could endanger the continuity of its business activity. The most meaningful opportunities for HENSOLDT AG result from the current increase of defense budgets. The diversification of the product range and the extension of the service business as well as the ability of the HENSOLDT Group and thus the Group companies to act as the innovation leader in their industry present further opportunities.

4. Forecast

Within the Company's operational planning, the Management Board assumes a strong increase in revenue and a moderate reduction of the loss after taxes for the year 2021. Those represent the most significant financial key performance indicators for HENSOLDT AG. The main driver is the anticipated absence of expenses for the IPO, partly offset by higher interest expenses. This expectation does not take into account possible influences of the global COVID-19 pandemic, in particular possible effects of further waves and additional lockdowns. The forecast strongly depends on the development of the HENSOLDT Group and the interest rate level.

1 Reproduction of the Auditor’s Report

Based on the results of our audit, we have issued the following unqualified audit opinion:

Independent Auditor's Report

To HENSOLDT AG, Taufkirchen, District of Munich

Report on the Audit of the Consolidated Financial Statements and the Combined Management Report

Opinions

We have audited the consolidated financial statements of HENSOLDT AG, Taufkirchen, District of Munich and its subsidiaries (the Group), which comprise the consolidated statement of financial position as at December 31, 2020, the consolidated income statement, the consolidated statement of comprehensive income, the consolidated statement of changes in equity and the consolidated statement of cash flows for the financial year from January 1, 2020 to December 31, 2020, and notes to the consolidated financial statements, including a summary of significant accounting policies. In addition, we have audited the combined management report of HENSOLDT AG and the HENSOLDT Group (hereinafter: “combined management report“) for the financial year from January 1 to December 31, 2020.

In accordance with German legal requirements, we have not audited the content of those components of the combined management report specified in the “Other Information” section of our auditor’s report.

In our opinion, on the basis of the knowledge obtained in the audit,

– the accompanying consolidated financial statements comply, in all material respects, with the IFRSs as adopted by the EU, and the additional requirements of German commercial law pursuant to Section 315e (1) HGB [Handelsgesetzbuch: German Commercial Code] and, in compliance with these requirements, give a true and fair view of the assets, liabilities, and financial position of the Group as at December 31, 2020, and of its financial performance for the financial year from January 1, 2020 to December 31, 2020, and

- the accompanying combined management report as a whole provides an appropriate view of the Group's position. In all material respects, this combined management report is consistent with the consolidated financial statements, complies with German legal requirements and appropriately presents the opportunities and risks of future development. Our opinion on the combined management report does not cover the content of those components of the combined management report specified in the "Other Information" section of the auditor's report.

Pursuant to Section 322 (3) sentence 1 HGB, we declare that our audit has not led to any reservations relating to the legal compliance of the consolidated financial statements and of the combined management report.

Basis for the Opinions

We conducted our audit of the consolidated financial statements and of the combined management report in accordance with Section 317 HGB and the EU Audit Regulation No 537/2014 (referred to subsequently as "EU Audit Regulation") and in compliance with German Generally Accepted Standards for Financial Statement Audits promulgated by the Institut der Wirtschaftsprüfer [Institute of Public Auditors in Germany] (IDW). Our responsibilities under those requirements, principles and standards are further described in the "Auditor's Responsibilities for the Audit of the Consolidated Financial Statements and of the Combined Management Report" section of our auditor's report. We are independent of the group entities in accordance with the requirements of European law and German commercial and professional law, and we have fulfilled our other German professional responsibilities in accordance with these requirements. In addition, in accordance with Article 10 (2)(f) of the EU Audit Regulation, we declare that we have not provided non-audit services prohibited under Article 5 (1) of the EU Audit Regulation. We believe that the evidence we have obtained is sufficient and appropriate to provide a basis for our opinions on the consolidated financial statements and on the combined management report.

Key Audit Matters in the Audit of the Consolidated Financial Statements

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the consolidated financial statements for the financial year from January 1, 2020 to December 31, 2020. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, we do not provide a separate opinion on these matters.

Recoverability of goodwill

With regard to the accounting policies applied, please refer to section "I. Basis of preparation (note 3.3. Assets acquired and liabilities assumed as well as goodwill and 3.4. Impairment testing)" in the notes to the consolidated financial statements.

Further information is provided in section "IV. Operating assets and liabilities (note 17.2. Goodwill)" in the notes to the consolidated financial statements.

RISKS FOR THE FINANCIAL STATEMENTS

Goodwill with a carrying amount of EUR 637.2 million as at December 31, 2020 represents a significant proportion (21.6%) of total assets.

Goodwill is tested for impairment annually in the fourth quarter of the financial year at the level of the Sensors and Optronics operating segments, irrespective of any indication of impairment. If an indication of an impairment loss on goodwill arises during the year, this also triggers an impairment test to be performed during the year. For the purposes of impairment testing, the carrying amount of goodwill is compared with the recoverable amount of the relevant operating segment. If the carrying amount is higher than the recoverable amount, an impairment loss is required to be recognized. The recoverable amount is determined as the value in use of the operating segment. The valuation date for the impairment test was September 30, 2020. HENSOLDT engaged the services of an external expert to assist in the performance of the impairment test.

Testing goodwill for impairment is a complex matter and is based on a number of discretionary assumptions. These include the forecast revenue growth, the forecast level of long-term EBITDA margins and the discount rate to be used, given that even minor changes in these assumptions can have a material impact on estimated recoverable amounts.

There is a risk for the financial statements that an impairment loss existing at the end of the reporting period is not identified and therefore not recognized appropriately. Furthermore, there is a risk that the disclosures in the notes to the consolidated financial statements relating to the impairment test are not appropriate.

OUR AUDIT APPROACH

We tested selected internal controls relating to the forecasting process underlying the impairment test.

With the involvement of our own valuation specialists, we assessed, among other things, the appropriateness of the key assumptions and the Company's calculation methodology and discussed these with the external expert. In parallel, we discussed the expected development of business performance and earnings and assumed growth rates with the persons responsible for drawing up the forecasts. We also performed reconciliations with the budget prepared by the management board and approved by the supervisory board.

We also assured ourselves of the quality of the Company's forecasting procedures to date by comparing previous financial years' forecasts with actual outcomes and by analyzing variances arising. We considered the appropriateness of the assumptions and data used to determine the discount rate (in particular the risk-free interest rate), the market risk premium and the beta factor, by comparing them with our own assumptions and with publicly available data.

In order to take account of forecasting uncertainties and the early valuation date selected for the impairment test, we examined the effects of possible changes in the above-mentioned assumptions on the recoverable amount by calculating alternative scenarios and comparing them with the Company's values (sensitivity analysis).

Finally, we assessed whether the disclosures on the recoverability of goodwill in the notes to the consolidated financial statements are appropriate.

OUR CONCLUSIONS

The Company's assumptions and data underlying the impairment test are appropriate. The disclosures in the notes to the consolidated financial statements relating to impairment testing are appropriate.

Measurement of pension provisions

With regard to the accounting policies applied, please refer to section “I. Basis of preparation (notes 2.8. Employees Benefits and 3.6. Employees Benefits)” in the notes to the consolidated financial statements.

Further information is provided in section “IV. Operating assets and liabilities (note 32. Pension benefits)” in the notes to the consolidated financial statements.

RISKS FOR THE FINANCIAL STATEMENTS

Provisions for retirement benefits amounting to EUR 429.8 million are recognized in the consolidated financial statements as at December 31, 2020, representing the net liability arising by setting off the defined benefit obligation (DBO) relating to pension plans (EUR 488.3 million) and deferred compensation (EUR 167.1 million) against the fair value of plan assets amounting to EUR 211.8 million and EUR 13.9 million respectively. The present value of obligations under these defined benefit plans is measured using the projected unit credit method, the outcome of which depends significantly on the judgment applied when determining various assumptions such as the discount factor, the future salary trend, life expectancy and the exercise of options relating to the disbursement of pensions. The measurement of retirement benefit obligations was based on actuarial reports commissioned by HENSOLDT.

A significant proportion of plan assets relates to an investment in HENSOLDT Real Estate GmbH & Co. KG, which primarily holds investments in real estate. The determination of the fair values of these assets depends on the judgment applied when determining various assumptions such as the amount of future rental income to be generated and the discount factor. HENSOLDT engaged the services of an external expert to assist in determining the fair values of the main properties.

There is a risk for the financial statements that inappropriate assumptions are used both in the measurement of the retirement benefit obligations and of the plan assets, which could result in the provision for retirement benefits being measured at an incorrect amount.

Furthermore, there is a risk that the disclosures in the notes to the consolidated financial statements relating to the measuring of the provision for the provision for retirement benefits are not appropriate.

OUR AUDIT APPROACH

Within the scope of our audit, we evaluated amongst other things the actuarial reports obtained as well as the professional qualifications of the external expert. We were assisted in this evaluation by our own internal actuarial specialists. We tested the appropriateness of the actuarial assumptions and valuation methodology applied. Based on this, we traced the amounts recognized in the consolidated financial statements as well as disclosures in the notes, based on the relevant actuarial reports.

For the purposes of auditing the fair values of plan assets, we assessed the valuation of the main properties as well as the professional qualifications of the external expert. In light of the specific features of real estate valuation, we were assisted in this matter by own internal real estate specialists. We tested the appropriateness of the valuation methodology and of the underlying parameters and premises applied. Based on this, we agreed the amounts recognized in the consolidated financial statements and the disclosures made in the notes to the consolidated financial statements.

OUR CONCLUSIONS

The assumptions used by the Group to measure its retirement benefit obligations and plan assets are, in each case, considered appropriate overall. The notes to the consolidated financial statements contain the necessary information on assumptions underlying the valuation.

Revenue recognition in the project business of the Sensors operating segment

With regard to the accounting policies applied, please refer to section "I. Basis of preparation (note 2.3. Revenue from contracts with customers and 3.1. Revenue recognition over time)" in the notes to the consolidated financial statements.

Further information is provided in section "III. Group performance (note 11. Revenue and cost of sales)" in the notes to the consolidated financial statements.

RISKS FOR THE FINANCIAL STATEMENTS

Group revenue totaled EUR 1,206.9 million in the financial year 2020. The Sensors operating segment accounted for EUR 922.5 million of this amount, including EUR 480.5 million recognized on the basis of a point in time and EUR 442.7 million recognized over time.

Customer contracts in the project business of the Sensors operating segment are predominantly complex, in some cases involving high order volumes and long terms. Customer-specific requirements often means that there is no alternative use for project business output. HENSOLDT has established detailed guidelines, procedures and processes for accounting for revenue from contracts with customers. Application of the guidelines requires considerable judgment, particularly in identifying performance obligations, estimating total costs, determining the time of fulfilment of performance obligations and determining costs incurred up to the reporting date and hence the progress of performance in the case of revenue recognized over time.

Due to the complexity of contracts with customer and the judgement required when assessing the criteria for determining the point in time at which a customer obtains control, there is a risk for the financial statements that revenue is recognized in the wrong period.

OUR AUDIT APPROACH

Based on the understanding of processes gained during our audit, we assessed the design, structure and effectiveness of identified internal controls, in particular with regard to the correct determination of costs incurred, expected total costs, the method used for measuring the progress of contracts and the procedures applied by project controlling for recognizing revenue.

For new contracts entered into during the year under report, we analyzed contracts and assessed whether the criteria applied for recognizing revenue at a point in time or over time were met. For this purpose, we assessed the appropriate application of the accounting guidelines for a sample of contracts selected on a risk-oriented basis.

We checked the methodology used to determine actual costs incurred in relation to the various types of cost included as well as the use of the applicable hourly rates.

On the basis of projects selected by us using a risk-oriented approach, we also examined the process for determining expected total costs in relation to the various types of cost and risk included and for updating forecasts of expected total costs on the occurrence of triggering events. In this context, we discussed the estimation of total expected costs for the selected projects with the relevant project managers from both the commercial and the technical side. The total amount of revenue underlying the selected projects was agreed to the relevant contracts.

We also checked the computation of the progress of the contracts concerned. In a final step, we assessed whether the timing of revenue recognition was consistent with the progress of the project or with the transfer of control.

OUR CONCLUSIONS

The approach used by the HENSOLDT Group to recognize project business revenue relating to the Sensors operating segment is appropriate. The assumptions underlying the accounting treatment are appropriate.

Other Information

The management board and the supervisory board are responsible for the other information. The other information comprises the following components of the combined management report, whose content was not audited:

– the non-financial Group declaration to which reference is made in the combined management report, and

– the corporate governance statement included in section VIII. of the combined management report.

The other information also includes the remaining parts of the annual report.

The other information does not include the consolidated financial statements, the combined management report information audited for content and our auditor’s report thereon.

Our opinions on the consolidated financial statements and on the combined management report do not cover the other information, and consequently we do not express an opinion or any other form of assurance conclusion thereon.

In connection with our audit, our responsibility is to read the other information and, in so doing, to consider whether the other information

– is materially inconsistent with the consolidated financial statements, with the combined management report information audited for content or our knowledge obtained in the audit, or

– otherwise appears to be materially misstated.

Responsibilities of the Management Board and the Supervisory Board for the Consolidated Financial Statements and the Combined Management Report

The management board is responsible for the preparation of consolidated financial statements that comply, in all material respects, with IFRSs as adopted by the EU and the additional requirements of German commercial law pursuant to Section 315e (1) HGB and that the consolidated financial statements, in compliance with these requirements, give a true and fair view of the assets, liabilities, financial position, and financial performance of the Group. In addition, the management board is responsible for such internal control as they have determined necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, the management board is responsible for assessing the Group's ability to continue as a going concern. They also have the responsibility for disclosing, as applicable, matters related to going concern. In addition, they are responsible for financial reporting based on the going concern basis of accounting unless there is an intention to liquidate the Group or to cease operations, or there is no realistic alternative but to do so.

Furthermore, the management board is responsible for the preparation of the combined management report that, as a whole, provides an appropriate view of the Group's position and is, in all material respects, consistent with the consolidated financial statements, complies with German legal requirements, and appropriately presents the opportunities and risks of future development. In addition, the management board is responsible for such arrangements and measures (systems) as they have considered necessary to enable the preparation of a combined management report that is in accordance with the applicable German legal requirements, and to be able to provide sufficient appropriate evidence for the assertions in the combined management report.

The supervisory board is responsible for overseeing the Group's financial reporting process for the preparation of the consolidated financial statements and of the combined management report.

Auditor's Responsibilities for the Audit of the Consolidated Financial Statements and of the Combined Management Report

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and whether the combined management report as a whole provides an appropriate view of the Group's position and, in all material respects, is consistent with the consolidated financial statements and the knowledge obtained in the audit, complies with the German legal requirements and appropriately presents the opportunities and risks of future development, as well as to issue an auditor's report that includes our opinions on the consolidated financial statements and on the combined management report.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Section 317 HGB and the EU Audit Regulation and in compliance with the German Generally Accepted Standards for Financial Statement Audits promulgated by the Institut der Wirtschaftsprüfer (IDW) will always detect a material misstatement. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial Statements and the combined management report.

We exercise professional judgement and maintain professional skepticism throughout the assurance engagement. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements and of the combined management report, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinions. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal controls.

- Obtain an understanding of internal control relevant to the audit of the consolidated financial statements and of arrangements and measures (systems) relevant to the audit of the combined management report in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of these systems.
- Evaluate the appropriateness of accounting policies used by the management board and the reasonableness of estimates made by the management board and related disclosures.
- Conclude on the appropriateness of the management board's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in the auditor's report to the related disclosures in the consolidated financial statements and in the combined management report or, if such disclosures are inadequate, to modify our respective opinions. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to be able to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements present the underlying transactions and events in a manner that the consolidated financial statements give a true and fair view of the assets, liabilities, financial position and financial performance of the Group in compliance with IFRSs as adopted by the EU and the additional requirements of German commercial law pursuant to Section 315e (1) HGB.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express opinions on the consolidated financial statements and on the combined management report. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our opinions.
- Evaluate the consistency of the combined management report with the consolidated financial statements, its conformity with German law, and the view of the Group's position it provides.
- Perform audit procedures on the prospective information presented by the management board in the combined management report. On the basis of sufficient appropriate audit evidence we evaluate, in particular, the significant assumptions used by the management board as a basis for the prospective information, and evaluate the proper derivation of the prospective information from these assumptions. We do not express a separate opinion on the prospective information and on the assumptions used as a basis. There is a substantial unavoidable risk that future events will differ materially from the prospective information.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with the relevant independence requirements, and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, the related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the consolidated financial Statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter.

Other Legal and Regulatory Requirements

Assurance Report in accordance with Section 317 (3b) HGB on the Electronic Reproduction of the Consolidated Financial Statements and the Combined Management Report Prepared for Publication Purposes

We have performed an assurance engagement in accordance with Section 317 (3b) HGB to obtain reasonable assurance about whether the electronic reproduction of the consolidated financial statements and the combined management report (hereinafter the "ESEF documents") contained in the file that can be downloaded by the issuer from the electronic client portal with access protection,

hensoldtag-2020-12-31.zip" (SHA256-Hashwert: 9ec430fb528e8236a87
c1f127cc29aabece4c587e4210b2243fac59035c8d624)]

and prepared for publication purposes complies in all material respects with the requirements of Section 328 (1) HGB for the electronic reporting format ("ESEF format"). In accordance with German legal requirements, this assurance engagement only extends to the conversion of the information contained in the consolidated financial statements and the combined management report into the ESEF format and therefore relates neither to the information contained in this reproduction nor any other information contained in the above-mentioned electronic file.

In our opinion, the reproduction of the consolidated financial statements and the combined management report contained in the above-mentioned electronic file and prepared for publication purposes complies in all material respects with the requirements of Section 328 (1) HGB for the electronic reporting format. We do not express any opinion on the information contained in this reproduction nor on any other information contained in the above-mentioned file beyond this reasonable assurance conclusion and our audit opinion on the accompanying consolidated financial statements and the accompanying combined management report for the financial year from January 1 to December 31, 2020 contained in the "Report on the Audit of the Consolidated Financial Statements and of the Combined Management Report" above.

We conducted our assessment of the reproduction of the consolidated financial statements and the combined management report contained in the above-mentioned electronic file in accordance with Section 317 (3b) HGB and the Exposure Draft of the IDW Assurance Standard: Assurance in accordance with Section 317 (3b) HGB on the Electronic Reproduction of Financial Statements and Management Reports Prepared for Publication Purposes (ED IDW AsS 410) and the International Standard on Assurance Engagements 3000 (Revised). Accordingly, our responsibilities are further described below. Our audit firm has applied the IDW Standard on Quality Management 1: Requirements for Quality Management in Audit Firms (IDW QS 1).

The management board is responsible for the preparation of the ESEF documents including the electronic reproduction of the consolidated financial statements and the combined management report in accordance with Section 328 (1) sentence 4 item 1 HGB and for the tagging of the consolidated financial statements in accordance with Section 328 (1) sentence 4 item 2 HGB.

In addition, the management board is responsible for the internal controls they consider necessary to enable the preparation of ESEF documents that are free from material non-compliance with the requirements of Section 328 (1) HGB for the electronic reporting format, whether due to fraud or error.

The management board is also responsible for the submission of the ESEF documents together with the auditor's report and the attached audited consolidated financial statements and audited combined management report as well as other documents to be published to the operator of the German Federal Gazette [Bundesanzeiger].

The supervisory board is responsible for overseeing the preparation of the ESEF documents as part of the financial reporting process.

Our objective is to obtain reasonable assurance about whether the ESEF documents are free from material non-compliance with the requirements of Section 328 (1) HGB, whether due to fraud or error. We exercise professional judgement and maintain professional skepticism throughout the assurance engagement. We also:

– Identify and assess the risks of material non-compliance with the requirements of Section 328 (1) HGB, whether due to fraud or error, design and perform assurance procedures responsive to those risks, and obtain assurance evidence that is sufficient and appropriate to provide a basis for our assurance conclusion.
– Obtain an understanding of internal control relevant to the assessment of the ESEF documents in order to design assurance procedures that are appropriate in the circumstances, but not for the purpose of expressing a conclusion on the effectiveness of these controls.
– Evaluate the technical validity of the ESEF documents, i.e. whether the electronic file containing the ESEF documents meets the requirements of Commission Delegated Regulation (EU) 2019/815 on the technical specification for this electronic file.
– Evaluate whether the ESEF documents enable an XHTML reproduction with content equivalent to the audited consolidated financial statements and the audited combined management report.
– Evaluate whether tagging the ESEF documents with Inline XBRL technology (iXBRL) provides an appropriate and complete machine-readable XBRL copy of the XHTML reproduction.

Further Information pursuant to Article 10 of the EU Audit Regulation

We were elected as group auditor at the annual general meeting on August 11, 2020. We were engaged by the supervisory board on December 2, 2020. We have been the group auditor of HENSOLDT AG (in its capacity as a capital-market-oriented entity) since financial year 2020.

We declare that the opinions expressed in this auditor's report are consistent with the additional report to the audit committee pursuant to Article 11 of the EU Audit Regulation (long-form audit report).

German Public Auditor Responsible for the Engagement

The German Public Auditor responsible for the engagement is Martin Leistner.

Munich, March 8, 2021

KPMG AG
Wirtschaftsprüfungsgesellschaft

[signature]Leistner	[signature]Peschel
Wirtschaftsprüfer	Wirtschaftsprüfer