LPKF Laser & Electronics

FOR 40 YEARS
PERSEVERANCE AND A PIONEERING SPIRIT

2016

ANNUAL REPORT

LPKF LASER & ELECTRONICS AG AT A GLANCE

CONSOLIDATED REVENUE AS OF 31 DECEMBER

		2012	2013	2014	2015	2016
Revenue	EUR million	115.1	129.7	119.7	87.3	91.1
Revenue by region						
Germany	EUR million	13.2	11.7	12.2	12.6	12.9
Other Europe	EUR million	14.5	17.7	14.9	17.3	16.5
North America	EUR million	22.2	21.3	25.6	19.0	17.7
Asia	EUR million	63.3	77.4	63.4	35.6	42.3
Other	EUR million	1.9	1.6	3.6	2.8	1.7
Revenue by segments [1]						
DevelopmentQuipment	EUR million	19.4	20.9	25.1	25.5	22.6
ElectronicsQuipment	EUR million	56.4	75.7	51.2	29.9	30.6
WeldingQuipment	EUR million	17.1	21.5	20.9	23.3	24.0
SolarQuipment	EUR million	21.8	11.1	21.9	8.5	13.9
All other segments	EUR million	0.4	0.5	0.6	0.1	0.0

1 The figures prior to 2013 were adjusted.

CONSOLIDATED FINANCIAL KEY FIGURES AS OF 31 DECEMBER

		2012	2013	2014	2015	2016
EBIT	EUR million	20.4	23.2	12.7	-3.7	-6.8
EBIT margin	%	17.7	17.9	10.6	-4.3	-7.4
Consolidated net profit after non-controlling interests	EUR million	13.5	15.1	8.5	-3.5	-8.8
Net margin before non-controlling interests	%	12.4	12.1	7.1	-4.0	-9.7
ROCE[1] (Return on Capital Employed)	%	26.5	26.4	12.1	-3.6	-6.9
Cash and cash equivalents	EUR million	2.5	12.5	6.0	-0.9	3.6
Equity ratio	%	58.0	56.6	53.5	53.4	46.5
Cash flow from operating activities	EUR million	17.1	34.2	1.8	10.1	5.7
Investments in property, plant and equipment and intangible assets	EUR million	12.8	21.3	15.0	13.7	7.5
Earnings per share, diluted [1]	EUR	0.61	0.68	0.38	-0.16	-0.40
Dividend per share [1,2]	EUR	0.25	0.25	0.12	0.00	0.00
Orders on hand	EUR million	34.3	17.7	17.7	13.3	27.8
Incoming orders	EUR million	124.1	113.1	119.7	82.8	105.7
Employees [3,4]	Number	690	752	795	778	700

1 The figures prior to 2013 were adjusted retrospectively due to the capital increase from Company funds.
2 2016: Proposal at Annual General Meeting
3 excl. trainees and workers in minor employment
4 2016: Number as of the 31 December 2016 reporting date. For more information see p. 48, Workforce development

LIGHT-BASED PRECISION

LPKF Laser & Electronics AG is a highly specialized mechanical engineering company. It designs and manufactures laser systems. A typical application for these systems is in the production of electronic components. Since these components need to be built into smaller and more compact devices – such as smartphones – the utilization of high-precision laser beams as tools is becoming increasingly relevant.

LPKF has pioneered the use of lasers in micro material processing. Since its formation in 1976, the Company has created entirely new markets with its innovative ideas. Today, technology from LPKF is deployed in a wide range of industries – such as in the electronics sector, where LPKF systems are used to design or separate circuit boards. The automotive industry uses LPKF lasers for particulate-free welding of sensors or taillights. Solar cell manufacturers boost the efficiency of their modules by deploying LPKF laser scribers. Most recently, LPKF started offering a laser-based glass processing method for microelectronics. And a digital printing process for functional pastes has been added to the LPKF portfolio in 2016. In many areas, the superior precision offered by laser technology is replacing traditional techniques, thus paving the way for more intelligent, digital production. LPKF has used its knowledge and experience in the field of laser technology to acquire leadership in all of its markets. This is why the Company invests around 10% of its revenue into research and development every single year.

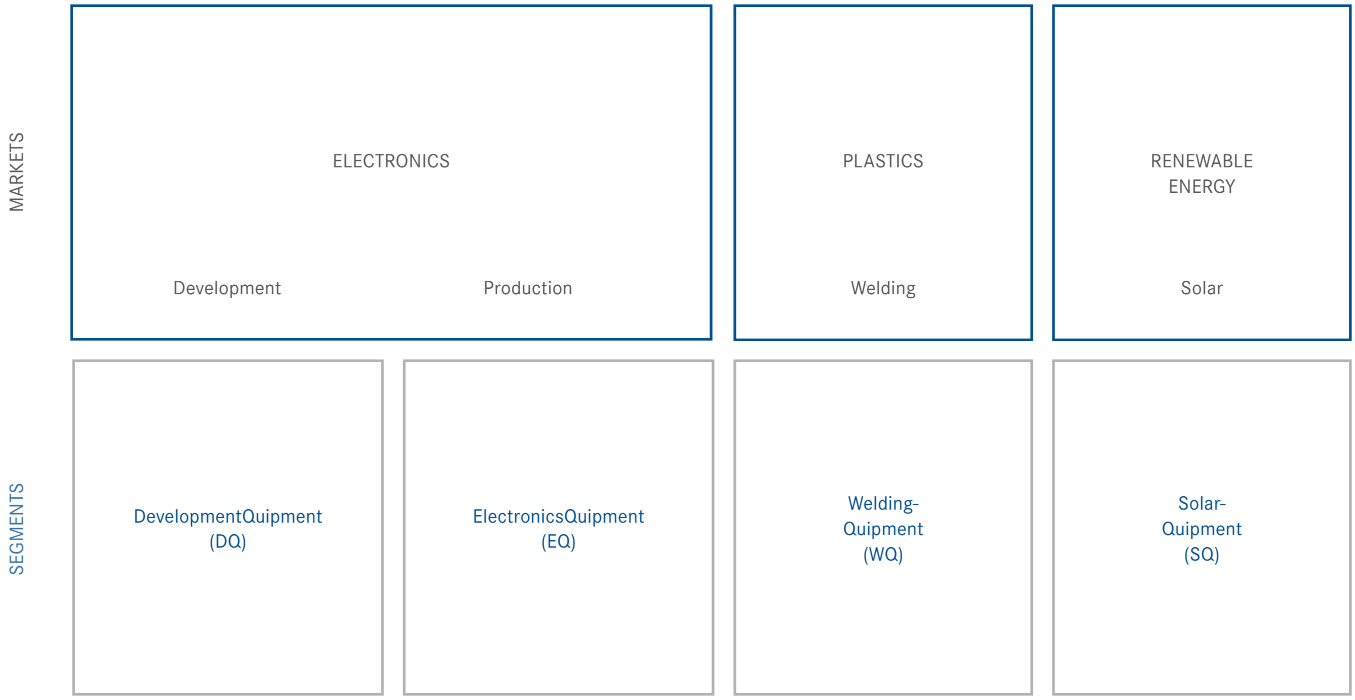
LPKF is headquartered in Garbsen near Hannover, Germany. The Company maintains a broad-based global presence, with a workforce of 700 based at sites in Europe, Asia and the US. The export share was around 86% in the 2016 financial year. The shares of LPKF Laser & Electronics AG are listed on the Prime Standard segment of Deutsche Börse.

FOR 40 YEARS PERSEVERANCE AND A PIONEERING SPIRIT

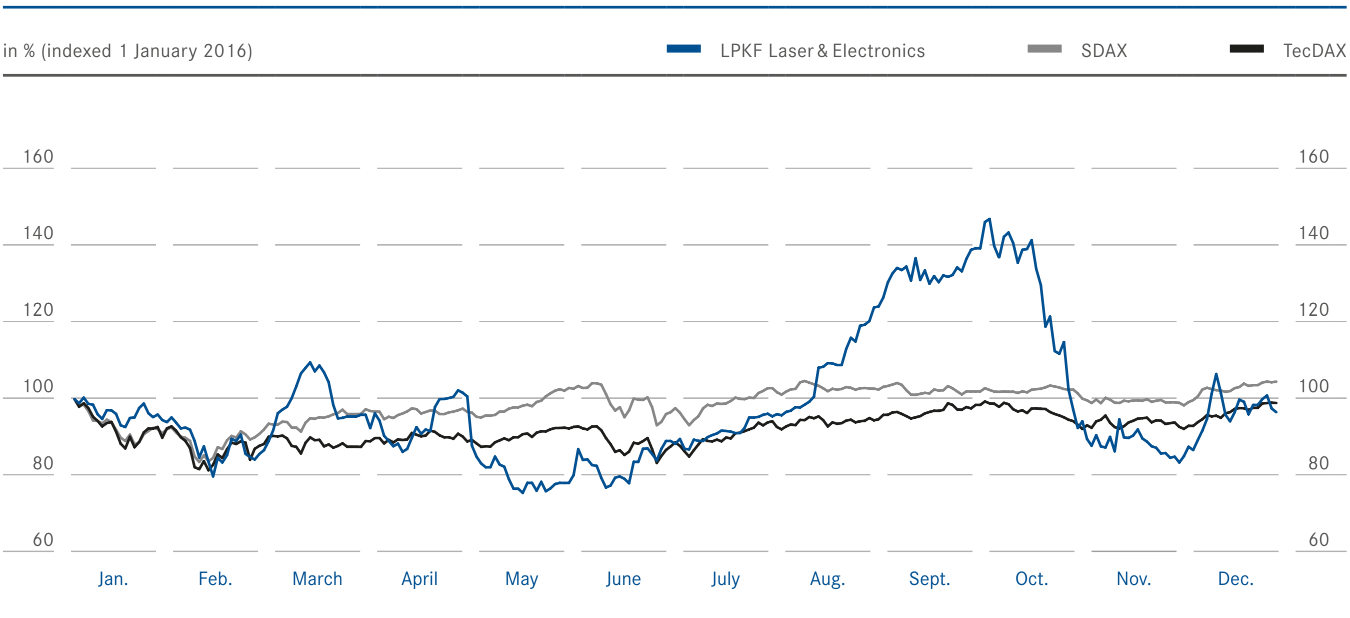
LPKF
Laser & Electronics

THE LPKF GROUP AT A GLANCE

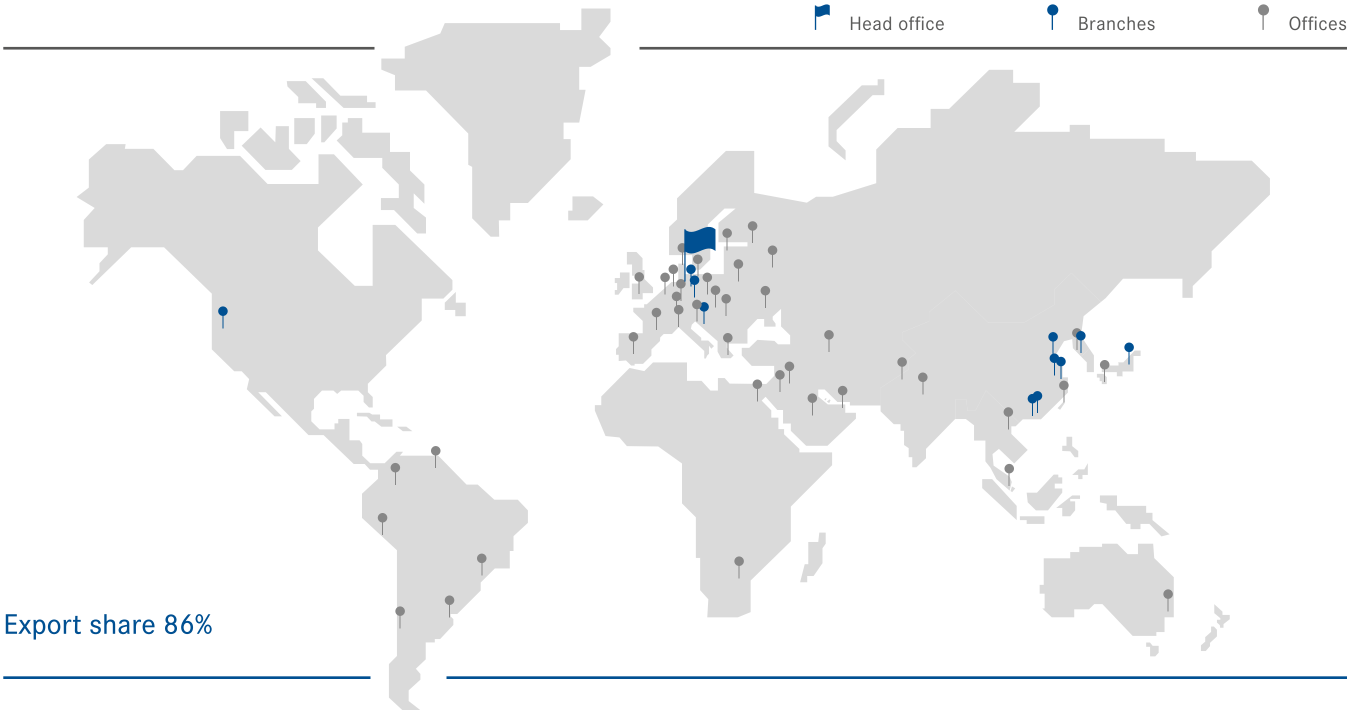
MARKETS AND SEGMENTS



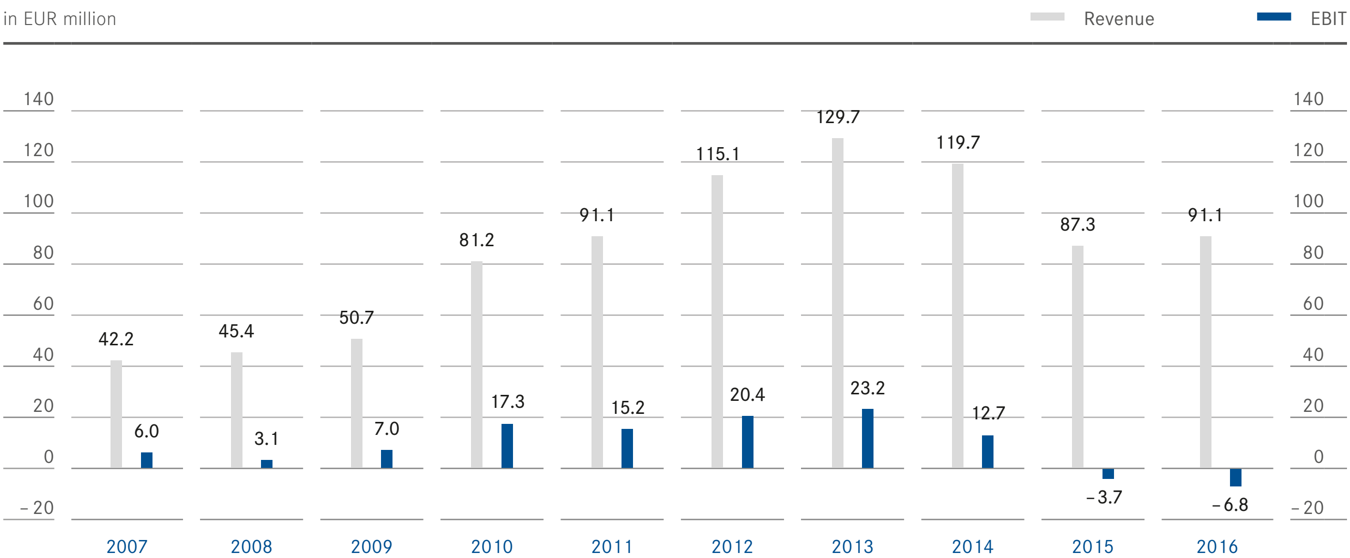
PERFORMANCE OF THE LPKF SHARE IN 2016



LPKF SITES WORLDWIDE



REVENUE AND EBIT



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TO OUR SHAREHOLDERS

COMBINED MANAGEMENT REPORT 2016

FOR 40 YEARS PERSEVERANCE AND A PIONEERING SPIRIT

PIONEERING SPIRIT

The future plays a crucial role for an innovation-driven company like LPKF. This hasn't been any different in the past. A look a the Company's 40-year history shows that both the great ideas of the people working for LPKF and their vision and determination have repeatedly set the Company on a good course.

CONSOLIDATED AND ANNUAL FINANCIAL STATEMENTS

FURTHER INFORMATION

FOCUS ON CORE SKILLS

MEGATRENDS

Future needs history

CHAIRMAN'S STATEMENT

Chief Executive Officer
DR. INGO BRETTHAUER

Ladies and Gentlemen,

The start to the 2016 financial year was highly dissatisfying. Revenue and incoming orders in particular were extremely low in the initial weeks of the year. In our business, financial years tend to have a weak start and then pick up during the course of the year. However, the start to 2016 was significantly more anemic than we had expected, even in the worst case scenario.

In view of this development, we decided in early May 2016 to introduce a comprehensive package of cost-cutting measures. Unfortunately, this also meant that the largest workforce reduction in LPKF's history to date was unavoidable. We needed to bring the Company's costs down to a level that would enable us to operate in the black, even with revenue much lower than planned. It was clear that this would not succeed in the 2016 financial year, because non-recurring expenses, for instance for downsizing, initially increase our costs. But at the end of the year, we had achieved our main goal: We lowered our costs so much that from 2017 onward our break-even point will be around EUR 90 million.

The key driver of our growth from 2010 to 2013, our laser direct structuring (LDS) business, saw another decline in revenue in 2016. Compared with our highest figure of approximately EUR 55 million in 2013, revenue fell to just around EUR 2.5 million in 2016. After unprecedented growth in the initial years, we have suffered our greatest revenue drop in recent years due to LDS. We also experienced adverse effects from our WeldingQuipment business in the United States and our DevelopmentQuipment business in China in 2016. In addition to all of this, we also had to deal with delayed product launches in this challenging financial year.

Despite all of these difficulties, we are happy that after two years of declining revenue, we were able to close out financial year 2016 with an increase in revenue of 4.4%. From mid-year onward, business improved again and the last quarter was even a relatively strong one. Unfortunately, in the end, our revenue numbers were not sufficient to generate positive earnings for 2016. In fall 2016, it became clear that we would be unable to hit our revenue targets, especially in the LDS segment. This made it necessary to recognize substantial impairment losses. This increased our loss in 2016 even further, but it did reduce risks for subsequent years.

Despite the aforementioned negative effects, I would like to point out that in three out of four segments, we grew revenue at the end of the year, in some cases very sharply. Of course, this is cold comfort because it was insufficient to propel us back into profitability. Strong downward pressure was additionally put on EBIT by the impairment losses I mentioned. Looking at our quarterly results without extraordinary items, however, our EBIT in the last three quarters was already positive.

To me, it is particularly important to note that the ElectronicsQuipment segment was able to increase revenue despite the overall further drop in the LDS business. With the exception of North America, WeldingQuipment also saw strong growth in nearly all important regions, especially in China.

"DESPITE THE DIFFICULT BUSINESS SITUATION IN 2016, WE DID NOT EASE UP ON DEVELOPING NEW PRODUCTS."

In the SolarQuipment segment, revenue nearly doubled, and the high level of orders on hand at the end of the year indicates that this figure will continue to rise in 2017.

Only in our DevelopmentQuipment segment did we see revenue decline year on year for the first time in seven years. In addition to regional weakness, particularly in China, this was due to the delayed launch of new ProtoLasers. In 2017, our special focus will be on these two areas.

Despite the difficult business situation in 2016, we did not ease up on developing new products. Although some planned deadlines were not met due to the considerable complexity of our technologies, we made significant progress with both new products. The products have been available from early 2017 onward, although the original plan was for them to contribute to revenue as early as 2016.

We had a better start to 2017 than the previous year. In this regard, we can currently look to the future with somewhat more optimism. Above all, this trend is receiving a push from growth in incoming orders, which at the end of the year put our orders on hand at 110% of the prior-year figure. The healthy flow of incoming orders did not abate in the initial weeks of 2017, and the positive trend is currently continuing. It goes without saying that we are just beginning a new financial year and to this extent, we still have a long road ahead of us. In view of this information, we made a more detailed forecast in early February 2017 and currently project a revenue increase to between EUR 92 million and EUR 100 million for 2017 with an EBIT margin of 1% to 5%.

At this point, my fellow Management Board members and I would like to thank our employees most of all. We asked a lot of them in 2016. Given the large cuts in staff numbers in particular, the remaining employees have much to do. Anyone who has been through this type of consolidation phase will understand this.

We would also like to thank the members of our Works Council for whom staff reductions are a particular challenge. The discussions were not easy by any means, but in the end we succeeded in conjunction with our Works Council in putting our company on much more solid footing and – above all – to safeguard the remaining jobs.

Thank you to the Supervisory Board members who challenged us during this difficult time, but also supported us constructively. In a number of meetings, we continually discussed measures and reported on their implementation. Needless to say, the experience we have had in recent years has influenced our strategic considerations for the future.

We would also like to thank our shareholders who stayed true to us during this difficult phase. LPKF can now look back at an impressive 40-year history. Despite hard times, the Company has not lost any of its innovative capabilities. We appreciate your loyalty!

Yours sincerely,

DR. INGO BRETTHAUER
Chief Executive Officer

THE MANAGEMENT BOARD

DR. INGO BRETTHAUER
Chief Executive Officer (CEO)
Strategy, Marketing, Sales
and Corporate Communications

Born 1955, member of the Management Board since 2009
Ingo Bretthauer studied engineering and economics in Germany and business administration in the USA. After gaining a doctorate at the University of Gießen, he worked for a number of different German and international companies.

DR. CHRISTIAN BIENIEK
Chief Operating Officer (COO)
Production, ERP and
Administration

Born 1967, member of the Management Board since 2012
Christian Bieniek studied mechanical engineering (with a focus on manufacturing technology) before completing his doctorate at TU Braunschweig. He then worked in a number of companies and joined the LPKF Management Board in December 2012.

KAI BENTZ
Chief Financial Officer (CFO)
Finance, Human Resources
and Organization

Born 1971, member of the Management Board since 2007
Upon completion of his degree in economics at the University of Hannover, Kai Bentz worked for a large international accounting and auditing firm. After qualifying as a tax advisor, he joined the LPKF Group in 2002.

BERND LANGE
Chief Technology Officer (CTO)
Technology, Research
and Development

Born 1961, member of the Management Board since 2004
Bernd Lange studied electrical engineering at the University of Odessa and has worked in a variety of companies in the fields of electrical engineering and scientific instrumentation. He joined the LPKF Group in 2000.

QUESTIONS FOR THE MANAGEMENT BOARD

Dr. Bretthauer, LPKF's share price fluctuated wildly in 2016, ranging from EUR 5.41 to EUR 10.64. It was not easy for many shareholders to steady their nerves. Can investors expect a better year of trading in 2017?

BRETTHAUER: Due to our weak business results in the period from 2014 to 2016, our share price was naturally volatile. We are putting every effort into returning to the black in 2017. The chances for success are good and this should also be reflected in our share price performance. Of course, we want to earn enough to pay dividends again as soon as possible.

In 2016, LPKF's loss was much higher than in the previous year for reasons including impairment losses. When do you aim to return to the high double-digit EBIT margins of recent years?

BRETTHAUER: First off, our top priority in 2017 after two years of losses is to return to profitability. And in the medium term, we want to again generate double-digit EBIT margins. Our current and future product range offers a good chance of success. Time will tell how quickly we will achieve this. But you can be sure that we will not be satisfied with single-digit EBIT margins.

What have you learned from the unexpected slump of the LDS business? How will you deal with risky business segments like this in the future?

BRETTHAUER: The LDS business generated excellent results for us over many years. The slump obviously caused the Company to suffer losses, but averaged out over the years, the profits have far outpaced the losses. However, we did draw certain conclusions from the LDS decline. In the future, we will more carefully weigh the opportunities and risks of new “star” products in our planning. And we intend to better balance out our high-risk ventures by expanding less risky or less volatile businesses.

Your current forecast for 2017 is equivalent to your last forecast for 2016. Have you become very cautious?

BRETTHAUER: We have always tried to be as realistic as possible in our forecasts. In volatile markets like ours, there will always be ups and downs. That's why accurate projections are so difficult. Recent events have taught us to focus on doing business cautiously, which is advisable in any case, and therefore not to promise too much. At the same time, however, we are looking boldly to the future.

Mr. Bentz, in 2016, you reduced the Group's workforce by around 100 full-time jobs. How can you ensure that employees who possess key knowledge remain in the Company?

BENTZ: That was really not easy. We lost many good employees due to the staff cuts. What was and remains important are discussions at all levels. We are trying to convey that our staff and the Company truly have good prospects. And the personnel cuts weren't the only thing that happened: a number of new products and processes were also developed. Moving forward requires all of our employees to be on board.

The Group's cost base was reduced substantially in 2016. How do you intend to maintain this level of spending in 2017 while hopefully boosting revenue?

BENTZ: It is in fact very important to maintain our cost discipline while our business grows. The much greater awareness of costs in the Company is also helpful. On the whole, our vertical integration is low, which means that our ratio of directly revenue-related costs to fixed costs is also lower. So, when our business grows, our fixed costs do not simply increase proportionately. That has quite a positive effect on profitability.

It looks like LPKF's shareholders will again fail to receive a dividend this year. How do you intend to make the Company's shares attractive to investors again?

BENTZ: LPKF does business in growing markets. In the electronics segment, everything is getting smaller, but at the same time, product life cycles are becoming shorter and shorter. Miniaturization and the essential flexibility are therefore key drivers for our customers' business and thus for our business as well. Thanks to new technologies and processes, lasers are now being implemented in applications that formerly used mechanical tools. And some applications were not even possible to date with conventional methods. Even during 2016, which was difficult and marked by cost cutting, we invested more than 10% of our revenue in development, and therefore in the future. From my point of view, our shares are attractive precisely due to these opportunities.

Mr. Lange, new products are slated to close the revenue gap that LDS left. In 2016, it appears this approach has not yet been successful. What progress is LPKF making with newly developed products?

LANGE: It is true that brand new products are currently playing a particularly important role for our growth strategy in all business segments. The high degree of novelty of course entails considerable risks in determining requirements, conducting development and launching the products. In view of the LDS downturn, the time we planned for these activities was too optimistic in some cases. What is notable is the broad range of new products that will contribute to revenue for the first time in 2017.

The LIDE process newly developed by LPKF is considered a key technology for the use of thin glass in the chip industry. What are the strengths of this technology? Where do you see the risks?

LANGE: Glass could play a significant role as a substrate material in electronic circuits in the future. LIDE stands for "laser-induced deep etching." This technology enables various possibilities, such as the efficient manufacture of very small, highly precise holes in glass (TGV). That is a large step forward toward using thin glass in the chip industry and beyond. The process is also suitable for the manufacture of inkjet nozzles, which have very high geometrical requirements, for filters, display glass, and much more. We developed the necessary equipment for this purpose and are currently obtaining approval for the process from partners for individual applications. What remains to be seen is how quickly it can be put into wider use.

The new digital LTP printing process will be used to print a very wide range of functional pastes. What are LPKF's prospects for 2017 and beyond?

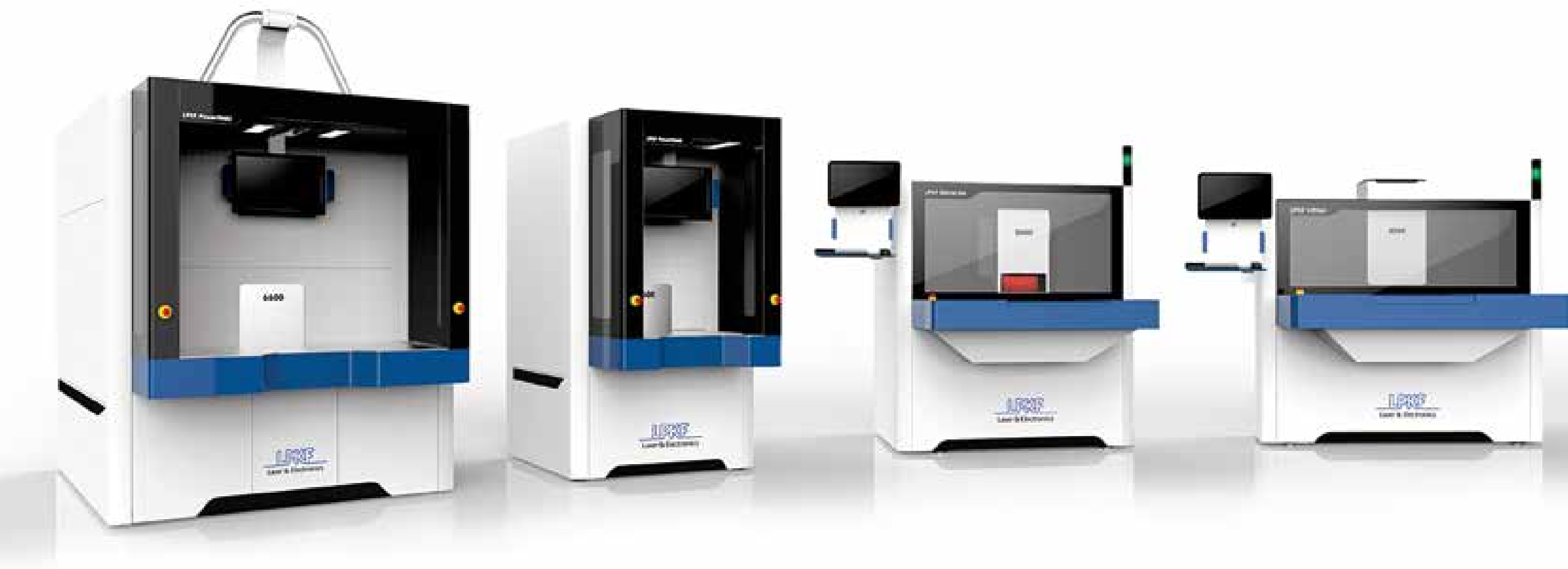
LANGE: LPKF's LTP technology offers a digital alternative to screen printing in the electronics industry. The range of potential applications for the technology is accordingly broad. In 2016, we began marketing in the area of flexible glass printing. This can produce economic effects very quickly and will therefore be our focus in 2017. We will provide evidence of suitability for industrial uses and subsequently develop additional applications.

LPKF operates in very dynamic markets. What does this mean for the development process?

LANGE: A key feature of dynamic markets is that manufacturing solutions are sought in a very short timeframe, so there are opportunities for those who can fill this need. Likewise, the requirements can change at any time during the product development process. We are mastering these challenges by stepping up the pace of our development processes and making our planning tools more dynamic. Here we concentrate on encouraging the motivation and self-organization of our development teams as best we can.

Dr. Bieniek, you have made slashing working capital a priority. What is it that you want to achieve? How do you intend to make progress?

BIENIEK: Reducing working capital is extremely important in order to improve liquidity. In addition, we also want to minimize the risk that our inventories will age and lose value. That can happen in particularly fast-paced high-tech industries, like ours. In optimizing our inventories, however, we cannot lose sight of the volatility of our markets. Projects often crop up very quickly and must be completed under extreme time pressure. The ability to deliver quickly is increasingly the factor that clinches a sale. We must therefore weigh the opportunities and risks when optimizing our inventories and define the correct approach in each case. In a project to optimize working capital across sites, we are therefore working hard on improved forecasting, increasing the flexibility of the supply chain, and better receivables management.



Capital expenditure has also been scaled back markedly at LPKF in recent years. What is your planned investment volume for the next few years?

BIENIEK: After substantial investments in infrastructure by LPKF from 2010 to 2015, we are currently well equipped for the future in three of our four production sites. Suhl, our solar scriber and LTP equipment site, is the only facility where we are currently planning the expansion of our production capacity. The gratifyingly high level of orders on hand and possible follow-on projects with extremely large and heavy equipment justifies a moderate investment here. Otherwise, we will continue to focus our capital expenditure on the innovative development projects that are our future.

LPKF operates four different production sites in Germany and Slovenia. How do you assess this structure from the perspective of efficiency? Does this make sense in the future as well?

BIENIEK: The current structure with four production sites in Europe is a historical development. As part of efficiency programs, we have repeatedly reviewed the advantages and disadvantages of further centralization. The opportunity to reduce the cost of site-specific overhead functions stands in contrast to the risk of losing employees with key knowledge by moving sites. Since our employees with their highly specialized knowledge and skills are our most important capital, we decided to combine and further multiply the advantages of a decentralized organization with those of a centralized organization as best as possible. A business segment is concentrated at each site. With streamlined processes and short paths of communication in compact organizational units, we can react quickly to the needs of our customers. Then again, we organize functions like basic research, purchasing, human resources and finance across sites to further leverage synergies.

Against the backdrop of our extremely knowledge-intensive products and the various markets that we serve with our four segments, I consider a structure with decentralized, agile, and largely autonomous units plus a strong backbone of centralized support functions to be an efficient system for LPKF's future.

THE LPKF PRODUCT FAMILY
The new design represents LPKF's high-tech systems across the entire product spectrum.

REPORT OF THE SUPERVISORY BOARD

The Supervisory Board:
BERND HACKMANN
DR. HEINO BÜSCHING
PROF. DR.-ING. ERICH BARKE

Ladies and Gentlemen,

Financial year 2016 left much to be desired for LPKF Laser & Electronics AG and our shareholders. Contrary to management expectations at the beginning of the year, 2016 was not a significant improvement over 2015. The consolidated operating loss of EUR – 6.8 million and EBIT margin of – 7.4% reflect the less than satisfactory revenue of EUR 91.1 million. These figures were also impacted by expenses for the workforce reduction and in particular also write-downs of inventories.

Newly developed technologies such as the laser systems for digital printing of functional pastes (LTP) and laser systems for processing glass (LIDE) did not yet contribute substantially to revenue in the 2016 financial year, but hold promise for a positive impact in the future.

MONITORING AND ADVISING

Reflecting the course of business, financial year 2016 also posed special challenges for the Supervisory Board. In the 2016 financial year, the Supervisory Board closely monitored the performance of LPKF Laser & Electronics AG and fulfilled its duties pursuant to the law and Articles of Incorporation. A total of sixteen Supervisory Board meetings including eight extraordinary meetings took place in the reporting period. With one exception, all three members of the Supervisory Board attended all meetings personally.

At the start of each meeting, the Supervisory Board customarily meets without the Management Board. because the first agenda item is reserved for internal Supervisory Board discussions.

The Supervisory Board passed resolutions after considering the opportunities and risks where required by the law, the Articles of Incorporation or the rules of procedure.

The Management Board presented to the Supervisory Board proposals requiring its approval in accordance with the Articles of Incorporation and rules of procedure of the Management Board, and the Supervisory Board approved them, if necessary after amending the proposals submitted. In addition, the Supervisory Board monitored the legality, propriety and fitness for purpose of the Management Board's actions.

The Supervisory Board regularly monitored the Company's management and advised the Management Board with regard to managing the Company at the Supervisory Board meetings and in a multitude of discussions with the Chairman of the Management Board as well as the members of the Management Board and the Supervisory Board members.

The Management Board informed the Supervisory Board without delay and comprehensively of all issues with regard to strategy, planning, business development, risk situation, risk management and compliance. In doing so, it addressed any deviations in the Company's development from plans and targets, stating the reasons for such differences (for more details see the section "Main focus of the discussions"). The Supervisory Board was involved at an early stage in all decisions of importance to the Group. The Management Board reports monthly in writing to the Supervisory Board at the level of the parent company about the statement of financial position, income statement, liquidity planning, business situation, product quality, status of development projects, risk management and the Company's risk situation. Such reports on the Group are submitted once a quarter.

MAIN FOCUS OF THE DISCUSSIONS

The main topic of the 2016 financial year was the Group's economic situation. The Management Board communicated key figures to the Supervisory Board regularly, particularly orders on hand, incoming orders, working capital, cash flow and the profit/loss situation. The Supervisory Board also monitored the situation with regard to the subsidiaries.

In accordance with the schedule agreed back in mid-2015, the Supervisory Board continued to meet monthly in 2016. The meetings in spring focused on analyzing revenue figures, also with a view to the pronounced seasonality of the revenue LPKF generates. In three meetings in April and early May 2016, the Supervisory Board along with the Management Board discussed the very weak business performance in the first quarter of 2016 and the planning for 2016. They also talked about the conclusions to be drawn from these, which were ultimately incorporated into measures to ensure profitability. These measures had a material impact as downsizing of around 100 full-time equivalents (FTE) became necessary. At the same time, our focus was and continues to be on guaranteeing the liquidity of the Company and the Group, particularly by reducing working capital.

The measures to ensure profitability affect all areas of the Company, including development, production, sales and administration. In this difficult period for LPKF, it is important to maintain a balance between necessary cuts and simultaneous preservation of the potential for developing new products. The aforementioned topics were discussed in every meeting in financial year 2016 from then on.

The Management Board also contributed to ensuring profitability by waiving its entitlement to variable remuneration in financial year 2016. The Supervisory Board thanks the Management Board for foregoing this compensation. Upon recommendation by the Supervisory Board, the Annual General Meeting voted to reduce the remuneration of the Supervisory Board.

In an organizational/HR context, the Supervisory Board discussed the legal requirements for a quota of women at Board (Supervisory and Management) and first/second-tier management level, and the implications that such a quota would have (see also under "Staffing").

A significant and permanent part of Supervisory Board meetings every year is the Supervisory Board's strategy meeting. This meeting is held along with the Management Board and the heads of segments. In the course of a two-day session, the Supervisory Board first addressed strategy proposals from Management Board members for their various divisions, followed by strategy items for the segments and, lastly, the overall strategy for the LPKF Group. In the meeting on 25 January 2017, the Supervisory Board approved the strategy paper updated by the Management Board following the strategy meeting.

The legal disputes involving patents held by LPKF Laser & Electronics AG are a regular agenda item.

And finally, internal auditing issues are also a fixture in Supervisory Board meetings. Internal auditing at LPKF Laser & Electronics AG has been outsourced to an auditing firm, which is reviewing all units of the Company according to a set schedule and action plan. During this agenda item, the Management Board reported on the internal audit findings. In each case, the Supervisory Board duly noted the report and approved the measures proposed for improving internal workflows.

CORPORATE GOVERNANCE AND DECLARATION OF COMPLIANCE

In 2016, the Supervisory Board also intensively discussed the implementation of corporate governance standards in the Company. LPKF Laser & Electronics AG reports extensively on corporate governance in the corporate governance report. On 21 March 2017, the Management Board and Supervisory Board issued the annual Declaration of Compliance in accordance with Section 161 German Stock Corporation Act (Aktiengesetz) which reports deviations from the recommendations and outlines the Supervisory Board's objectives for its composition. The declarations are also reproduced in the corporate governance report. Additionally, the Declaration of Compliance is publicly available on the Internet at http://www.lpkf.com/investor-relations/corporate-governance/declaration-compliance.htm. LPKF Laser & Electronics AG fulfills nearly all of the recommendations and is committed to the Corporate Governance Code as an integral part of its corporate governance activities. No conflicts of interest arose in the reporting year (see "Potential conflicts of interest"); the independence of the members of the Supervisory Board was ensured. Sustainability was and continues to be an important part of the Group's strategy. The Supervisory Board supports the activities presented in the Sustainability Report relating to the corporate, social, and environmental responsibility of LPKF Laser & Electronics AG.

AUDIT OF THE PARENT COMPANY'S ANNUAL FINANCIAL STATEMENTS AND OF THE CONSOLIDATED FINANCIAL STATEMENTS

As resolved by the Company's Annual General Meeting, the Supervisory Board engaged PricewaterhouseCoopers GmbH Wirtschaftsprüfungsgesellschaft (PwC) to audit the 2016 annual and consolidated financial statements and defined the focal points of the audit at its meeting on 1 December 2016. The annual and consolidated financial statements as well as the combined management and Group management report were audited by the auditors and issued with an unqualified auditors' report. The auditor participated in the Supervisory Board meetings on 27 February 2017 and 21 March 2017 and reported on the audits of the annual and consolidated financial statements and the combined management and Group management report. Furthermore, after reviewing the risk early warning system, the auditor of the financial statements confirmed that the Management Board executed the measures required by the German Stock Corporation Act to identify risks that could endanger the continued existence of the Company as a going concern.

The documents concerning the annual financial statements of the parent and the consolidated financial statements and the combined management and Group management report as well as the audit reports prepared by PwC were submitted to the members of the Supervisory Board for inspection and review in a timely manner. The representatives of the auditor reported on the main findings of their audit at the relevant Supervisory Board financial meetings, especially providing explanations on the net assets, financial position and results of operations of the Company and the Group as well as further information. There were no circumstances that cast doubt on the impartiality of the auditor. The auditor reported on these activities along with the auditing of the financial statements to the Supervisory Board as agreed.

The Supervisory Board discussed PwC's audit reports and the documents relating to the financial statements at length with the representatives of the auditor and examined them meticulously. The Supervisory Board came to the conclusion that no objections have to be raised against annual and consolidated financial statements as well as the combined management and Group management report. The Supervisory Board agreed with result of the auditor's audit and approved the annual financial statements of the parent and the consolidated financial statements prepared by the Management Board at its meeting on 21 March 2017. The annual financial statements of LPKF Laser & Electronics AG are thereby adopted.

The Supervisory Board reviewed the proposal by the Management Board for the appropriation of net accumulated losses. Given the business performance in the reporting year and the outlook for 2017, the Management Board and the Supervisory Board will propose to the Annual General Meeting on 1 June 2017 not to pay a dividend.

POTENTIAL CONFLICTS OF INTEREST

The Supervisory Board gave approval for Mr. Bernd Hackmann to consult for LPKF customer Becktronic GmbH. Until the end of 2015, Mr. Hackmann advised this customer on occasional questions regarding the production of a new type of print stencils. This work has been suspended for the time being. The Management Board of LPKF AG does and did not believe that this constitutes a conflict of interest with the activities of LPKF Laser & Electronics AG's Supervisory Board.

STAFFING

In the first six months of 2016, the Supervisory Board had considered expanding the Board to four members, and proposed to the Annual General Meeting such an expansion, naming a female candidate, along with the invitation. Against the backdrop of the measures taken in May 2016 to ensure profitability and the associated reduction in the workforce, the Supervisory Board withdrew this proposal prior to the Annual General Meeting. When the time is right, the Supervisory Board will revisit the issue of ensuring the participation of women in the Company's Supervisory Board.

THANKS

The Supervisory Board would like to thank the Management Board, the division heads, the members of the executive management of the subsidiaries as well as all of the LPKF Group's employees worldwide for their valuable contributions and commitment to the Company in what has been a difficult economic environment in financial year 2016. During this time of less than satisfactory performance for the Group, the Works Council members not only constructively represented the interests of the Group's employees, but always kept the welfare of the Company as a whole in their sights. We are particularly thankful for their efforts.

Garbsen, Germany, March 2017

DR. HEINO BÜSCHING
Chairman of the Supervisory Board

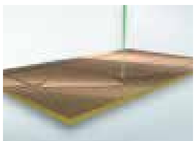
SEGMENTS AT A GLANCE

LPKF offers a broad portfolio of products for a diverse range of applications and markets. This broad-based approach makes the Company less dependent on cycles within individual markets. Notwithstanding the various product groups, (almost) everything at LPKF revolves around micro material processing with lasers.

DEVELOPMENTQUIPMENT (DQ)

LPKF ProtoLaser S4

LPKF leads the market in zero-chemical prototype production in the electronics lab. Instead of etching, board materials are scribed by a mechanical or laser system.



Laser structuring with the ProtoLaser S4

LPKF's lab lasers are especially popular for processing the kinds of specialized, high-quality materials now increasingly used in electronics. Sensitive as they are to mechanical stresses and geometric inaccuracies, these expensive materials cannot be worked properly with conventional tools. The solution is laser systems that precisely vaporize the coatings laser pulse by laser pulse while leaving the circuit board's network structure untouched.

LPKF has developed the ProtoLaser S4 (IR laser) and ProtoLaser U4 (UV laser) for these tasks. And LPKF's new ultrashort pulse system ProtoLaser R now offers customers a way to experiment with entirely new materials in the lab at the micro- and nanoscale.

ELECTRONICSQUIPMENT (EQ)

LPKF MicroLine

In the "conventional" circuit board milling segment, some brand new options are now offered by the new LPKF MicroLine 5000 laser drilling system, which is capable of drilling holes with diameters of up to 20 µm in various organic and inorganic substrates. The system can also cut flexible circuit board materials such as IC substrates and HDI boards.

With these features, the high-performance system already handles the challenges the electronics industry has yet to face. Compact LPKF MicroLine 2000 units are now increasingly to be found in manufacturing facilities: The high-precision laser process cuts close to the edge of sensitive structures and components.

Before the board is populated with the components, solder paste is screen-printed onto the board. The stencils required for this job must be precisely cut to tolerances of a few microns. All over the world, this is done around the clock by StencilLasers from market leader LPKF. The StencilLaser G 6080 is the industry's benchmark system.

Full flexibility: precise, complex contour cutting and perfectly drilled holes with LPKF laser tech

LPKF Vitrion

For the connection of integrated circuits in chip packages (IC packaging, ICP) and with conventional circuit boards, the contacts are routed using interposers and thereby spread to wider pitches. LPKF's innovative LIDE process enables the use of inexpensive glass substrates for this purpose.

This does depend on the ability to achieve rapid, precise formatting of the holes for the through-glass-vias, however. Capable of up to 5,000 formations/second with hole diameters of less than 15 µm, the LPKF Vitrion laser system represents a breakthrough for the use of glass as a substrate material for high-density circuit carriers.

Powering-up: processes from LPKF are offering new opportunities for chip package miniaturization

For MID projects with three-dimensional components (MIDs) and IC packaging, the laser systems and processes for laser direct structuring (LDS) achieve high-precision, ultrafine 3D conductive traces on plastics. The patented process offers space-saving solutions for many applications. As just one example, the previously unused upper surface of chip packages can be used for scribing antennas that are connected to the internal components. This is an area ripe for further miniaturization.

WELDINGQUIPMENT (WQ)

LPKF PowerWeld3D 8000

LPKF pioneered the innovative process of laser plastic welding. Laser plastic welding has the advantage of being very clean, since the process works without foreign materials such as adhesives, while minimizing component stress from high-frequency motion (for example). In laser plastic welding, the laser beam penetrates the upper joining partner and is absorbed by the lower component, thereby creating a reliable and visually appealing weld seam. The systems and processes offered by LPKF cover a broad spectrum of applications and new usages are regularly being identified. One specialized area of excellence involves systems for the high-volume production of large 3D parts such as vehicle taillights and other components.

With its new, patent-pending "WobbleWelding" technology, LPKF is expanding its lead in this area and supporting the lightweight trend. LPKF is also well-positioned at the other end of the component scale, such as in microfluidics. A major contribution is being made here by LPKF's next-generation ProSET software for rapid weld path configuration.

Automotive parts: a large-scale laser plastic welding application

SOLARQUIPMENT (SQ)

LPKF Allegro

In the solar sector, success or failure is decided by the production costs of solar modules and their energy output under real-world conditions.

Making the most of sunlight: precise laser processes maximize the per-module yield

LPKF is setting new standards globally with its "Allegro" laser scribers: The systems maximize the active module surface and thus the yield from a thin-film solar module. The combination of rapid processing and on-the-fly glass feeding minimizes unit costs while maximizing cost-efficiency.

LTP (Laser Transfer Printing) is the new digital printing process for functional pastes developed by LPKF as an alternative to screen printing. In addition to the obvious benefits of a digital printing system in terms of its flexibility, the LTP method also offers higher-resolution printing.

SERVICE & SUPPORT

LPKF has been actively involved in high-performance systems for industrial production and efficient prototyping methods for many years, all over the world.

From the outset, one important goal and differentiator was that LPKF would offer a reliable, worldwide support structure for its systems around the clock. Today, our support works from three Service Hubs based in Europe, the US and Asia. A global warehouse network ensures spare parts are available at short notice without complex formalities.

LPKF's skilled customer service team can draw on many years of experience gained in a wide range of production and application areas. After system installation and commissioning, LPKF also provides support for the customer production ramp-up. Customers are also increasingly using service contracts as a preventive approach to system availability. Remote services offer an efficient way to analyze performance and apply updates. If things do go "haywire", however, experts from an LPKF Service Hub are onsite quickly, plus a trained LPKF representative if necessary.

LPKF's subsidiary LaserMicronics GmbH helps customers with process design and optimization and can also provide support for production orders.

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SCHEFFELSTRASSE

THIS SMALL WORKSHOP IN HANOVER, GERMANY, WAS WHERE IT ALL BEGAN.

1976 – Company formation

1979 – LPKF posts revenue of over DEM 1 million

1982 – LPKF enters the US market


1976
PIONEERING SPIRIT
Find out more
600 units sold after ten years
1986
Entry into laser technology
1989
Formation of present-day SolarQuipment GmbH in Suhl
1991
Move to new company head office in Garbsen
1991
Formation of US subsidiary
1992

PIONEERING SPIRIT

In the mid-1970s, the four founding members Jürgen Seebach, Klaus Barke, Klaus Sülter and Bernd Hildebrandt came together to form LPKF, united by their ingenious idea for manufacturing circuit boards without the use of etching. Over the space of just ten years, the four founders had used their boundless inventiveness and pioneering spirit to build up a successful high-tech company that had established a presence on the global market with its products for PCB milling.

"Dynamic innovation has always been our focus at LPKF, and we always had plenty of ideas and concepts. We wanted to try some new approaches and we certainly weren't afraid to make mistakes. And this was just the mindset we adopted when we jumped into laser technology."

Bernd Hildebrandt, former LPKF director, CEO and later Chairman of the Company's Supervisory Board

First circuit board plotters for small-scale production runs

BUILDING A SUCCESSFUL ENTERPRISE WITH COURAGE, KNOW-HOW AND CREATIVITY

StencilLaser
SL 600x600
from 1995

THE ENTRY INTO LASER TECHNOLOGY IN 1989 PROVED TO BE JUST THE START OF A WHOLE SERIES OF TECHNOLOGICAL BREAKTHROUGHS AT LPKF

MASTERING CHALLENGES

Miniaturization in electronics was already underway in the 1970s, and the trend has continued unabated to the present day. Then as now, the market was highly competitive and LPKF had to improve its machinery and modify it to match new requirements on a continuous basis.

ENTRY INTO LASER TECHNOLOGY

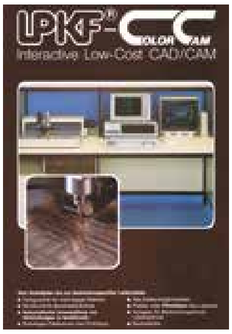
In 1989, laser technology gave LPKF access to truly new dimensions of precision. While entry into the market was initially time-consuming and costly, the foundation stone had been laid for the long-term success of the business. Not least because laser technology offered access to many new applications in the field of material processing.

Step by step, and with a wealth of development work, LPKF established itself in the many fields of application for contactless laser milling. In the case of rapid prototyping, for example, which was at the time entirely dependent on the use of mechanical milling drills, it took many years before the Company was able to offer laser-based systems for printed circuit board milling, plastic welding or laser direct structuring.

GOING PUBLIC

Research and development both need a strong capital base. Capital requirements increased in particular with the entry into laser systems and the aim of exploiting the many opportunities offered by this technology. When Deutsche Börse established its “New Market” in 1997, the time had finally come: the new segment offered a unique opportunity for startups or smaller companies to gain access to fresh capital. LPKF decided to go public in 1998, finally taking its place on the world’s stage.

The small “garage business” had transformed itself into an international corporation. LPKF Laser & Electronics AG, which celebrated its 40th anniversary in 2016, is now represented by subsidiaries and distributors in over 70 countries worldwide.



LPKF COLORCAM from the mid-1980s

LPKF brochure from the 1990s

COMPLEX CAD/CAM SOLUTIONS

During the eighties and nineties, LPKF developed into a sought-after provider of CAD/CAM solutions for the design and manufacture of PCB layouts.

7 OSTERIEDE

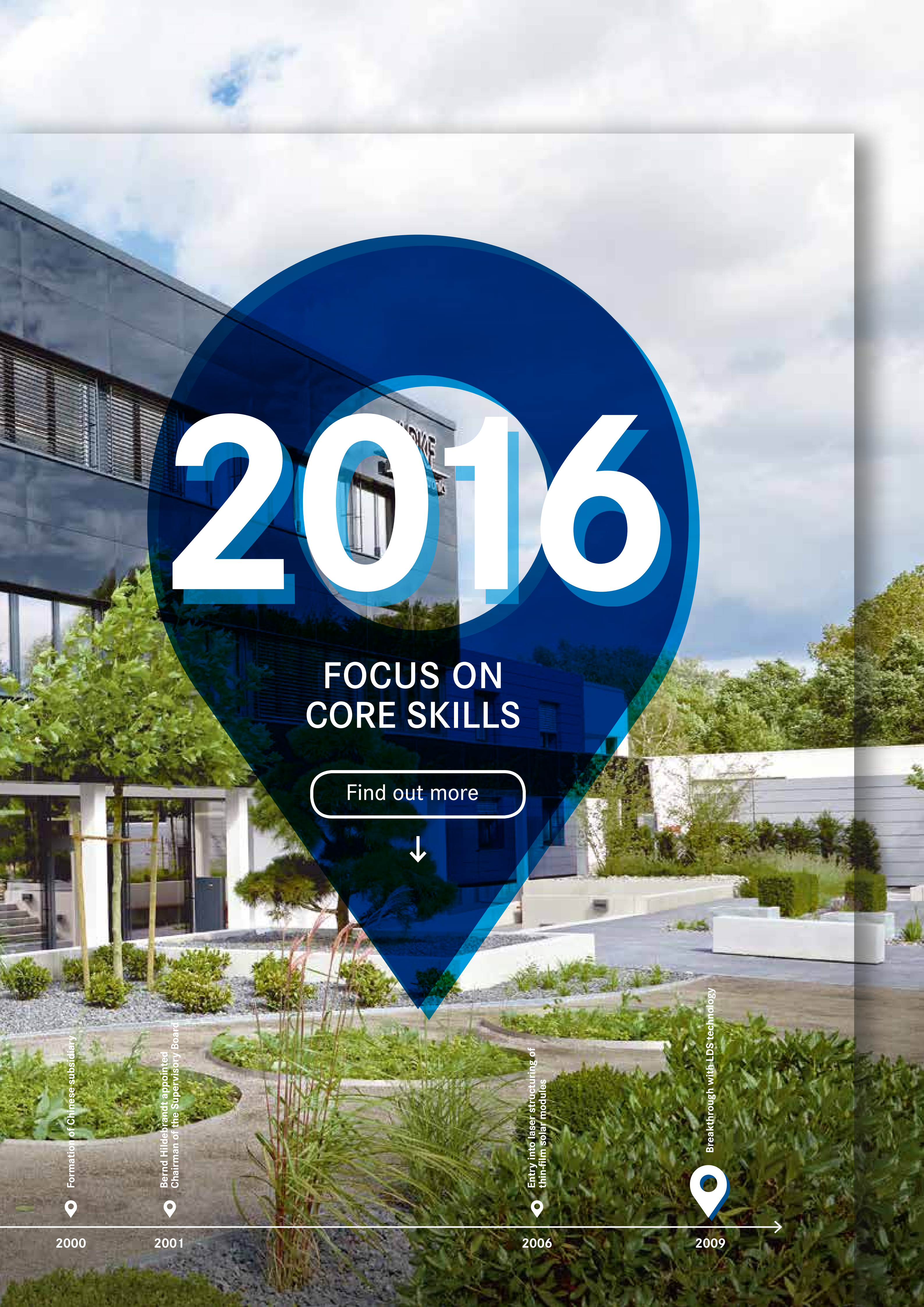
THE NEW COMPANY HEAD OFFICE IN GARBSEN.

1992 StencilLaser development

1994 Formation of the present-day LPKF Laser & Electronics d.o.o. in Naklo

1998 IPO

1999 LPKF's workforce passes the 100 mark



2016

FOCUS ON CORE SKILLS

Find out more

2000 – Formation of Chinese subsidiary

2001 – Bernd Hildebrandt appointed Chairman of the Supervisory Board

2006 – Entry into laser structuring of thin-film solar modules

2009 – Breakthrough with LDS technology

FOCUS ON CORE SKILLS

Especially when times are hard, it is important that a technology business maintains focus throughout the company and follows a clear path back to a profitable growth trajectory. After the revenue and earnings downturn in the previous two years and issues affecting the LDS business, LPKF decided in 2016 to concentrate on expanding and strengthening its core business. These include segments such as DevelopmentQuipment and WeldingQuipment, for example. Both segments enjoy an excellent position in the market and very solid growth potential. Development work has also been focused on those projects that can be expected to contribute to revenue and earnings at relatively short notice. Other development projects have not been cancelled but have been initially postponed.

KNOW-HOW AND EXPERIENCE

All product groups within LPKF are based on know-how and experience gained in laser-based micro material processing.

- High-precision drive technology: This forms the basis for the efficient deployment of a laser as a tool. Several of our machines work within tolerances under 10 microns.

- Laser technology and optics: Laser sources and lenses are the primary components within our machines. We use a wide variety of laser sources, and we actually develop and manufacture several source types in-house.

- Control technology and software: Software is an increasingly important part of mechanical engineering, and 50% of our development expenditure is now used for software development. In-house software also offers effective protection against imitators.

- Materials science: Most of our technologies do not involve a single, monolithic machine but depend on multi-stage processes in which material properties always have an important role to play. Expertise in chemicals is therefore now one of our core skills as well.

TODAY AND TOMORROW – A CLEAR FOCUS ON OUR CORE SKILLS

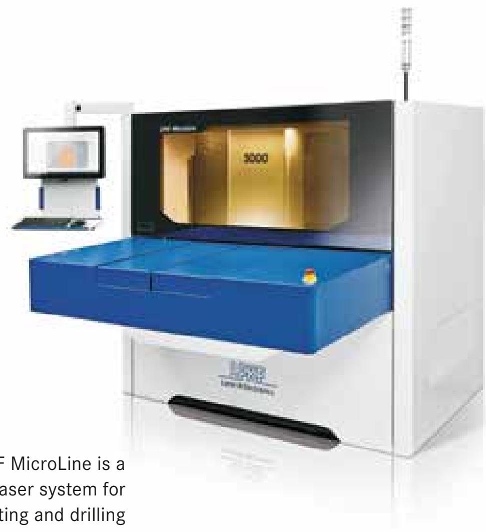
ULTRASHORT PULSE LASER DEPLOYMENT

The LPKF ProtoLaser R is the first laser system using an ultrashort pulse laser that is optimized for use in development labs. The short pulse length changes the interaction between laser beam and material, enabling the cold material processing of heat-sensitive substrates, the structuring of thin-film systems or the use of non-linear effects – such as in transparent components, for example.

EFFICIENT CUTTING OF FLEXIBLE CIRCUIT BOARDS

LPKF's MicroLine-2000 laser systems are to be found in electronics factories all over the world. The systems use a UV laser to cut circuit boards while applying zero mechanical force, right up to the edge of sensitive components or conductive paths. Working from customer requirements, LPKF can supply systems in several power classes and a range of handling configurations that permit seamless integration into the customer's own production line.

Laser machining with an ultrashort pulse laser



LPKF MicroLine is a UV laser system for cutting and drilling flexible printed circuits

NEW HIGH-END SYSTEM

The LPKF MicroLine 5000 is our premium system for the industrial machining of thin, flexible circuit board materials, offering precision drilling and cutting of holes and contours. Featuring a UV laser source, the system is also suitable for the delicate machining of IC substrates or HDI (high-density interconnect) boards.

20XX

DIGITALIZED PRODUCTION

FAST, DIRECT AND FLEXIBLE

2009 – Revenue cracks the EUR 50 million barrier

2011 – LPKF wins single largest order to date worth EUR 43 million

2012 – Inclusion in the TecDAX

2012 – Revenue exceeds EUR 100 million for the first time

future

MEGATRENDS

Find out more ↓

The financial year turns out to be the most successful in LPKF's history

2013

Establishment of independently operating business units

2015

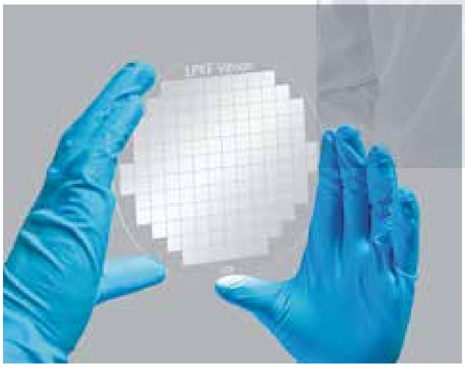
LPKF launches two completely new product groups: LIDE and LTP

2016

MEGATRENDS

As a high-tech company and innovation leader, LPKF must identify market trends, predict the issues faced by potential customers and offer new technologies in good time as part of a continuous process. Lasers are flexible and precise tools that help our customers deal with long-term trends such as miniaturization, lightweight automotive and production process digitalization in the future. Whether clients are looking to achieve efficiency gains in production or solve technical problems such as printing sequential serial numbers on vehicle windshields, LPKF concentrates on producing real-world competitive advantages for its users and customers.

Laser deployment results in competitive advantages



Glass is a high-tech microsystems technology material

DIGITAL PRODUCTION – INDUSTRY 4.0 – NEEDS THE RIGHT KIND OF TOOL: ONE THAT IS RAPID, DIRECT AND FLEXIBLE

GLASS IS THE MATERIAL OF THE FUTURE FOR MICROSYSTEMS TECHNOLOGIES

Manufacturers of chip housings, sensors, displays, medical microfilters or MEMS (microelectromechanical systems) devices have long appreciated the benefits of using glass. Glass features excellent electrical properties, is an insulator, does not react with chemical substances, and has a uniform, smooth surface. Glass is also transparent and is pleasant to the touch. On the other hand, glass is also difficult to work, and machining tiny, fissure-free holes in glass has presented a particular problem to date. LPKF has now solved this problem with its patent-pending Laser-Induced Deep Etching (LIDE) process. The LIDE process enables the creation of ultra high-precision holes and structures in glass at very high speeds. LPKF has therefore paved the way for an increased usage of glass in microsystems technology.

LASER TRANSFER PRINTING (LTP)

Printed electronics is a burgeoning market now experiencing rapid growth. According to ID-TechEX, all segments within printed electronics are likely to see average annual growth of around 18% by 2024, boosting its total volume to nearly EUR 58 billion. LPKF intends to enjoy a share of this growth with its laser systems for the digital printing of metallic pastes. LTP (Laser Transfer Printing) is the new digital printing process for functional pastes developed by LPKF as an alternative to screen printing. Screen printing is a very common process within the electronics industry.

In addition to the obvious benefits of a digital printing system in terms of its flexibility, the LTP method also offers higher-resolution printing and can therefore contribute to reducing the consumption of pastes containing expensive metals. In early 2015, LPKF enhanced its presence in this field with an acquisition, and the first machine was sold to an automotive glassmaker in 2016.

A VISION OF DIGITAL PRODUCTION IN THE FUTURE

- Laser processes supplant a subset of mechanical tools, making assembly lines more flexible
- Workpieces are transformed into smart data media
- Components change to match data records
- Components consist entirely of data records
- On-demand production is the new standard

The Vitrion 5000’s LIDE technology is opening up new markets in microsystems technology

THE LPKF SHARE

SHARE PRICE TRAJECTORY MIRRORS BUSINESS PERFORMANCE

In 2016, LPKF's shares took a roller coaster ride. At the beginning of the year, the Company's share price stood at EUR 7.12. At year-end, it was EUR 6.95. The high price of EUR 10.64 was reached on 5 October and the low of EUR 5.41 on 17 May.

LPKF's share price was primarily influenced by the Company's disappointing business performance. Political factors also had a substantial impact on stock markets. Following a weak first quarter, consolidated revenue improved considerably in the second quarter, and LPKF AG's share price topped EUR 10 as a result. This performance did not continue in the third quarter. Following the profit warning issued by LPKF in October 2016, the share price dropped to under EUR 6 by the start of December. It improved again to just under EUR 7 by the end of the year.

LPKF's market capitalization was EUR 158.56 million on 4 January 2016, and EUR 154.77 million on 30 December 2016.

The share price performance was also reflected in the demand for LPKF's shares. The trading volume was between 2,118 and 270,939, with an average of 51,993 shares trading hands on Xetra each day.

STOCK MARKETS

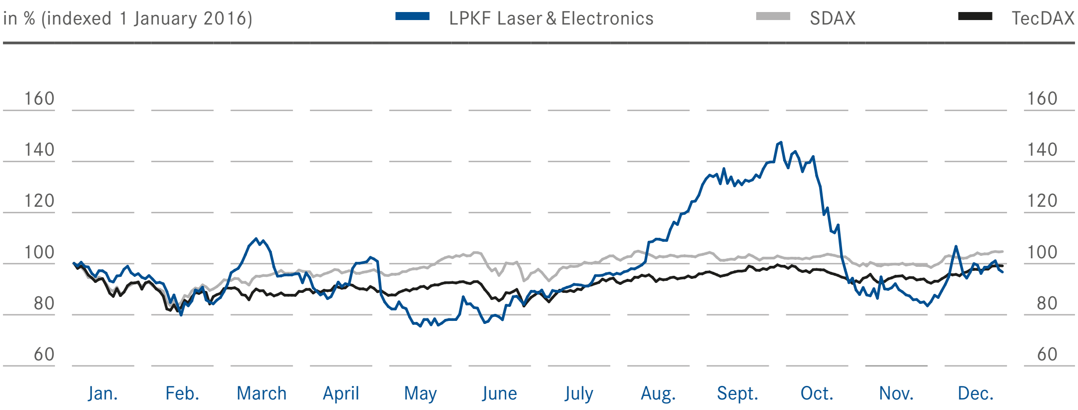
Three key stock market trends shaped 2016

At the end of 2016, the four major German stock indices registered results for the year ranging from a loss of 1% to a gain of 7%. The three major trends here can be summed up as follows: Brexit, the US election and the US Federal Reserve. The first half of the year in particular was marked by Brexit, with strong fluctuations observed in both directions in the markets as a whole. Still, even when – contrary to all polls – the results of the vote were clear, the markets settled down noticeably over the summer months. In November, investors then experienced déjà-vu with the US elections and again, all experts and predictions were proven wrong. When the results were in, the markets began a rally, which quickly stalled in view of a further interest rate hike by the US Federal Reserve.

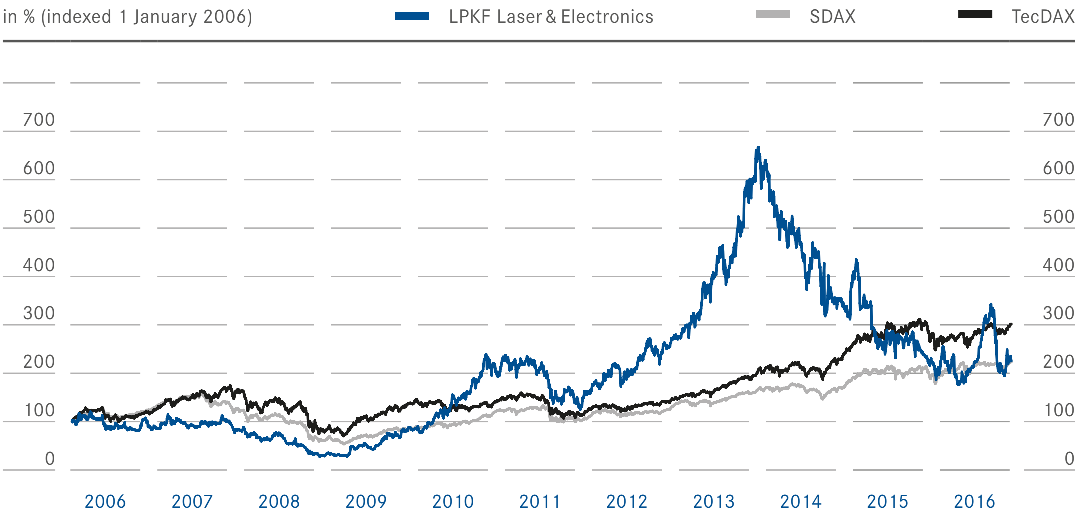
The markets' largely positive results are due to this year-end rally. The DAX closed at 11,481 points for an increase of 6.9%. At 22,189 points, the MDAX closed out the year with a gain of 6.8%. The SDAX was up 4.6% to 9,519 points. Only the TecDAX was unable to keep the pace, recording a loss of 1.0% at 1,812 points.

The major international stock exchanges developed unevenly. The Euro Stoxx 50, which features the eurozone's blue chip stocks, finished 2016 at 3,290 points, up 0.1%. In the United States, the Dow Jones gained 12.3% during the year, closing at 19,762 points. The Nasdaq Composite climbed 6.3% ending the year at 5,383 points.

PERFORMANCE OF THE LPKF SHARE IN 2016



PERFORMANCE OF THE LPKF SHARE 2006 – 2016



STOCK MARKET OUTLOOK ON 2017

The global economy is humming, and commodities prices are rising. Analysts therefore expect that the global economy will grow 3.5% after 3% in the previous year. The larger emerging economies of Brazil and Russia are nearing the end of a recession. In the United States, growth is also picking up. Forecasts suggest growth of 2.3% for 2017 after 1.3% a year before. Nonetheless, all forecasts must be treated with caution. The situation continues to be fraught with uncertainty. A key role here is played by the president of the United States. In 2017, we will see which domestic and foreign policy plans he will really implement and which of these will be sustained. Limiting global trade would have a strong impact on capital markets. Another factor influencing the situation is developments in Europe. Elections in the Netherlands, France and Germany could reshape the political landscape. Italy's banks urgently require capital increases to stay afloat, Brexit must be managed, and the UK's economy is facing major challenges.

A key factor for the stock market is whether and how much corporate profits will grow. If economic growth forecasts prove correct, conditions will continue to be good for equities in 2017. Most experts are more optimistic about Europe's chances in this regard than those of the United States. After the sharp rise of the Dow Jones, listed companies in Europe have significant ground to make up.

MARKET CAPITALIZATION AND SHAREHOLDER STRUCTURE

The subscribed capital of LPKF Laser & Electronics AG amounted to EUR 22,269,588.00. The corresponding number of ordinary shares are admitted to trading on the Prime Standard segment of the Frankfurt Stock Exchange's Regulated Market. According to Deutsche Börse AG's definition, 85% of LPKF's shares are in free float. LPKF closed the year with a market capitalization of EUR 154.77 million as of 30 December 2016.

DIVIDEND POLICY AS PART OF CORPORATE STRATEGY

LPKF AG wants to increase the Company's enterprise value and attractiveness in the long term. After successful financial years, shareholders should also participate directly in the positive performance through dividend payments. Our dividend policy is based on continuity and reliability. As a rule, the Company aims to propose to the Annual General Meeting that between 30% and 50% of LPKF's earnings per share be distributed as a dividend. LPKF will only deviate from this aim if it faces an uncertain future due to circumstances such as an economic downturn, or if paying a dividend would jeopardize its ability to finance investments or dilute the financial position of LPKF AG or the Group.

Given the weak performance of the Company's operating business in financial year 2016, the Management Board and the Supervisory Board will propose to the Annual General Meeting on 1 June 2017 not to pay a dividend.

The equity ratio amounts to 46.5%.

The focus of management is on solid financing of the Company. Ensuring a high equity ratio of at least 40% (currently: 46.5%) is one of the key prerequisites.

KEY FIGURES ON THE LPKF SHARE

	2016	2015	2014
Number of shares as on 31 December	22,269,588	22,269,588	22,269,588
High (XETRA)	EUR 10.64	EUR 13.53	EUR 20.80
Low (XETRA)	EUR 5.41	EUR 7.14	EUR 9.90
Closing price at year's end (XETRA)	EUR 6.95	EUR 7.20	EUR 10.83
Market capitalization at year's end	EUR 154.77 million	EUR 160.34 million	EUR 241.2 million
Average daily trading volume (shares)	51,993	100,182	159,169
Earnings per share, diluted	EUR – 0.40	EUR – 0.16	EUR 0.38
Dividend per share[1]	EUR 0.00	EUR 0.00	EUR 0.12

1 2016: Proposal at Annual General Meeting

DIALOGUE WITH SHAREHOLDERS, ANALYSTS, AND THE BUSINESS MEDIA

Eight road shows with institutional investors and analysts.

Openness in communication with the capital markets was another hallmark of the 2016 financial year. LPKF AG participated in a total of 78 talks. CEO Dr. Ingo Bretthauer and CFO Kai Bentz spoke with institutional investors and analysts from Germany, the UK, Switzerland and Luxembourg at eight road shows. Five of the events took place in Germany, while the remaining three were organized abroad. LPKF's shares are regularly analyzed by seven banks.

Shareholders are still keenly interested in our company. Over 400 shareholders accepted the invitation to the Annual General Meeting held in Hannover on 2 June 2016. In direct discussions with the members of the Management Board and Supervisory Board, investors acquired knowledge of our company's economic situation and of its short- and long-term prospects.

The strong commitment of individual shareholders is impressive. Some of them have held investments in the Company for a long time now. Investing clubs visit LPKF in Garbsen to gain an even better insight into our company on-site.

LPKF also maintains regular contact with journalists for financial and business publications. Many regional and national media regularly reported on developments at the Company and the performance of its shares. One-on-one interviews with the CEO are actively offered by LPKF even in difficult times in order to provide shareholders with a comprehensive, independent picture of the Company.

IR CONTACT

LPKF AG's website is an important platform for providing comprehensive and transparent information. Existing and potential shareholders can also contact LPKF personally with their questions. All information on the Company is available online at www.lpkf.com. In addition, the Investor Relations department can be contacted at the following address:

LPKF Laser & Electronics AG
Bettina Schäfer
Investor Relations Manager
Tel. +49 5131 7095-1382
investorrelations@lpkf.com

CORPORATE GOVERNANCE REPORT

SUSTAINABLE VALUE CREATION AND EFFICIENT COLLABORATION

Corporate governance stands for responsible corporate leadership and management aimed at increasing the shareholder value in the long term; purposeful and efficient collaboration between the Management Board and the Supervisory Board; consideration for the interests of shareholders and employees; transparency and responsibility in all corporate decision making; as well as appropriate risk treatment. LPKF follows the German Corporate Governance Code (GCGC).

The actions of the LPKF Group's management and supervisory bodies are guided by the principles of responsible and good corporate governance. The Management Board reports on issues of corporate governance in this chapter – also on behalf of the Supervisory Board – pursuant to Article 3.10 of the German Corporate Governance Code. This chapter also contains the corporate governance declaration pursuant to Sections 289a and 315 (5) of the German Commercial Code (Handelsgesetzbuch – HGB). For the remuneration report, please see page 54 of the combined management and Group management report.

CORPORATE GOVERNANCE DECLARATION

1. PROCEDURES OF THE MANAGEMENT BOARD AND THE SUPERVISORY BOARD

LPKF AG is an enterprise incorporated according to German law, on which the German Corporate Governance Code is based. The dual management system comprising the Management Board and the Supervisory Board as corporate bodies, both of which have distinct responsibilities, is a fundamental element of German corporate law. The Management Board and the Supervisory Board of LPKF AG work together closely and in an atmosphere of trust in managing and supervising the Company. The Management Board of LPKF AG consists of four members. They are responsible for managing the Company's business in the interests of the Company and with the aim of creating sustainable value. The Supervisory Board set a target of 0% for the share of women on the Management Board to be fulfilled by 30 June 2017 since no changes in the composition of the Management Board are planned at present.

In accordance with the German Act on the Equal Participation of Women and Men in Executive Positions in the Private and the Public Sector, the Management Board also laid down a target for the share of women in the two management levels below the Management Board: 17% in each case. The deadline set for achievement of this target is 30 June 2017.

The Supervisory Board advises and monitors the Executive Management Board with regard to its management of the Company. The Supervisory Board is integrated in corporate strategy and planning, as well as all aspects of fundamental importance to the Company. The rules of procedure require the Management Board to obtain the approval of the Supervisory Board for significant business transactions. The Chairman of the Supervisory Board coordinates the work of the Supervisory Board, chairs its meetings and represents the Supervisory Board externally.

The Management Board informs the Supervisory Board in a timely and comprehensive manner – both in writing and at regular meetings – of the Group's planning, performance and situation, including risk management and compliance. Extraordinary Supervisory Board meetings are convened as necessary in connection with material events. The Supervisory Board adopted rules of procedure for its own work.

For all members of its Management Board and Supervisory Board, LPKF AG has taken out a D&O insurance policy subject to a deductible corresponding to 10% of the damage but no more than one-and-a-half times the fixed annual remuneration.

The Supervisory Board of LPKF AG currently consists of three members. At the most recent Supervisory Board election during the Annual General Meeting on 5 June 2014, the Supervisory Board members were elected individually as recommended by the German Corporate Governance Code. The term of office of the Supervisory Board members runs until the 2019 Annual General Meeting. All election proposals concerning potential Supervisory Board members shall consider the expertise, abilities and professional experience that are required for carrying out the respective tasks as well as issues of diversity. For its proposals to the Annual General Meeting for the election of new Supervisory Board members, the Supervisory Board makes sure that the candidates in question can devote the requisite amount of time to the Company.

According to Article 5.4.1 GCGC, the Supervisory Board shall disclose specific objectives with regard to its composition in view of the Company's international activities, potential conflicts of interest, an age limit to be specified for Supervisory Board members, a regular limit of length of membership to be specified for the members of the Supervisory Board, the independence of Supervisory Board members and diversity, and disclose the status of implementation in the corporate governance report.

To this end, the Supervisory Board formulated the following objectives regarding its composition:

a) Addressing the international nature of the Company's activities

The international activities of LPKF Laser & Electronics AG have been reflected to date in the participation of shareholder representatives in the Supervisory Board and will continue to be addressed in the future in nominations of candidates by the Supervisory Board to the Annual General Meeting. In addition to the ability to speak and write English, the measure here is the professional experience acquired in other German and foreign companies with international operations, whether in management or supervisory bodies, and the understanding of global economic issues. The criterion of internationality does not stipulate that the Supervisory Board's composition include one or more Supervisory Board members holding foreign citizenship. Instead, German citizens can also contribute this desired experience.

b) Avoiding potential conflicts of interest

Potential conflicts of interest should be avoided as early as when the Supervisory Board nominates candidates to the Annual General Meeting. With the exception of the Supervisory Board's Deputy Chairman, who was Chairman of the Management Board of LPKF AG until December 2008, no former LPKF Management Board members sit on the Supervisory Board. In addition, when candidates are proposed to the Annual General Meeting, attention is paid to ensuring that the relevant candidate does not hold a management or advisory position or a position on the supervisory body of competitor companies, suppliers, creditors or clients in order to prevent conflicts of interest from the start. If conflicts of interest arise during a Supervisory Board member's term, the respective Supervisory Board member must disclose this to the Supervisory Board to the attention of the Chairman. In the event of material, not just temporary, conflicts of interest, the member must step down from his or her position.

c) Specifying an age limit

The age limit for members of the Supervisory Board was set at under 70 years at the time of election by resolution of the Supervisory Board on 22 January 2014.

d) Specifying a regular limit of length of membership for the members of the Supervisory Board

To ensure a balanced mix of experience and new members on the Supervisory Board, the Supervisory Board specified a regular limit of 10 years for the average length of membership for the members of the Supervisory Board based on the date of their election.

e) Independence of Supervisory Board members

The Supervisory Board, currently with three members, must have at least two members who are independent within the meaning of the German Corporate Governance Code. All current members of the Supervisory Board can be classified as being independent.

f) Diversity

The composition of the Supervisory Board of LPKF Laser & Electronics AG should reflect as broad as possible a spectrum of professional expertise and experience in various areas relevant to the Company.

g) Target for the share of women on the Supervisory Board pursuant to Section 111 (5) German Stock Corporation Act

The Supervisory Board at its meeting on 26 January 2016 adopted a resolution to specify a target for the share of women on the Supervisory Board of 25% to be fulfilled by 30 June 2017.

Both the Management Board and the Supervisory Board are obliged to observe the corporate interests of LPKF AG. There were no conflicts of interest in the financial year just ended that would have had to be disclosed to the Supervisory Board without delay. No member of the Management Board held more than three appointments to the supervisory boards of listed stock corporations not belonging to the Group.

The status of implementation of the objectives regarding the composition of the Supervisory Board outlined in a) to g) above is as follows:

The objectives relating to a) "Addressing the international nature of the Company's activities," b) Avoiding potential conflicts of interest," c) "Specifying an age limit," d) "Specifying a regular limit of length of membership for the members of the Supervisory Board," e) "Independence of Supervisory Board members" and f) "Diversity" have already been achieved. Target g) "25% share of women on the Supervisory Board" has not yet been achieved because as of the end of the reporting period there has not yet been a vacancy on the Supervisory Board. The Supervisory Board intends to stick to its target of having a 25% share of women on the Supervisory Board even after 30 June 2017. According to the current planning, this target is to be taken into account by finding a suitable female candidate in connection with the regular election of the entire Supervisory Board by the Annual General Meeting in 2019. The term of office of the Supervisory Board members is five years, and the current term ends with the Annual General Meeting in 2019.

2. CORPORATE GOVERNANCE REPORT

LPKF implements the recommendations and suggestions of the German Corporate Governance Code apart from a few exceptions. The Management Board and the Supervisory Board jointly issued the 2017 Declaration of Compliance on 21 March 2017 pursuant to Section 161 German Stock Corporation Act (Aktiengesetz). The Declaration is permanently made public on LPKF AG's website.

Declaration of Compliance of LPKF Laser & Electronics AG for the 2017 financial year with the Corporate Governance Code in accordance with Section 161 German Stock Corporation Act (Aktiengesetz)

The Management Board and the Supervisory Board of LPKF Laser & Electronics AG declare that since the most recent Declaration of Compliance dated 22 March 2016 the recommendations of the Government Commission on the German Corporate Governance Code as amended on 5 May 2015, have been observed. LPKF will continue to comply with these recommendations. The following exceptions apply:

No severance pay cap agreed for Directors' contracts in case of premature termination of a Director's contract (Article 4.2.3 (4) and (5) GCGC).

Because they only run for a maximum of three years, the Directors' contracts do not contain a cap on severance pay. If a Director's contract is terminated prematurely without cause, remuneration is limited to no more than the remaining contractual period. The Supervisory Board therefore considers it unnecessary to include in the Directors' contracts a cap on severance pay amounting to two years remuneration.

Formation of Supervisory Board committees (Article 5.3.1 and 5.3.2 GCGC)

Given that it has three members, the Supervisory Board of LPKF Laser & Electronics AG does not form any committees.

3. SHAREHOLDERS AND ANNUAL GENERAL MEETING

The shareholders of LPKF AG exercise their co-determination and control rights at the General Meeting, which takes place at least once per year. It resolves all matters determined by law with binding effect on all shareholders and the Company. Each share grants one vote at the Annual General Meeting.

Every shareholder who registers in due time has the right to participate in the Annual General Meeting. Shareholders who cannot or do not want to attend in person have the option of appointing a bank, a shareholders' association, the proxies appointed by LPKF AG who are bound by instructions, or any other agent as their proxy to exercise their voting right.

The notice of the Annual General Meeting as well as the reports and information required for the resolutions are published in accordance with the requirements of German corporate law and are also made available on LPKF AG's website in both German and English.

4. RISK MANAGEMENT

The responsible handling of business risks is an integral part of all good corporate governance. The Management Board of LPKF AG is supported in its work by a comprehensive Group-wide reporting and control system that makes it possible to record, assess and manage risks of this kind. This system is continuously refined, adjusted to changing parameters, and audited by the auditors of the financial statements. The Management Board informs the Supervisory Board on a regular basis of existing risks and their development. The risk report contains details of the LPKF Group's risk management. The risk report is part of the Group management report and contains the report on the accounting-related internal control and risk management system pursuant to the German Commercial Code.

5. TRANSPARENCY

LPKF regularly, immediately and simultaneously informs the participants in the financial markets and interested members of the public about the commercial situation of the Group and any new facts. The annual report, the half-yearly financial report and the quarterly financial reports are published within the specified deadlines. Press releases, and ad hoc announcements where stipulated, provide information on current events and new developments. All of the information is published in printed form and via suitable electronic media such as email and the Internet. The www.lpkf.com website also provides comprehensive information on the LPKF Group and LPKF shares.

A financial calendar lists the scheduled dates for the most important regular events and publications such as the Annual General Meeting, annual report, quarterly financial reports, financials press conference and analyst conferences. The calendar is published well in advance of the scheduled events and is made available permanently on the LPKF AG website.

6. SHARE TRANSACTIONS OF MEMBERS OF THE COMPANY'S CORPORATE BODIES

Reportable directors' dealings were published on the Company's website and reported to the competent supervisory authorities. A listing of the shares held by members of the Company's corporate bodies is shown in the remuneration report.

7. ACCOUNTING AND AUDITING

LPKF AG prepares its consolidated financial statements and its interim consolidated financial statements in accordance with the International Financial Reporting Standards (IFRS) as applicable in the European Union. The annual financial statements of LPKF AG are prepared in accordance with the German Commercial Code. The consolidated financial statements are prepared by the Management Board, audited by the auditor of the financial statements and reviewed by the Supervisory Board. The interim reports and the half-yearly financial reports are discussed by the Supervisory Board and the Management Board before publication. The consolidated financial statements and the annual financial statements of LPKF AG were audited by PricewaterhouseCoopers GmbH Wirtschaftsprüfungsgesellschaft, Hannover, the auditor elected by the 2016 Annual General Meeting. The audit reports were signed by German public auditors Jens Wedekind (since the 2016 annual financial statements) and Prof. Dr. Mathias Schellhorn (since the 2013 annual financial statements). The audits were conducted in accordance with German auditing standards and taking the generally accepted German standards for the audit of financial statements promulgated by the Institute of Public Auditors (IDW) into account. The International Standards on Auditing were also taken into account. The audits also assessed the risk management and compliance with the reporting obligations defined for proper corporate governance pursuant to Section 161 German Stock Corporation Act.

LPKF AG also entered into a contract with the auditor pursuant to which they must notify the Supervisory Board immediately, while the audit is in progress, of any grounds for excluding them, any partiality on their part as well as any material findings and events. Nothing of this nature arose in the course of the audit covering the 2016 financial year.

8. COMPLIANCE – PRINCIPLES GOVERNING CORPORATE ACTIONS AND BUSINESS ACTIVITIES

Acting in compliance with the principles of corporate, environmental and social sustainability in accordance with applicable law is an indispensable element of LPKF's corporate culture. This includes trust, respect and integrity in interactions with other people, values expressed in exemplary behavior vis-à-vis employees, business partners, shareholders and the public. LPKF's understanding of compliance includes observing all laws, statutes and the Articles of Incorporation, complying with internal regulations, and honoring voluntary obligations.

LPKF AG considers it particularly important to raise the awareness of compliance among all of the Group's employees, to entrench compliance in the internal processes (for example, through adherence to the principle of dual control) and to build a compliance structure for the Group that makes compliance guidelines binding on all LPKF employees worldwide and is suitable for effectively preventing compliance violations for the benefit of the Group as a whole.

Training for employees was offered in connection with the Group-wide compliance code to familiarize employees with the goal of this code of conduct and to guarantee uniform ethical and legal standards throughout the entire Group.

The Compliance Office holds regular meetings to discuss current topics, some times in the presence of the technical officers.

Reliable reporting channels for internal and external stakeholders help to ensure that possible irregularities are reported confidentially to carry out an objective and comprehensive investigation. Internal auditing is also used for this purpose. To obtain knowledge of any possible compliance violations, LPKF makes the following contact channels available to internal and external whistleblowers: Email address of the Compliance Manager (compliance@lpkf.com). Employees who feel it necessary to have an anonymous and confidential conversation when submitting such reports also have the opportunity to contact LPKF Laser & Electronics AG's independent legal counsel. The legal counsel for LPKF AG is lawyer Dr. Carsten Thiel von Herff, Thiel von Herff law firm, Bielefeld. He has been responsible for providing legal counsel to LPKF since 1 March 2017 and can be contacted as follows: Tel: +49 (0)521 5573330, Mob.: +49 (0)151 58230321, Email: vertrauensanwalt@thielvonherff.de. Additional employee contact details can be found in the Compliance Code, on the intranet and on notices posted at the Company.

Internal training on compliance and liability issues was provided to the Management Board, Supervisory Board and managing directors of the subsidiaries as part of the strategy meeting in October 2016.

An online anti-corruption training session has been prepared for around 80 employees in the LPKF Group's Purchasing and Sales departments and will be held in the first quarter of 2017. This training concerns the "United Nations Convention against Corruption" and explores several issues, including dealing with gifts, facilitation payments and corruption, use of intermediaries/lobbyists, corruption/social investments and insider information.

Internal auditing, which is performed by an international audit firm functioning as a third-party service provider, plays a key role in the compliance organization. The relevant audits are also used to update the internal control system.

Dr. Ingo Bretthauer — Bernd Lange — Kai Bentz — Dr.-Ing. Christian Bieniek

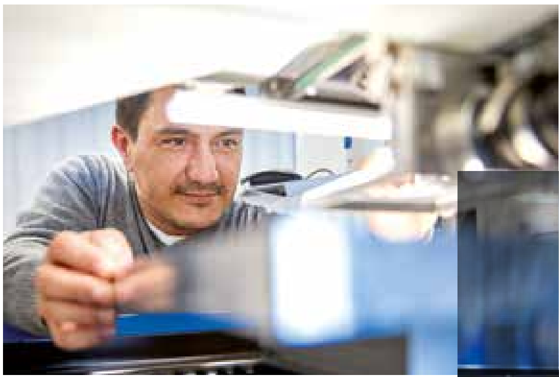
LPKF AS AN EMPLOYER

Laser industry offers exciting possibilities for professionals

ATTRACTIVE JOBS IN THE LASER INDUSTRY

LPKF employees can continue their education by taking advantage of various training opportunities

After a slight correction in financial year 2015, the trend toward rising employee numbers was abruptly halted in 2016. Unfortunately, we were forced to cut jobs due to the economic situation. The LPKF Group's workforce therefore declined from 778 to 700. We now feel that we are well positioned to become profitable again and return to a growth trajectory in the long term. It is now all the more important to promote unity among our employees and continue to offer an attractive working environment. As before, the pioneering power of laser technology is our major selling point, offering plenty of future potential and attracting a great many specialists and executives to our company.



Skilled and motivated employees are the key to success

Professional and personal development are important to our employees

CONTINUING EDUCATION AND LEADERSHIP SKILLS

We continued to focus our efforts on personnel development and implemented various training and continuing education measures for technical specialists and executives. Employees can refer to our training catalog to select from the training options offered to help them do their jobs better. Other focal points are the development of leadership skills and the promotion of young talent. For instance, in 2016, LPKF again brought on board 13 trainees in various professions.

More information about training and continuing education opportunities and the leadership culture at LPKF is provided in sections 2.3.4 and 2.3.5 of the management report starting on page 49.

MOTIVATION AND WELL-BEING

We want our employees to feel well-cared for at LPKF. We therefore supplement our options for personal development by emphasizing a strong sense of community – even over regional boundaries. This is constantly renewed by our regular group activities – a motorcycle tour, a skiing event attended by colleagues from all over the world or Christmas parties at various sites. Employee health is another area to which we devote our attention at LPKF. We use various programs here to promote our employees' well-being, motivation and general health and fitness.

More information about the working environment at LPKF is provided in section 2.3.7 of the management report on page 50.

SKILLED AND MOTIVATED EMPLOYEES AS THE KEY TO SUCCESS

A successful company needs skilled and motivated employees. We too have to face the challenge of finding suitably-qualified personnel, and we do so by employing a number of strategies. The high standards we set for our company in the technological and financial realms also apply to selecting our employees. LPKF is a highly attractive employer – which is reflected in the large number of applications that have reached us despite the difficult economic situation. But for us, that's not nearly enough. In order to attract and retain good employees, we work tirelessly on further improving our reputation as an attractive employer among small- and medium-sized mechanical engineering firms.

Detailed information on LPKF as an employer is provided in section 2.3 of the management report starting on page 48.

COMBINED MANAGEMENT REPORT 2016

OF THE LPKF GROUP AND LPKF AG

I. FUNDAMENTAL INFORMATION ABOUT THE GROUP

1.1 GROUP STRUCTURE AND BUSINESS MODEL

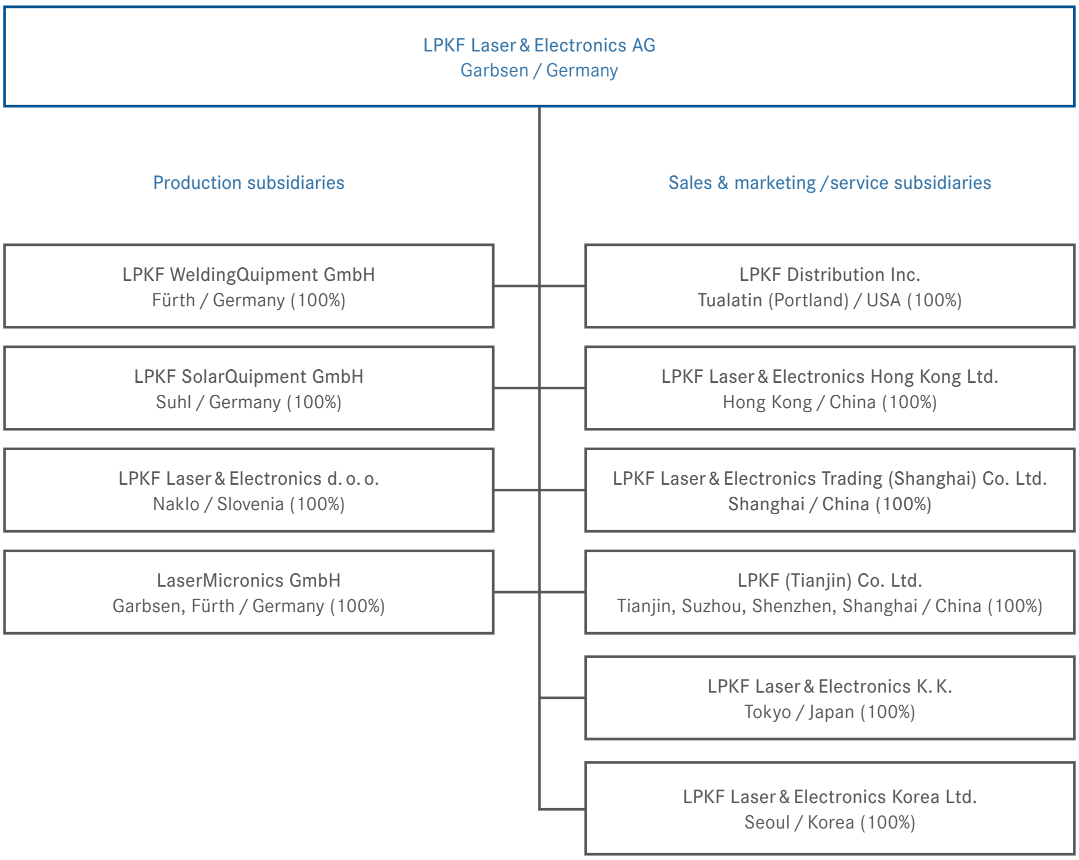
LPKF is one of the leading laser technology companies worldwide

The LPKF Group develops and produces material processing systems. The mechanical engineering company has become one of the world's leading laser technology providers on the strength of its technical leadership in a number of areas of laser micro material processing. The LPKF Group has specialist know-how in the fields of laser technology, optics, precision drive systems, control technology and software as well as materials engineering. LPKF's laser systems are used primarily in the electronics industry, in polymer technology applications and for the manufacture of solar panels. In many sectors, the innovative processes developed by LPKF replace established techniques. The Group generates 86% of its revenue abroad. The Group had 700 employees worldwide on the reporting date. LPKF Laser & Electronics AG (LPKF AG) is listed in the Prime Standard segment of the German Stock Exchange.

1.1.1 Legal structure of the Group

In financial year 2016, a profit and loss transfer agreement was signed between LPKF AG and LPKF WeldingQuipment GmbH. Other than that, the legal structure of the LPKF Group did not change. As of 31 December 2016, LPKF AG had ten subsidiaries, which together with the parent company form the basis of consolidation.

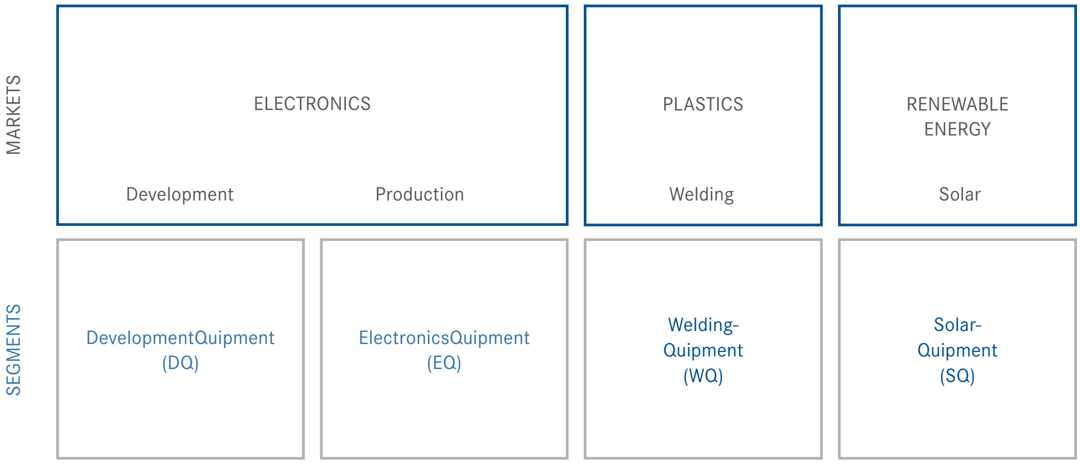
GROUP STRUCTURE



The companies are headquartered at the locations mentioned first in each case.

Domiciled in Garbsen, near Hannover, Germany, LPKF AG carries out top-level Group functions such as strategic business development and innovation management and performs core activities in the areas of management accounting, investor relations, HR, accounting, legal, internal audit, risk management, marketing, strategic purchasing and management systems. Sales and marketing, service, production and development work is handled by separate business units per segment. In LPKF's most important markets outside Germany, sales and service functions are provided by sales and service subsidiaries in close collaboration with business unit management.

MARKETS AND SEGMENTS



1.1.2 Operating segments

LPKF was active in four segments in financial year 2016

LPKF was active in the following four segments in financial year 2016.

DevelopmentQuipment

In the **DevelopmentQuipment** (DQ) segment, LPKF supplies almost everything required by developers of electronic equipment to manufacture and assemble printed circuit board prototypes largely without the use of chemicals. In addition to the development departments of industrial customers, the Company primarily supplies public organizations such as research institutes, universities and schools. Customers in this segment mainly make their purchasing decisions on the basis of their available budget.

ElectronicsQuipment

The following product groups comprise the **ElectronicsQuipment** (EQ) segment. In the SMT Equipment product group, LPKF supplies StencilLasers for print stencil cutting and UV laser systems for circuit board depaneling. The PCB Equipment product group includes UV laser systems for cutting and drilling flexible circuit boards. The MID equipment product group mainly comprises laser systems and process expertise for the production of molded interconnect devices (MIDs) using the laser direct structuring (LDS) method patented by LPKF. In the ICP Equipment group, LPKF supplies laser systems for the high-precision drilling of ultra-thin glass (laser-induced deep etching, LIDE).

WeldingQuipment

WeldingQuipment (WQ) comprises laser systems for welding plastic components. These systems are primarily used by the automotive supply industry, medical technology and in the production of consumer electronics.

SolarQuipment

In the **SolarQuipment** (SQ) segment, LPKF develops and produces LaserScribers for the structuring of thin-film solar cells. Its customers are mainly solar cell manufacturers. This segment also includes laser systems for the digital printing of functional pastes and inks (laser transfer printing, LTP).

All other segments

The all other segments category mainly includes undistributed costs and income.

1.1.3 Competitive position

LPKF strives to become at least the number two in all markets

In the segments in which it is active, the Group either is already market and technology leader or number two in the market. As a rule, LPKF strives to become at least the number two in new markets. LPKF competes with an entirely separate set of competitors in each segment and in each product group. These groups of competitors range from multinational corporations to smaller, regional providers, who are often active in only a single market.

1.1.4 Primary locations

Germany

Garbsen: Group headquarters, production, development, sales & marketing and services – The activities of LPKF in Garbsen focus on the EQ segment.

Fürth: Production, development, sales & marketing and services – In Fürth (WQ segment), LPKF develops and produces plastic welding systems.

Suhl: Development, sales & marketing, production and services – The activities of LPKF in Suhl focus on the SQ segment.

Slovenia

Naklo: Production, development and services – The Slovenian subsidiary concentrates on the manufacturing of products for the DQ segment and on the development and production of laser sources.

USA

Portland, Oregon: Sales & marketing as well as services – The subsidiary in Portland is responsible for sales and marketing as well as services in North America.

China

Shanghai, Shenzhen, Suzhou, Tianjin: Sales & marketing as well as services – The Shanghai branch is the Company's headquarters in China and ensures sales & marketing as well as services within metropolitan Shanghai. The other sites in the country serve the further key economic urban areas in China.

Hong Kong: Services – Because a large portion of revenue is generated in Asia, it is very important for LPKF to maintain competent and timely services in the region. Hong Kong operates as a service location, particularly for Asian countries without local service capacity.

Japan

Tokyo: Sales & marketing as well as services – Established in 2010, the subsidiary in Tokyo provides sales support to local distributors and is in the process of establishing its own customer base in the EQ, WQ and SQ segments. The Japanese market possesses great significance for LPKF owing to its technological position.

Korea

Seoul: Sales & marketing as well as services – Besides China and Taiwan, South Korea is one of the most important markets for laser technology. The Company's subsidiary in Seoul provides a local service to South Korean customers while developing new business.

There is a further site in Malaysia (Penang). The business activities previously handled by the offices in Beijing and Chengdu have now been reassigned to other Chinese sites.

1.1.5 Production and procurement

Rapid Prototyping Equipment and other equipment for the DQ segment, as well as some of the laser sources used within the Group, are supplied by the subsidiary LPKF Laser & Electronics d.o.o. in Naklo (Slovenia). Systems for the EQ segment are mainly manufactured in Garbsen. Welding equipment is produced in Fürth, Germany. Solar module equipment and LTP systems are produced in Suhl. LPKF generally acquires no complete systems from third parties. If system components are purchased from outside the Group, several suppliers are available in most cases. A large portion of the procurement volume involves a relatively small number of suppliers.

1.1.6 Sales & marketing

The Group is represented in 73 countries

Global sales & marketing, especially in important regions such as China, Japan and North America are handled by subsidiaries. Overall, the Group is represented by subsidiaries or distributors in 73 countries. Distribution, sales and marketing activities for the DQ and EQ segments are managed by the Garbsen office. The WQ and SQ segments are managed by the subsidiaries in Fürth and Suhl.

1.1.7 Management and control

Organization of management and control

The Management Board represents the Company and is responsible for running it. The members of LPKF's Management Board are appointed by the Supervisory Board. The Supervisory Board may withdraw appointments for cause. The Supervisory Board determined that certain transactions require its approval. The Annual General Meeting may only decide on management issues if requested to do so by the Management Board. Any amendment to the Articles of Incorporation requires a resolution by the Annual General Meeting to be passed with a majority of the share capital represented at the adoption of the resolution. Article 25 (1) of the Company's Articles of Incorporation stipulates that in cases where the law requires that a resolution be passed by a majority of the share capital represented, a simple majority of the share capital represented is sufficient, unless the law mandates a larger majority.

The following persons were members of the Management Board of LPKF AG in financial year 2016:

- Dr. Ingo Bretthauer as chairman of the Management Board (CEO)
- Kai Bentz (CFO)
- Dr.-Ing. Christian Bieniek (COO)
- Bernd Lange (CTO)

In the 2016 financial year, the Supervisory Board consisted of the following members:

- Dr. Heino Büsching (Chairman)
- Bernd Hackmann (Deputy Chairman)
- Prof. Dr.-Ing. Erich Barke

1.1.8 Legal factors

The Company and each of its segments are subject to the general legal requirements applicable to listed companies. Over and above this, no special legal provisions apply.

1.2 STRATEGY

1.2.1 Strategic Framework

Vision

Electronic components are increasingly becoming smaller, more complex and more precise. The complexity of components is increasing due to advances in miniaturization and the growing use of nanoscale materials. This trend of miniaturization necessitates innovative processing methods that enable precision to a degree never before achieved. Laser-based processes will contribute substantially to this development.

Mission

With its products, the LPKF Group wants to help its customers improve the efficiency of their development and production activities. Developing and continually improving laser-based processes and products is intended to replace conventional processes and create new processing options.

Corporate responsibility

For the LPKF Group, sustainability means acting with responsibility, achieving economic success as well as both ecological and social progress while working to secure the future of the Company.

Mission statement

All activities of the LPKF Group are geared toward the success of its customers. All activities and decisions are aimed at improving the competitiveness of the Group's customer base through technical advancement and cost savings. Strengthening LPKF in the long term serves the interest of all customers, business partners, employees and shareholders. Management therefore emphasizes strengthening the Group's innovation resources and ensuring profitability.

LPKF is a technology group. LPKF shapes technological progress and gains leading market positions through the strength of its superior technical solutions. LPKF concentrates its efforts on products with the potential to become market leader or at least number two in the market. A sense of professional partnership characterizes relationships with customers, suppliers and representatives as well as the working relationships among employees within the LPKF Group. As an internationally active group, LPKF strives for understanding various cultures and philosophies and always places the Group's interests above those of its individual subsidiaries.

The high product quality is the key to customer satisfaction

The high quality of its products is the key to customer satisfaction. All employees shoulder responsibility for the quality of the work the LPKF Group does for its customers. LPKF promotes the professional qualifications of its employees to sustain the high quality of LPKF products.

With laser-based technology, LPKF helps to reduce the environmental impact generated by chemical waste. LPKF designs its products and internal processes as eco-friendly as possible. Health and well-being are the foundation for success. LPKF pays special attention to both occupational safety and promoting the health of its employees. As a technology leader, LPKF always strives to optimize its products and the processes necessary for their development. It goes without saying that this requires a corporate culture that is open and encourages learning and constructive criticism. LPKF's responsibility extends to its customers, employees, business partners, shareholders and the public. Being a good corporate citizen includes obeying applicable laws at all times and everywhere, respecting ethical principles and pursuing sustainability. The LPKF Compliance Code supports the Company's employees in this endeavor.

Success factors

LPKF specializes in innovative mechanical engineering solutions, primarily laser-based systems.

The Group's success is based on its understanding of laser microprocessing of different materials. A key factor of success is the LPKF's focus on core competencies and the interplay between them:

Core competencies
- Laser technology and optics
- Precision drive systems
- Control technology and software
- Materials technology

Other success factors include close relationships with customers and a thorough understanding of the core markets of electronics, automotive, solar and medical technology.

1.2.2 Corporate Goals, Objectives and Action Areas

Corporate goals

LPKF aims for healthy revenue growth

The Group's fundamental, overarching corporate goal is to increase the value of the Company in the long term. The Group's technical edge is continually sharpened to achieve this goal. A strong emphasis on R&D work is of central importance. Furthermore, a solid financial basis with a high equity ratio contributes towards achieving this goal. LPKF aims for healthy expansion with average annual revenue growth of 10%. Profitability over the long term should reach an EBIT margin of 10 – 15% per year, while the net working capital ratio should be lower than 35%.

Strategic objectives

The Company's long-term activities for reaching the top-level corporate goals are mainly grouped into three strategic objectives:

- Increasing customer benefit
- Driving innovation
- Boosting efficiency

Strategic action areas

The interplay of corporate goals and strategic objectives results in the following 12 action areas:

Basically:

1. Development of the Group and strengthening of its financial position

The Group's efforts are focused on the welfare of the Group as a whole. In order to ensure and advance the Group's welfare, LPKF supports the individual strategic objectives.

Increasing customer benefit:

2. Optimizing the existing product portfolio

The product portfolio is continually being reworked and overhauled

The product portfolio is continually being reworked and overhauled. In this context, LPKF aligns its efforts with changing customer needs and updates its products and processes to ensure it always offers its customers the best price-performance ratio. Closely networking the Company's development departments with market research, sales and service, and providing an R&D budget averaging 10% of revenue over a five-year period make a significant contribution to reaching this goal.

3. Optimizing product structure

Growth and the increasing complexity of products as well as cooperation across the Group place high demands on the product structure. Using economies of scale and Group-wide best practices is intended to further increase profitability. All products are regularly reviewed with the aim of justifying their continued existence.

4. Increasing and guaranteeing quality

Quality is a central value of LPKF products along with cost-efficiency. Rapidly offering customers stable machines suitable for volume production in view of frequently short development cycles requires LPKF to continually improve its ability to avoid defects, detect them, rectify them and learn from them.

5. Enhancing customer proximity

Strengthening key account management will enable the entire Group to respond to the demands of major international customers. The industry-specific expertise of individual segments should also be utilized to an even greater extent across segments.

Driving innovation:

6. Attaining technological leadership

The Company will further strengthen its technology management to systematically manage and co-ordinate the collective use of its resources. In addition to its own R&D activities, the LPKF Group will develop new processes and products for future markets in cooperation with universities and institutes as well as in joint projects with industry partners.

7. Expanding the business base

LPKF will expand its business base in the interest of minimizing its financial dependence on individual product lines and sectors and therefore reducing the risk and effects of economic volatility. This comprises both further penetration of established markets as well as the development of new sectors and areas of application to which the Company can transfer existing processes and products, e. g., through cross-selling activities within the Group.

8. Extending services and products to all development and manufacturing processes

For future products, the Group will try to extend its “product” beyond purely the machine to offer customers a complete process to solve their technical issues.

Boosting efficiency:

9. Improving the basis for making decisions

At LPKF, decision-making is analytical and structured, and uses standardized ratios as much as possible.

10. Breathing organization and establishment of lean concepts

To avoid activities that do not create value, LPKF institutes a culture of continual improvement and in accordance with lean principles throughout the Group.

11. Reinforcing cooperation across business units and sites

Within the Group, LPKF will network its capacity and potential and thus exploit these optimally. LPKF is focused on harmonizing processes and structures across the Group, thereby creating long-term added-value in all units of the Company.

12. Systematic personnel development

Personnel development is essential for the Company’s success

Personnel development is essential for the Company’s success in the long term. Continued systematization of key HR processes is a working priority within the LPKF Group.

1.2.3 Corporate management

LPKF manages its business performance using key performance indicators (KPI) and ratios at various reporting levels. The following section outlines the key figures LPKF uses.

At segment level, the financial indicators and ratios applied are revenue, earnings before interest and taxes (EBIT) and the EBIT margin. At Group level, LPKF also looks at net working capital, the net working capital ratio and the error rate. LPKF has developed targets for these financial indicators and ratios through strategic and operational planning processes, and these are reviewed annually. The applicable targets for the reporting period are listed along with the time series.

EBIT: The corporate goal of profitable growth can be reviewed by analyzing revenue in conjunction with EBIT. The EBIT margin is also given as a ratio and is calculated using the following formula: EBIT margin = EBIT / revenue x 100.

Net working capital: It is calculated by using inventories and current trade receivables less current trade payables and advances received. This KPI reflects the net capital tied up in the reported items.

Net working capital ratio: It is the ratio of net working capital to revenue. Generally, when business grows, net working capital also increases.

Error rate: This is the ratio of error costs to revenue. Error costs comprise expenditure associated with the fulfillment of warranty obligations and quality assurance. The aim is to lower the error rate in the Group calculated in 2013 by 50% within three years, i. e. by the 2016 financial year, and to keep it constant after that. The error rate calculated in the 2013 financial year is indexed at 100, thus establishing an error cost index.

Other than the error rate, no significant non-financial key performance indicator was used for controlling the Group in the 2016 financial year. Explanatory notes on the non-financial performance indicators for the LPKF Group are given in the Sustainability Report (chapter II).

The Group's control system remains in place

The Group's control system remains in place with no modifications.

The following table presents the changes in the Group's key financial figures over the past five years and the applicable target figures:

	Target 2016	2012	2013	2014	2015	2016
Revenue (EUR million)	100 – 120	115.1	129.7	119.7	87.3	91.1
EBIT (EUR million)	1 – 11	20.4	23.2	12.7	– 3.7	– 6.8
EBIT margin (%)	1.0 – 9.0	17.7	17.9	10.6	– 4.3	– 7.4
Net working capital (EUR million)	< 42	44.6	37.3	50.1	40.3	35.2
Net working capital ratio (%)	< 35	38.8	28.7	41.9	46.2	38.7
Error rate (%)	50	–	100	71	60	73

Target / Actual comparison of planning and realization

At the beginning of 2016, the Management Board expected a significant improvement in business performance with revenue growth to between EUR 100 million and EUR 120 million and a single-digit EBIT margin (guidance from 11 November 2015). After first-quarter results in which revenue was below expectations, the Management Board corrected the annual guidance on 2 May 2016 to between EUR 90 million and EUR 110 million. At the same time, comprehensive restructuring measures were announced to lower the break-even point for the following year to below EUR 90 million. On 12 May 2016, the Company confirmed the revenue guidance for 2016 and corrected the earnings guidance due to the expected restructuring expenses of up to EUR 2 million in the context of the planned downsizing measures to an EBIT margin of between – 3% and + 6%.

In October 2016, the Company used an ad hoc disclosure to announce impairment losses in the amount of between EUR 6 million and EUR 6.5 million and specified the existing guidance. The Management Board now expected that revenue and EBIT, excluding extraordinary items from the write-downs, would both be at the lower end of the guidance.

With revenue of around EUR 91 million in the 2016 financial year, the Group achieved the lower end of the guidance. This result is affected by extraordinary items totaling EUR 8.5 million, however. If one eliminates the extraordinary items, including the income from an insurance reimbursement of EUR 1.3 million, this results in positive EBIT of EUR 0.4 million for the financial year. The adjusted EBIT margin is 0.5% and therefore also within the most recent guidance.

Net working capital was reduced to EUR 35.2 million, primarily due to write-downs of inventories and specific measures taken to reduce working capital. As a result, the net working capital ratio fell to 38.7%, although missing the long-term goal of < 35%. The quality costs target, measured by error rate, was also not achieved.

1.2.4 Strategic orientation of operating business

For LPKF, the most important megatrend is miniaturization in the electronics industry

With its focus on micro material processing with a laser as the tool, LPKF supplies an important and advanced technology for many growth industries. The Company's broad portfolio of products and services contributes to boosting efficiency and thus conserving resources. LPKF is a strategic partner for international customers, with whom it works closely to design advanced solutions. For LPKF, the most important megatrend is miniaturization in the electronics industry. This trend continues unabated and is also being accelerated further by the use of LPKF technologies.

LPKF is positioned as a global laser specialist. From this vantage point, LPKF enjoys many advantages over competitors, who are often only active in one market or who act only as regional players. Since LPKF addresses a range of markets, it therefore reduces its dependence on the cycles in individual industries, making it easier to compensate for economic fluctuations. This approach requires the integration of business processes with potential synergies. LPKF has made further progress in this area in the past year.

Infrastructure and interdepartmental functions within the LPKF Group are used jointly by all of the segments. Examples include development or procurement activities, or use of the international sales network. Since segments share sites, this means that LPKF can cater to local service and sales business in key regions throughout the world. Shared use of infrastructure also simplifies market entry while helping to ensure optimization of the cost base by exploiting synergy effects.

Strategic alignment of the segments

In the DQ segment, LPKF addresses a global market with many individual customers

The **DQ** segment offers its customers the entire value chain for the manufacturing of circuit board prototypes. The core focus is on mechanical and – increasingly – laser-based systems that undergo continuous enhancement. In the DQ segment, LPKF addresses a global market with many individual customers from manufacturing and universities. Many customers invest on the basis of an R&D budget. DQ can draw on a worldwide network of agents, who are in many cases longtime partners of the Company and able to secure outstanding options for market entry. DQ is seen as relatively stable business. Despite a large market share of around 75%, the Management Board sees solid growth rates in this segment due to new products and applications. As one example, LPKF has offered micromachining systems for research use outside circuit board prototyping since 2016. This offers an opportunity to open up a new part of the market for electronics development.

The **EQ** segment addresses markets associated with the production and processing of circuit boards and electronic circuits. LPKF acts in a highly dynamic market offering opportunities for generating short-term revenue but with the risk that innovations will not be accepted by the market as soon as expected. EQ offers its customers systems for cutting, structuring and drilling a wide variety of materials at high speed and with outstanding precision. LPKF also has a major presence in its target market of Asia with wholly-owned subsidiaries and a global network of strong partners. Particularly in the field of production machinery, after-sales service is one of LPKF's major competitive advantages.

In the **WQ** segment, LPKF develops, produces and markets laser systems for welding plastics. This segment primarily targets the automotive supplier industry, medical technology and manufacturers of consumer electronics. Laser welding offers the opportunity to replace traditional methods of joining materials in many sectors, thereby creating a sizable market potential. Since this is not a conventional niche market, competitive pressure is much more substantial. LPKF's primary competitive differentiators are its superior product quality, its wealth of process know-how, its shorter lead times and its global service network.

Major orders from a single customer are a key feature of the **SQ** segment. Thanks to many years of working with this customer, LPKF has reached a leading position within the thin-film solar market. The precision and the speed of the Allegro systems are some of LPKF's key differentiators in the solar energy market. In 2016, LPKF was able to acquire new orders from other customers, which indicates a slight upturn in the solar market. LPKF is attempting to reduce its dependency on this single customer in the SQ segment. One approach being pursued is developing new markets outside the solar industry with the LTP method. With its new LTP technology, LPKF is addressing the market for printing functional pastes. There is potential here to replace the predominant screen printing method.

LPKF's strategy for growth also includes the continuous development and optimization of its product portfolio. Here, the Company is not only orienting its development work on market trends but is also pursuing its own concepts and innovations. Once a year, all products are reviewed with the aim of justifying their continued existence.

1.2.5 Group structure, equity investments and financing measures

The Group regularly examines whether it is necessary to adapt the Group structure to changing market conditions. LPKF's strong equity base provides financial security and stability and enables the Company to pursue the long-term enhancement of its products and business. As of the reporting date, 85% of LPKF's shares were held as free float in accordance with the definitions of Deutsche Börse AG. As a result of business developments, stabilizing Company financing was a top-priority objective in the 2016 financial year. The Company has access to various unused lines of credit. A number of opportunities for raising equity are also still available. The Management Board believes there is sufficient financial scope for further development of the business.

Stabilizing Company financing was a top-priority objective in the 2016 financial year

1.3 RESEARCH AND DEVELOPMENT

1.3.1 Focus of R&D activities

Research and development (R&D) is of considerable significance for LPKF as a technology company. Innovations decisively influence the future capabilities of the LPKF Group – and hence the business success of the Company. The primary strategic goal of R&D activities is to acquire, secure or develop the Company's role as an innovation leader within the sectors in question. Another focus is developing products with key differentiators and safeguarding these with patents. With this approach, LPKF can help boost customer profitability.

While the LPKF Group has focused on the systematic expansion of its product offering in recent years, changing economic conditions have resulted in last year's R&D activities being concentrated on finalizing LIDE and LTP development work as quickly as possible. Work has also been stepped up on further developments to the technology and building-block system for the plastic welding business. In order to continue providing inspiration for new ideas and technology over the medium and long term, the Group has expanded its activities in this area as part of publicly funded projects.

1.3.2 R&D expenses, R&D capital expenditures and R&D key figures

Continuous investment in near-to-market developments are of crucial importance

Continuous investment in near-to-market developments are of crucial importance to a technology-oriented Group such as LPKF. Development expenses in 2016 amounted to EUR 11.4 million, which is equivalent to 12.5% of revenue. LPKF capitalized EUR 4.9 million (previous year: EUR 6.2 million) in development expenses as intangible assets in the reporting year, which equates to a capitalization ratio of 43% (previous year: 63%). Amortization of capitalized development expenses in 2016 amounted to EUR 3.0 million (previous year: EUR 1.3 million). This also included write-downs of discontinued development projects in the amount of EUR 0.8 million.

Capital expenditures for development in the 2016 financial year focused on measuring machines and laboratory equipment.

1.3.3 R&D staff

The number of employees in the Group's R&D departments fell to 159 during the reporting period, up from 179 the previous year.

1.3.4 R&D results

Work in the DQ segment in 2016 included the development of a ProtoLaser for research applications. The first systems were sold at the end of the year.

In the SQ segment, the first printer based on the LTP process for digitally printing functional pastes was developed as a customer commission.

In the WQ segment, the PowerWeld 3D 8000 marked the development and production of a new system for welding large 3D parts. A new software package for controlling laser welding systems with 3D CAD data was also developed.

The following multi-period overview of R&D shows the development of key figures:

	2012	2013	2014	2015	2016
R&D expenses in EUR million[1]	10.0	13.5	11.1	9.9	11.4
in % of revenue	8.7	10.4	9.3	11.3	12.5
R&D staff	144	165	171	179	159

1 This figure shows the effect of R&D expenses on consolidated net profit.

II. CORPORATE RESPONSIBILITY

2.1 SUSTAINABILITY AT LPKF

2.1.1 Sustainability management, rules and objectives

For LPKF, increasing the long-term value of the Company has top priority

For LPKF, increasing the long-term value of the Company has top priority as the fundamental overarching corporate goal. Other goals are subordinate to this goal – and thus to the Company's focus on long-term planning. The measures taken to reduce costs and secure financing in the 2016 financial year support this long-term focus. This is how LPKF lays the groundwork for sustainability as part of its corporate strategy. Due to its size, the Company does not yet carry out explicit sustainability management; the full Management Board, management and staff are responsible for sustainability issues.

The LPKF Group's action areas can be grouped into four overarching sustainability aspects: value creation, employees, society and the environment.

Value creation: Increasing customer benefit, driving innovation, boosting efficiency

Employees: Attractive and responsible employer, occupational health and safety

Society: Value creation and active involvement in each region

Environment: Nature and resource conservation, replacing chemical production methods

The Company's corporate responsibility rules and targets are defined in several different documents, including: Strategy Paper, LPKF Mission Statement, Risk Management Handbook, Management Handbook, process descriptions, Compliance Code, German Corporate Governance Code and LPKF Executive Code of Conduct. At the strategy meeting on 17 and 18 October 2016, the Management Board and Supervisory Board of LPKF AG defined corporate responsibility in the 2017+ Strategy Paper. The Investor Relations department is responsible for reporting.

The Mission Statement of the LPKF Group is present at all branches and was reviewed and determined to be valid as part of a workshop on the topic of corporate culture at the management meeting held on 16 June 2016.

2.1.2 Stakeholder orientation

As a listed B2B company, LPKF maintains a dialog with a number of stakeholders with different demands of the Company. LPKF firmly believes that regularly exchanging information with different stakeholder groups is vitally important for the public and internal perception of the Company. Corporate communications are aimed at all of the Company's major stakeholder groups. These include customers, employees and the Works Council, analysts, shareholders and investors, bank representatives, suppliers, municipalities, authorities and policymakers.

Examples of stakeholder communication in 2016

External:
- Annual Report 2015
- Quarterly reports 2016
- Ad-hoc and press releases
- Press interviews
- lpkf.com website
- Annual General Meeting
- Road shows
- Analyst conferences
- Conference call for investors

Internal:
- Works and employee meetings
- Executive meetings
- Open lunch with the Management Board for employees
- “LPKF Journal” employee magazine
- Intranet

2.2 ECONOMIC RESPONSIBILITY

Due to the sharp decline in revenue, it was necessary to significantly lower the cost base in 2016

Economic responsibility for the Company and its employees is at the heart of the business activities of the LPKF Group. Due to the sharp decline in revenue in the LDS business, it was necessary to significantly lower the cost base in 2016. As part of these efforts, a total of 103 FTEs (full-time equivalents) were cut across the Group and further costs reduced. Local works councils were intensively involved in this process. Reducing the workforce was extremely painful but essential for the future viability of the Company. Further business development information for 2016 can be found in the report on economic position in chapter III of this management report as well as in the consolidated financial statements and notes.

2.3 RESPONSIBILITY FOR EMPLOYEES

2.3.1 Personnel strategy and corporate culture

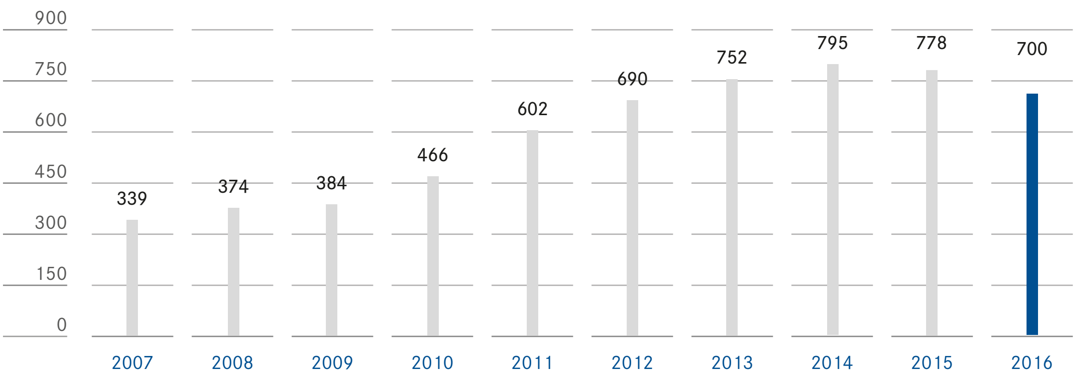
Attracting and retaining qualified staff is essential for the long-term success of the Company. In a growing and learning organization, demands on employees also change continually. LPKF seeks to address this issue with Group-wide staff development programs. Talent is being identified and promoted in a lasting way. This includes supporting and promoting international employee exchanges within the Group. LPKF maintained its commitment to these strategic objectives even amid a difficult economic environment in 2016, implementing the corresponding measures in a measured way. The support of executives when managing capacity adjustments posed an additional challenge in 2016.

Due to country-specific factors, operational human resources work is carried out autonomously in the international units. However, LPKF AG intensively involves the Group function in strategic issues. At the Company’s German sites, numerous human resources activities are available in bundled form via the shared services approach. Processes that have historically been characterized differently have been and continue to be harmonized gradually.

2.3.2 Workforce development

The number of employees was significantly reduced during the financial year as a result of the Company’s weak economic performance, falling from 778 in the previous year to 700 as of 31 December 2016. Additional departures were agreed with 28 employees prior to the reporting date. The Group’s workforce was reduced by a total of 103 FTEs. This significant cut was necessary to considerably reduce the Group’s cost base and thus lay the foundations for new profitable growth.

NUMBER OF EMPLOYEES IN THE LPKF GROUP FROM 2007 – 2016
(AS OF THE 31 DECEMBER REPORTING DATE)



While LPKF has a relatively young workforce – the average age is just 39 – it is nonetheless proud to have offered many of its employees continuous job security for several decades or more. Due to the workforce reduction, the employee turnover rate is 15.9%.

Almost all of the trainees are offered a permanent position at the end of their training period. The goal is to employ well-qualified staff and technicians at the Company for as long as possible.

2.3.3 Employee recruitment

As before, laser technology is a major selling point attracting many specialists to LPKF

As before, the pioneering power of laser technology is a major selling point, offering plenty of future potential and attracting a great many specialists and executives to LPKF. This is demonstrated by the high number of unsolicited applications received by the Company in 2016 despite the difficult economic situation.

The Company signed cooperation agreements with schools as part of its efforts to recruit and nurture young talent. In addition to funding school activities, LPKF will take on student interns with a view to possibly offering them a vocational traineeship later on. The tried-and-tested award of university scholarships was continued in 2016. Some of the scholarship holders, who in the past wrote their bachelor’s or master’s thesis at LPKF, have already received permanent contracts.

Despite the difficult economic situation, LPKF AG’s efforts in this area continued unabated in 2016. One important task for the Management Board and executives is to make the workforce aware of the prospects and opportunities the Company offers in order to motivate and retain many of its experienced employees.

2.3.4 Training and continuing professional development

Young professionals are a crucial investment for the future. LPKF therefore trains a constant stream of young people across a range of professions, including mechatronics, industrial management, applied IT systems, product design and technical drawing. In the long term, industry will see a shortage of MINT qualifications (mathematics, information technology, natural sciences, technology). This bottleneck is essentially a structural problem that must be considered an impediment to growth and innovation. LPKF addresses this bottleneck with solid vocational training. Special emphasis is placed on the level of commitment and motivation shown by the trainees.

Staff training and continuing professional development (CPD) are a key part of any sustainability policy. As a result, LPKF places considerable emphasis on providing employees and executives with targeted support. CPD was systematized further in 2016 with the help of the training catalog developed in 2015. Other training courses are aimed at management staff and are designed to offer them support for their leadership roles.

For capable, dedicated and high-achieving staff, LPKF offers a wide range of career prospects and options for professional development. In addition to its standard programs, LPKF offers especially dedicated and talented staff additional professional development options, which are discussed in regular appraisal meetings held between the employee and their supervisor. Goals agreed here may include project work, a personal training plan or career-integrated courses of study. In this way, all employees get the chance to fully develop their potential at LPKF.

2.3.5 Management culture

Executives' behavior shapes corporate culture to a considerable extent

In light of the significant reduction in the Company's workforce, it was especially important during the last financial year to motivate the remaining and employees and provide them with security and prospects within the Group. Management played a key role in this process. Executives serve as role models whose behavior shapes corporate culture to a considerable extent. In 2016, many of the Company's executives were faced with the challenge of having to part with capable, qualified employees and completing the tasks ahead with fewer staff. Various management events were particularly important in this regard, enabling executives to exchange experiences, discuss proposed solutions and develop communication strategies. The LPKF Executive Code of Conduct also provides individuals with guidance for their own actions.

2.3.6 Diversity and equal opportunities

The wide variety of cultures, skills and potential among employees is of utmost importance for the success of an international group like LPKF. LPKF has sites in seven countries around the globe (Germany, USA, Slovenia, China, Japan, Korea and Malaysia). Since members of staff often work with colleagues from different regions, they get the chance to experience life in other countries and gain intercultural skills. This often proves useful when liaising with foreign clients. The considerable diversity of LPKF's cultural base is matched by the balanced nature of its age structure: The sound experience contributed by longtime employees is enhanced by the bold ideas of junior talent.

2.3.7 Attractive working environment

Two factors make working at LPKF particularly attractive. The first is the fascination of laser technology, which attracts many engineers, mechatronics specialists and technicians. The second is the fact that many employees at LPKF can clearly see how their contributions add value to the Company's products.

The objective is to ensure that employees feel comfortable at LPKF. LPKF therefore supplements its options for personal development by emphasizing a strong sense of community – even over regional boundaries. The Group offers a wide range of activities launched by employees to foster a sense of community. These include events such as a motorcycle tour, ski trip, children's picnic or on-site Christmas parties. Time and again, there are chances to get to know one another and share experiences even across national borders. For ten years, LPKF has also had its very own dragon boat crew, which takes part successfully in competitive racing. Activities such as these make integration easier for new employees.

Employee health is equally important to LPKF. The Company uses various programs here to promote well-being, motivation and general health and fitness. In 2016 there were several events enabling staff and management to take part in workshops and lectures or compete with others in running events, for example. Employees also had the opportunity to have several preventive medical check-ups by Company physicians. While economic performance resulted in cuts to staff numbers in 2016, the Group was able to implement its workforce reduction measures in a socially acceptable manner.

2.4 RESPONSIBILITY FOR SOCIETY

LPKF can only succeed in a functioning social environment. The Company is committed to exploring possibilities at its different sites, where most initiatives are planned and implemented by employees in coordination with management at each site. In the Hannover area, LPKF supports the Tier hilft Mensch ("Animals Help People") foundation established by Company founder Bernd Hildebrandt with an annual family day on the Foundation's premises and by making a donation. The Group has also been making charitable contributions to the Médecins sans Frontières (MSF) organization for many years.

For a technology company like LPKF, encouraging young people with science and education is essential. The Group supports three scholarship students at the Hannover University of Applied Sciences in the areas of mechatronics, applied computer science and electrical engineering. LPKF strives to act and be perceived as an active and valuable member of society and responsible neighbor. The Company is also a member of Stifterverband für die Deutsche Wissenschaft e. V., a German organization seeking to address challenges in higher education, science and research.

2.5 RESPONSIBILITY FOR THE ENVIRONMENT

Environmental protection is an integral part of LPKF's business activities

Environmental protection is an integral part of LPKF's business activities and is embodied in the Group's strategy and Mission Statement. Laser technology generally involves lower tool costs and more energy-efficient operations. It enables flexible, resource-friendly production processes and the economical manufacturing of electronic components.

As a technology leader and pioneering innovator, LPKF's work naturally prioritizes product development. Its laser-driven technology is displacing chemical processes in many industries and making an active contribution to reducing the volume of scrap and waste at customers. One such area is PCB prototyping, which LPKF systems can now handle as a zero-chemical process. The copper swarf produced is removed with air extraction systems that incorporate filters to avoid polluting the environment. In another process, PCB depaneling, LPKF technology is reducing the mechanical loads to which work parts are subjected. This substantially reduces the volume of scrap – especially for soft or flexible materials. Laser plastic welding is another technology that is enabling cost-effective, resource-friendly production. This is made possible by a process that avoids the use of adhesives or other additives, merely requiring a set of simple workpiece clamps. Use of the LPKF laser structurers has made it possible to significantly increase the conversion efficiency of thin-film solar modules.

The production of high-tech systems does not generate significant quantities of waste, while water and energy consumption are also low. Nevertheless, LPKF works along the entire value chain to continually optimize its use of energy and resources.

The Group regularly reviews its energy consumption. When making investments in buildings and plants, consideration is given to how energy can be saved. The employee car park constructed at the Garbsen site in 2010 was clad in thin-film solar modules that provide the local power grid with solar energy. During 2016, the power supply at LPKF's German sites was largely converted to green electricity.

III. REPORT ON ECONOMIC POSITION

3.1 OVERVIEW OF THE COMPANY'S DEVELOPMENT

3.1.1 Macroeconomic environment

According to a study by the Kiel Institute for the World Economy (IfW), the global economy grew by 3.1% during the 2016 financial year. This rise was slightly weaker than in 2015 and the lowest growth rate since the crisis year of 2009. On a positive note, during the past year the global economy passed the lowest point of the weak period of performance experienced in recent years, with analysts now forecasting slightly increased economic growth.

Developed economies recorded moderate economic performance in 2016 despite an increase in production growth, with the US economy expanding at a relatively low rate of 1.6%. The eurozone economy continued to grow moderately in 2016 with a 1.7% rise in gross domestic product (GDP). According to the IfW, the fact that every country in Europe is finally contributing to the region's economic growth is a positive development. With an 1.9% increase in GDP according to the German Federal Statistical Office, the German economy continued its recovery in 2016, based primarily on domestic construction investments and consumption. Despite the Brexit vote, economists expected the United Kingdom's economic output to increase by 2.0% in 2016. As a result, the short-term effects of Brexit were minor.

Emerging markets have gained economic momentum since the summer. This trend was particularly driven by China, whose economic output rose by 6.6% as a result of the country's expansionary economic policy.

Economists believe that commodities prices remained low in 2016 due to the still relatively low price of oil. Expansionary monetary policy in some countries also contributed to economic development.

3.1.2 Sector-specific environment

The business development of laser technology specialist LPKF AG is characterized by the overall economic situation, the performance of various sectors, its high export share and other international factors. Key sectors such as the automotive, electronics – particularly consumer electronics – solar and plastics processing industries are of particular importance for the Group.

The following section addresses the performance of these sectors during the 2016 financial year.

The VDMA recorded a drop in incoming orders of 2% in 2016

The German Engineering Federation (Verband Deutscher Maschinen- und Anlagenbau – VDMA) recorded a drop in incoming orders of 2% in 2016. The main contributing factor to this decline was the lack of a year-end rally leading to a 15% reduction in orders in December compared to the end of 2015. The uncertainties created by Brexit and the US presidential election seem to have triggered caution among customers. In the full year 2016, domestic incoming orders decreased by 1%, while new orders from outside Germany declined by 3%. Fewer orders came from eurozone countries in particular (8%), while the remaining foreign markets amounted to a decline of just 1%. This strongly export-driven sector was still assuming a stagnation in incoming orders in the third quarter of 2016.

According to the German Automotive Industry Association (Verband der Automobilindustrie – VDA), 2016 was another good year for international automotive markets. 4.5 million more passenger cars were sold in the major sales markets of China, USA and Western Europe. In China, the passenger car sales volume rose by approximately 18% to 23.7 million vehicles in 2016, while in the USA this figure rose by 0.4% to 17.5 million units, with both countries thus recording new record highs. In Western

Europe, the world's third-largest automotive market, new registrations increased by 6% to 14.0 million vehicles. Japan recorded an almost 2% decline in registrations to 4.1 million vehicles, Brazil's sales volumes fell by 20% to 2.0 million passenger cars and Russia posted an 11% fall to 1.4 million units.

The global photovoltaics market also expanded in 2016. According to the German Solar Industry Association (Bundesverband der Solarwirtschaft, or BSW), total installed capacity rose by 30% to 300 gigawatts (GW). In particular, China – by far the largest solar market – doubled its added capacity in 2016. According to Bloomberg New Energy Finance, however, lower installation prices – partially helped by lower module prices – led to a 32% fall in investment volume to USD 116 billion. The share of thin-film technology is stagnating. This technology is represented by a small number of major producers.

In the consumer electronics segment, worldwide smartphone deliveries in 2016 fell to 1.888 billion devices (2015: 1.917 billion units) according to Gartner. One main reason for this was signs of saturation in important markets such as the USA, Europe, Japan and some Asian regions. According to Gartner, there are almost 7 billion mobile telephones, tablets and PCs currently in use. Smartphones now form the majority of this figure, making up over 80% of deliveries by units in 2016.

The German Plastics Processing Industry Association (Gesamtverband Kunststoffverarbeitende Industrie – GKV) forecasts slight growth for the sector in Germany in 2016 compared to the previous year. Revenues had reached a record high of approximately EUR 60 billion in 2015.

3.1.3 Effects on the LPKF Group

The macroeconomic environment slightly improved by emerging from a low point after a sustained period of restrained economic growth for LPKF AG in 2016. The sectors relevant to the Company exhibited different trends during the financial year ended. While the solar industry continued to show growth despite lower investment volumes and the automotive industry set a new record in 2016, the smartphone market continued to stagnate and the engineering sector even reported a drop in orders at the end of the year due to changing economic conditions in the USA and United Kingdom. The performance of the euro against other key currencies was positive for LPKF's exports.

The weak business performance in the 2016 financial year cannot be attributed to the macroeconomic environment

The overall weak business performance of the LPKF Group during the 2016 financial year cannot not largely be attributed to economic conditions in the markets. As in the past, some segments are more dependent (WQ, DQ) and others less dependent (SQ, EQ) on their respective markets. The primary reason for the Company's weak revenue growth in 2016 was the further decline in revenues in the LDS business. There were also negative effects for the WQ segment from the USA and for the DQ segment from China as well as product launches carried out later than planned.

3.2 DISCLOSURES RELATED TO ACQUISITIONS

The takeover-related disclosures required under Section 289 (4) and Section 315 (4) German Commercial Code are shown below.

On 31 December 2016, the share capital of LPKF AG amounted to EUR 22,269,588.00. The share capital is divided into 22,269,588 ordinary shares (no-par shares). No preferred shares have been issued. One no-par share represents a pro-rata interest of EUR 1.00 in the share capital. The rights and duties under the no-par shares comply with the relevant requirements of the German Stock Corporation Act, specifically, in Sections 12, 53a ff., 118 ff. and 186. Both the exercise of voting rights and the transfer of shares are subject solely to statutory limits.

Direct or indirect interests in the share capital exceeding 10% of the voting rights are disclosed in the consolidated notes.

The regulations on appointing and dismissing members of the Management Board, as well as on amending the Articles of Incorporation, comply with the respective requirements of both the German Stock Corporation Act and the Articles of Incorporation. Complementing Sections 84 and 85 of the German Stock Corporation Act, Article 7 of the Company's Articles of Incorporation governs the Management Board's composition as follows: The Management Board shall comprise at least two members. Deputy members of the Management Board may be appointed. They have the same rights as the regular members of the Management Board when representing the Company vis-à-vis third parties. The Supervisory Board shall determine the number of both regular and deputy members of the Management Board and appoint them, enter into director's contracts with them as well as dismiss them. Likewise, the Supervisory Board may also appoint a member of the Management Board to serve as its chairperson or speaker and appoint additional Management Board members to serve as deputy chairpersons or speakers.

Under Sections 133 and 179 German Stock Corporation Act, in conjunction with Article 25 (1) of the Company's Articles of Incorporation, the latter may only be amended by resolution of the Annual General Meeting, which must be adopted by the simple majority of the share capital represented at the Meeting unless larger majorities are required by law. The Supervisory Board is authorized under Article 12 (2) of the Articles of Incorporation to make amendments that affect solely the given wording.

3.3 REMUNERATION REPORT

Compensation of the Management Board

Basic features of the remuneration system

The system of Management Board remuneration at LPKF Laser & Electronics AG is set up to provide an incentive for successful and sustainable corporate management.

Remuneration of the Management Board is performance-based

The Supervisory Board of LPKF Laser & Electronics AG fixes and regularly reviews the overall structure of the remuneration of the Management Board as well as the key elements of the respective director's contracts. When determining the appropriate amount of remuneration for the members of the Management Board, the Supervisory Board focuses on the Company's size and activities, its economic and financial position as well as on the responsibilities and performance of the respective Management Board member, the success and future prospects of the Company, and the customary level of the remuneration under consideration of the level of executive remuneration at peer companies and the remuneration structure in place in other parts of the Company. The relationship between the remuneration of the Executive Board and that of senior management and the workforce overall is taken into account also in terms of its development over time, whereby the Supervisory Board determines how senior managers and the workforce are to be defined for the purposes of the comparison. The remuneration of the members of the Management Board is based on performance and calculated such that it is both appropriate and competitive, offering an incentive for committed and successful work. The remuneration system was approved by the Annual General Meeting on 5 June 2014 with a majority of 93%.

The overall remuneration of the members of the Management Board comprises a non-performance-based fixed component and variable performance-based components. These remuneration components are explained in more detail below.

Non-performance-based components

The fixed remuneration comprises both the base salary, which is paid in equal monthly installments, and benefits. The incidental benefits include a company car for both official and private use, as well as insurance contributions for individual members of the Management Board, particularly in connection with health and legal insurance.

Performance-based components
The variable remuneration components comprise both long-term incentives (LTI) and short-term incentives (STI).

The remuneration components Quality (LTI 1), Options (LTI 2) and Long-term EBIT (LTI 3) are designed as long-term incentives while EBIT (STI 1) and EBIT per employee (STI 2) are designed as short-term incentives. The LTI 1, LTI 3, STI 1, and STI 2 remuneration components are based on targets whose achievement is decisive for the amount of the remuneration component in question.

Short Term Incentives (STI)
STI 1 and STI 2 are each calculated based on the corporate planning approved prior to the beginning of a given financial year, in which the targets for EBIT and EBIT per employee are set for three different future scenarios (normal, aggressive, and defensive). A target achieved in the financial year under the normal scenario constitutes a target achievement in accordance with the target value shown in the benefits table and, under the defensive scenario, a target achievement of 0% (minimum). The maximum target achievement shown in the table is calculated when the planned aggressive scenario is exceeded by at least 20%. The scenarios are based on ambitious targets, which means that the maximum can only be reached if the targets are significantly overachieved. There is linear interpolation between the individual values. If negative EBIT is reported for the following year, in certain circumstances the given loss may be taken into account retroactively.

Long Term Incentives (LTI)
Safeguarding product quality at the highest level is one of the strategic action areas of LPKF Laser & Electronics AG. LTI 1 (Quality), which will run for three years, is measured by the achievement of these quality specifications. The aim is to lower the error rate in the Group calculated in the 2013 financial year by 50% by 2016 and maintain this improved rate thereafter. Target achievement is calculated based on three-year averages. If the error rate is not reduced, this constitutes a target achievement of 0%. The target achievement is calculated by means of linear interpolation between the initial value and the minimum value of the error rate.

For the variable multi-year remuneration components LTI 1 (Quality), the Company will make advance payments at the end of a given financial year based on the level of target achievement of the error rate at the end of the financial year. If the advance payments shown under allocations exceed the entitlement to variable remuneration under LTI 1, the Management Board members will be required to pay the excess.

A long-term bonus plan was established as LTI 2 (Options). Details are laid down in the plan's terms and conditions, which are part of the contractual arrangements with the Management Board members. Decisive factors for the amount of LTI 2 are the development of the EBIT margin of the LPKF Group and the share price performance. LTI 2 is therefore directly tied to the pursuit of the Group's objectives of profitable growth and a long-term increase in the enterprise value.

In detail, LTI 2 is designed as follows: Fictitious shares, known as phantom stocks, are granted to the Management Board members in a contractually stipulated amount, which for Chief Executive Officer Dr. Ingo Bretthauer is EUR 50 thousand and for the Management Board members Kai Bentz, Dr. Christian Bieniek and Bernd Lange EUR 25 thousand. The number of phantom stocks granted to a single Management Board member will be calculated based on the set amount to be granted divided by the average closing price of the shares of LPKF Laser & Electronics AG over the last 30 trading days prior to 1 January of the year in which the shares are allotted. After the expiry of a four-year performance period, the beneficiaries will be entitled for the first time to a disbursement amount whose calculation will depend on the final number of phantom stocks. The final number of phantom stocks will be calculated by multiplying the preliminary number of phantom stocks by a performance factor that is determined by the average EBIT margin of the LPKF Group during the relevant performance period. The amount to be paid out will in turn be calculated by multiplying the final number of phantom stocks by the average share price of LPKF Laser & Electronics AG on the last 30 trading days before the end of the relevant performance period. This is capped at three times the amount to be granted, the maximum shown in the benefits table. If the beneficiaries waive their right to a disbursement after the four-year performance period, they can obtain the amount to be paid out after a five- or six-year performance period. One prerequisite for a disbursement under the long-term bonus plan is an own investment in the form of shares of LPKF Laser & Electronics AG, which must correspond to at least half of the amount to be granted.

From 2016 onwards, the Directors' contracts have in included an additional long-term remuneration component, LTI 3 (Long-term EBIT), which is intended to replace STI 2 in future. Annual payments are calculated based on target achievement in accordance with STI 1 (EBIT) for the respective financial year, the prior financial year and the financial year before that.

Cap

Each of the components of variable performance-based remuneration has a maximum amount (cap). As a rule, the STI 1 remuneration component is only paid if Group EBIT amounts to at least EUR 9 million (floor). This floor will be replaced by an EBIT margin of at least 5% in the Directors' contracts from 2016 onwards. This floor was also agreed on a one-off basis for Dr. Bretthauer for the 2017 financial year to establish the same targets for all members of the Management Board when calculating remuneration.

Due to the economic situation, the Management Board and Supervisory Board agreed a reduction in variable remuneration for the 2017 financial year.

It was therefore agreed that there would be no entitlement to any of the variable remuneration components in the event of an EBIT margin of less than 5%. The calculation of STI 1 EBIT was also changed so that otherwise identical operating results generate lower values than under the previous contractual provisions: In the range of the aggressive scenario up to 5% EBIT margin, values decline on a straight-line basis, so that the target achievement amounts to 0% at 5% EBIT margin. The resulting provisional bonus amount is then reduced by 20% to give the final STI 1 EBIT amount.

Value of the benefits in the reporting period

The Management Board of LPKF Laser & Electronics AG opted to forgo the performance-based elements of their remuneration for the 2016 financial year. Members of the Management Board are thus making a personal contribution to the ongoing cost reduction measures at LPKF.

The remaining benefits for the 2016 reporting period are presented in the table below, supplemented by the minimum and maximum amounts that can be reached. The multi-year variable remuneration granted in the past is broken down according to various plans and the length of the respective periods is indicated. The target value of a moderately probable scenario is stated for LTI 1 and the fair value at the grant date is stated for LTI 2. This was determined with the help of an option price model based on Black / Scholes.

BENEFITS GRANTED (PLAN)

	Dr. Ingo Bretthauer Chief Executive Officer (CEO)				Bernd Lange Chief Technology Officer (CTO)				Kai Bentz Chief Financial Officer (CFO)				Dr.-Ing. Christian Bieniek Chief Operating Officer (COO)				Total
EUR thsd.	**2015**	**2016**	**(Min)**	**(Max)**	**2015**	**2016**	**(Min)**	**(Max)**	**2015**	**2016**	**(Min)**	**(Max)**	**2015**	**2016**	**(Min)**	**(Max)**	**2016**
Fixed remuneration [1]	325	325	325	325	243	243	243	243	203	213	213	213	210	210	210	210	991
Incidental benefits	38	40	40	40	22	23	23	23	18	20	20	20	20	20	20	20	103
Total	**363**	**365**	**365**	**365**	**265**	**266**	**266**	**266**	**221**	**233**	**233**	**233**	**230**	**230**	**230**	**230**	**1,094**
One-year variable remuneration																	
STI 1 (EBIT)	152	152	0	203	94	94	0	156	79	79	0	138	79	79	0	158	404
STI 2 EBIT per employee	49	49	0	81	38	38	0	63	32	32	0	55	32	n/a	n/a	n/a	119
Multi-year variable remuneration																	
LTI 1 Quality (3 years)	73	73	0	122	56	56	0	94	47	47	0	83	47	47	0	79	223
LTI 2 Options 2015 (4 years)	66	n/a	n/a	n/a	33	n/a	n/a	n/a	33	n/a	n/a	n/a	33	n/a	n/a	n/a	n/a
LTI 2 Options 2016 (4 years)	n/a	50	0	150	n/a	25	0	75	n/a	25	0	75	n/a	25	0	75	125
LTI 3 Long-term EBIT (3 years)	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	55	0	79	55
Other																	
Total	**340**	**324**	**0**	**556**	**221**	**213**	**0**	**388**	**191**	**183**	**0**	**351**	**191**	**206**	**0**	**391**	**926**
Cost of benefits [1]	0	0	0	0	7	7	7	7	7	7	7	7	0	0	0	0	14
Total remuneration	**703**	**689**	**365**	**921**	**493**	**486**	**273**	**660**	**419**	**423**	**240**	**591**	**421**	**436**	**230**	**621**	**2,034**

1 According to the contracts, the cost of benefits is part of fixed remuneration.

Allocations for the reporting period

In compliance with the recommendations of the German Corporate Governance Code (GCGC), the fixed remuneration and incidental (fringe) benefits are stated in the table below. The waiver by the Management Board members of their performance-based remuneration components in financial year 2016 does not result in allocations from the one-year variable remuneration components or from multi-year variable remuneration since none of the plan terms of LTI 2 ended in the reporting period. Following the recommendations of the GCGC, the benefit costs correspond to the committed contributions to old-age pensions, although they do not represent an allocation in the narrow sense.

The current members of the Management Board received a total remuneration of EUR 1,108 thousand (2015: EUR 1,462 thousand) for their activities in the 2016 financial year, EUR 1,094 thousand of which can be attributed to fixed remuneration components, including incidental benefits, that were fully paid out in the 2016 reporting period.

A total of EUR 0 thousand can be attributed to variable remuneration components.

ALLOCATIONS (ACTUAL)

EUR thsd.	Dr. Ingo Bretthauer Chief Executive Officer (CEO) 2015	2016	Bernd Lange Chief Technology Officer (CTO) 2015	2016	Kai Bentz Chief Financial Officer (CFO) 2015	2016	Dr.-Ing. Christian Bieniek Chief Operating Officer (COO) 2015	2016	Total 2016
Fixed remuneration	325	325	243	243	203	213	210	210	991
Incidental benefits	38	40	22	23	18	20	20	20	103
Total	**363**	**365**	**265**	**266**	**223**	**233**	**230**	**230**	**1,094**
One-year variable remuneration									
STI 1 (EBIT)	0	0	0	0	0	0	0	0	0
STI 2 EBIT per employee	0	0	0	0	0	0	0	0	0
Multi-year variable remuneration									
LTI 1 Quality (3 years)	117	0	94	0	79	0	79	0	0
LTI 2 Options (4 years)	0	0	0	0	0	0	0	0	0
Other									
Total	**117**	**0**	**94**	**0**	**79**	**0**	**79**	**0**	**0**
Cost of benefits	0	0	7	7	7	7	0	0	14
Total remuneration acc. to GCGC (allocation)	**480**	**365**	**366**	**273**	**307**	**240**	**309**	**230**	**1,108**
Share-based remuneration acc. to GCC / GAS 17 (for LTI 2 Options)	66	0	33	0	33	0	33	0	0
Total remuneration acc. to GCC / GAS 17 (allocation)	**551**	**365**	**399**	**273**	**340**	**240**	**342**	**230**	**1,108**

Commitments to members of the Management Board upon termination

Post-contractual non-competition agreements have been made with the members of the Management Board in the event their activities as such are terminated, irrespective of whether it is an ordinary or extraordinary termination. Under these agreements, the Company shall pay remuneration equivalent to 50% of the respective individual's most recent average base salary for the 12-month term of the post-contractual non-competition agreement unless the individual in question is retiring.

If the appointment of a member of the Management Board ends early on account of his or her death while in office, the fixed monthly remuneration shall be paid to the heirs for a six-month period.

The Company has not made any defined-benefit commitments to the current members of its Management Board. Contracts regarding a company pension were closed with the members of the Management Board, Kai Bentz and Bernd Lange. These are defined-contribution commitments. No provisions for pensions are required in this case.

No other provisions and commitments have been made with respect to the ordinary or extraordinary termination of a member of the Management Board.

Total remuneration of former members of the Management Board

Provisions were recognized for EUR 511 thousand (previous year: EUR 520 thousand) in pension commitments (pension plan, disability pension and widow's pension) toward former members of the Management Board and their survivors.

A total of EUR 17 thousand (previous year: EUR 17 thousand) in pensions was paid to a former member of the Management Board in 2016.

Shareholdings of members of the Company's corporate bodies

The shareholdings of the members of the Company's corporate bodies are distributed as follows:

	31 Dec. 2016	30 Sep. 2016	30 June 2016	31 March 2016
Management Board				
Dr. Ingo Bretthauer	60,000	60,000	60,000	60,000
Bernd Lange	35,000	35,000	35,000	35,000
Kai Bentz	17,600	17,600	17,600	17,600
Dr.-Ing. Christian Bieniek	1,500	1,500	1,500	1,500
Supervisory Board				
Dr. Heino Büsching	10,000	10,000	10,000	10,000
Bernd Hackmann	125,600	125,600	125,600	125,600
Prof. Dr.-Ing. Erich Barke	2,000	2,000	2,000	2,000

Remuneration of the Supervisory Board

Each member of the Supervisory Board receives fixed basic remuneration for each full financial year of membership on the Supervisory Board that is specified by resolution of the Annual General Meeting and is payable after the end of the financial year. The Chairman of the Supervisory Board receives double and the Deputy Chairman receives one-and-a-half times the amount of the fixed basic remuneration. The fixed remuneration from 1 January 2017 was set at EUR 32 thousand by resolution of the Annual General Meeting on 2 June 2016.

By resolution of the Annual General Meeting on 2 June 2016, there will no longer be any performance-based remuneration starting with the financial year beginning on 1 January 2016.

The remuneration of the Supervisory Board is as follows:

EUR thsd.		Dr. Heino Büsching (Chairman)	Bernd Hackmann	Prof. Dr.-Ing. Erich Barke	Total
Fixed remuneration	2016	80	60	40	180
	2015	80	60	40	180
Variable remuneration	2016	0	0	0	0
	2015	2	2	2	6
Total remuneration	2016	80	60	40	180
	2015	82	62	42	186

Supervisory Board members

Dr. Heino Büsching (Chairman)	Lawyer / tax consultant at CMS Hasche Sigle Partnerschaft von Rechtsanwälten und Steuerberatern mbB, Hamburg, Germany
Bernd Hackmann (Deputy Chairman)	Consultant to technology companies previously: Chief Executive Officer of LPKF Laser & Electronics AG Chairman of the Supervisory Board of Viscom AG, Hannover, Germany Member of the Supervisory Board of SLM Solutions Group AG, Lübeck, Germany
Prof. Dr.-Ing. Erich Barke	Retired professor of Leibniz University Hannover, Germany previously: President of Leibniz University Hannover, Germany Member of the Supervisory Board of the following companies: Esso Deutschland GmbH, Hamburg, Germany ExxonMobil Central Europe Holding GmbH, Hamburg, Germany hannoverimpuls GmbH, Hannover, Germany Solvay GmbH, Hannover, Germany

3.4 RESULTS OF OPERATIONS, FINANCIAL POSITION AND NET ASSETS OF THE GROUP

3.4.1 Results of operations

Development of revenue

The LPKF Group generated revenue of EUR 91.1 million in the 2016 financial year

The LPKF Group generated revenue of EUR 91.1 million in the 2016 financial year, an increase of 4.4% from the previous year. This was primarily due to higher revenue in the SQ segment, which was able to once again record growth of EUR 5.4 million from a substantial order after a weak previous year. Revenue in the WQ segment was also slightly up on the previous year. Revenue development was split in the EQ segment, with the LDS business only generating EUR 2.4 million in revenue after EUR 9.5 million the previous year. The delay in the development of new systems led to weaker-than-expected performance in the laser cutting and PCB drilling business. At the same time, revenue from cutting systems for the SMT industry increased considerably. The newly developed LIDE technology also contributed to revenue for the first time with the sale of the first glass drilling system. The EQ segment slightly exceeded the previous year's revenue. As a result, only the DQ segment lagged behind its prior-year figure, down 11%. The reasons for this weaker-than-expected business performance were the delayed launch of new ProtoLasers and regional weaknesses, particularly in China.

The following table shows the revenue by region:

in %	2016	Previous year
Asia	46.5	40.8
Germany	14.2	14.5
Europe excluding Germany	18.0	19.8
North America	19.4	21.7
Other	1.9	3.2
	100.0	**100.0**

The Group's export rate remains high at 85.8%

The Group's export rate remains high at 85.8%. Demand from Asia increased again compared to the previous year, thus cementing the region's role as the most important market for LPKF. The entire European market fell below the previous year's revenue, with the effects of Brexit yet to make themselves felt. Europe, including Germany, is the second-largest sales market for LPKF.

While the US market declined slightly in the financial year under review compared to other regions, it remains a strategically significant region for the Group. Many important customers are ordering laser systems for their production sites in Asia but conduct negotiations from their headquarters in the USA.

Development of orders

At EUR 105.7 million, incoming orders during the reporting period were 28% up on the previous year's level. Orders on hand at the end of the year, at EUR 27.8 million also were clearly above the previous year's figure of EUR 13.3 million (+110%). This increase is primarily attributable to a strong solar business.

Development of main income statement items

Production costs for prototypes and application systems of EUR 0.1 million and capitalized development costs for products and software of EUR 4.8 million are shown in own work capitalized. Other operating income declined by EUR 1.3 million on the previous year. This is partially attributable to lower insurance payments connected with the fire at the Garbsen site, as settlement of the claim was completed in 2016, but also due to a reduction in currency gains and income from the reversal of provisions. In contrast, research and development grants increased compared to the previous year.

The material cost ratio relative to revenue and changes in inventories rose significantly, climbing to 34.9% from 28.6% a year earlier. This was mainly due to write-downs of inventories and scrappages with a total value of EUR 5.9 million primarily carried out due to the decline in sales and recycling opportunities for LDS systems and components as well as in the solar industry. Adjusted for these write-downs, the material cost ratio was slightly below the prior-year level at 28.3%.

The number of employees was reduced from 778 to 700 during 2016

The number of employees was reduced from 778 to 700 during 2016. Restructuring measures had a negative effect of EUR 1.8 million on the Group's staff costs. The Management Board supported the cost reduction initiatives by voluntarily forgoing any performance-based remuneration. As a result, staff costs were EUR 43.9 million, close to the previous year's figure of EUR 43.7 million. The ratio of staff costs to total revenue was 48.2% in 2016 after reaching 50.1% a year earlier. The full reduction in staff costs caused by cuts to the workforce will only become evident in 2017.

Depreciation, amortization and impairment losses rose by EUR 0.9 million from the previous year to reach EUR 8.1 million. This increase was primarily driven by impairment losses on capitalized development costs of EUR 0.8 million (previous year: EUR 0.3 million).

Other operating expenses fell significantly during the financial year. While these costs still amounted to EUR 29.1 million in the previous year, the expenses for the year under review were only EUR 23.3 million, 20% lower than in 2015. The effects of the strict cost reduction program imposed by the Company in 2016 can be clearly seen here. These cost-cutting measures affected almost every unit and site within the Group. In particular, initiatives were launched to reduce expenses for development (EUR – 0.7 million), legal and consulting costs (EUR – 0.5 million), training expenses (EUR – 0.5 million), travel expenses (EUR – 0.4 million) and third-party work (EUR – 0.4 million). Repair costs also fell by EUR 1.1 million, having significantly increased in 2015 as a result of the fire. Currency losses declined by EUR 1.0 million, primarily due to the development of the EUR-USD exchange rate.

Weaker than expected revenue and high levels of extraordinary expenses led to a negative EBIT of EUR – 6.8 million (previous year: EBIT of EUR – 3.7 million). The EBIT margin fell to –7.4%, down from – 4.3% the previous year. In summary, these extraordinary expenses consisted of write-downs of inventories and scrappages amounting to EUR 5.9 million, impairment losses on capitalized development costs totaling EUR 0.8 million and restructuring expenses of EUR 1.8 million. The insurance payment of EUR 1.3 million is considered extraordinary income. This has a net negative effect on earnings totaling EUR 7.2 million. Without this negative impact, the Group would have recorded a positive EBIT of EUR 0.4 million and thus significantly reduced the break-even point as envisaged.

Increased utilization of short-term credit lines led to a EUR 0.1 million increase in interest expenses. As a result, net interest income totaled EUR – 0.8 million during the financial year (previous year: EUR – 0.7 million).

Based on an operating loss tax expense amounted to EUR 1.2 million. The tax ratio is – 16.4% (previous year: 20.9%). The Group again recorded a consolidated net loss for the year after taxes of EUR 8.8 million after posting a consolidated net loss of EUR 3.5 million in the previous year.

Multi-period overview of results of operations

		2012	2013	2014	2015	2016
Revenue	EUR million	115.1	129.7	119.7	87.3	91.1
EBIT	EUR million	20.4	23.2	12.7	– 3.7	– 6.8
Material cost ratio	%	30.6	26.7	31.4	28.6	34.9
Staff cost ratio	%	30.5	31.2	36.3	50.1	48.2
Tax rate	%	26.8	30.1	28.6	20.9	– 16.4
EBIT/employee	EUR thousand	31.2	32.0	16.1	– 4.7	– 9.0

Details regarding the operating segments can be found in the notes to the consolidated financial statements.

3.4.2 Financial position

Principles and goals of financial management

Funds are raised from external sources by issuing shares, for one, and by current and non-current borrowings, for another. The Group uses mainly its profits, as well as the retention of proceeds generated by depreciation / amortization and provisions, as sources for its internal financing.

Within the LPKF Group, derivatives are managed by the parent company, LPKF Laser & Electronics AG. Derivatives are used only to hedge foreign exchange rates and interest rates. The European companies optimize their liquidity peaks by way of cash pooling. All other companies carry out their ongoing cash management locally. LPKF is continually reviewing whether to expand cash pooling to other international companies. If large amounts of funds are required, reviews are performed to determine whether to utilize local financing or financing via LPKF AG.

The Group plans to generate a positive free cash flow in the 2017 financial year

The Group plans to generate a positive free cash flow in the 2017 financial year.

Statement of cash flows

The following statement of cash flows shows the origin and use of financial resources.

EUR million	2016	Previous year
Cash flow from operating activities	5.7	10.1
Cash flow from investing activities	- 7.5	– 13.7
Cash flows from financing activities	6.3	– 3.2
Change in cash funds due to changes in foreign exchange rates	0.0	–0.1
Change in cash funds	4.5	– 6.8
Cash funds on 1 Jan.	–0.9	6.0
Cash funds on 31 Dec.	3.6	–0.9
Composition of cash funds: cash-in-hand, bank balances	3.6	3.8
Overdrafts	0.0	– 4.7
Cash funds on 31 Dec.	3.6	–0.9

The Group's cash funds rose from EUR – 0.9 million at the end of the previous year to EUR 3.6 million. While write-downs of inventories had a negative effect on cash funds, they also led to a reduction in inventories. As a result, this had no impact on cash funds. Notional cash inflows from depreciation and amortization of non-current assets and higher advances received more than offset higher trade receivables and led to an overall cash inflow from operating activities of EUR 5.7 million. The Group's investing activities amounted to EUR 7.5 million, which meant that although free cash flow (balance of cash flow from operating activities and cash flow from investing activities) remained negative at EUR – 1.8 million, this figure represented an improvement from the previous year (EUR – 3.6 million).

Cash inflows of EUR 6.3 million were also generated by financing activities. Long-term borrowings were repaid on schedule, while net short-term borrowings of EUR 10.0 million were recorded.

Long-term financing is used for non-current assets

Long-term financing is used for non-current assets. subject to long-term fixed interest periods. The loans have interest rates of 1.0% to 4.35%. Sufficient credit lines (EUR 12.5 million) that have not been used to date are still available.

The financial position was stable in financial year 2016.

Multi-period overview of financial position

EUR million	2012	2013	2014	2015	2016
Cash flow from operating activities	17.1	34.2	1.8	10.1	5.7
Net liabilities to banks	13.1	11.2	30.2	37.3	39.9

(–) balance (+) debt

3.4.3 Net assets

Analysis of net assets and capital structure

The Company's net assets and capital structure developed as follows year on year:

	31 Dec. 2016		31 Dec. 2015	
	in EUR million	in %	in EUR million	in %
Non-current assets	66.4	56.8	67.6	56.9
Current assets	50.5	43.2	51.2	43.1
Assets	**116.9**	**100.0**	**118.8**	**100.0**
Equity	54.3	46.5	63.5	53.5
Non-current liabilities	24.1	20.6	27.1	22.8
Current liabilities Income	38.5	32.9	28.2	23.7
Equity and liabilities	**116.9**	**100.0**	**118.8**	**100.0**

The capitalization of development costs led to an increase in non-current assets. However, this was surpassed by a decline in property, plant and equipment. As a result, only the rise in deferred taxes led to higher non-current assets compared to the previous year. A total of 85% of the non-current assets are covered by equity (previous year: 99%).

Of the current assets, inventories were reduced significantly by write-downs in particular. Higher revenue in the fourth quarter led to higher levels of trade receivables at the reporting date that once again compensated for the fall in inventories. As of 31 December 2016, cash and cash equivalents hovered around the prior-year level at EUR 3.6 million. Net working capital fell by EUR 5.1 million to

EUR 35.2 million at the reporting date. This figure declined due to a significant increase in advances received compared to the previous year and a slight rise in trade liabilities. The growth of these two items (EUR 5.1 million in total) led to a decline in net working capital as they are deducted from inventories and receivables. Since revenue increased only slightly, the net working capital ratio declined from 46.2% in the previous year to 38.7% in the reporting period.

The equity ratio decreased from 53.4% in the prior year to 46.5%

The second successive loss-making year has left its mark on the balance sheet structure, with the equity ratio decreasing from 53.4% in the prior year to 46.5%. Liabilities to banks rose by a total of EUR 2.4 million. Long-term loans were reduced by EUR 2.9 million through scheduled repayments. By contrast, the Group recorded EUR 10.0 million in short-term liquidity loans also attributable to overdrafts totaling EUR 4.7 million. Of the current liabilities, advances received and trade liabilities increased by a total of EUR 5.1 million. With these exceptions, there has been no substantial change in the structure of the statement of financial position.

The return on capital employed (ROCE) is used to quantify an adequate return on the employed capital and to measure the achievement of performance targets. ROCE is calculated in percent as a ratio of EBIT and capital employed (interest-bearing equity and borrowings). The capital employed is determined by deducting provisions for pensions and non-interest bearing items in the statement of financial position from total assets.

Multi-period overview of net assets

		2012	2013	2014	2015	2016
Ratio of non-current assets to total assets	%	36.5	44.5	44.9	54.1	54.4
Inventories ratio	%	32.4	27.6	25.1	26.2	21.3
ROCE	%	26.5	26.4	12.1	– 3.6	– 6.9
Net working capital	EUR million	44.6	37.3	50.1	40.3	35.2
Net working capital ratio	%	38.8	28.7	41.9	46.2	38.7
Days sales outstanding	Days	57	53	54	64	63

Days sales outstanding (DSO) are determined based on the average amount of outstanding receivables between reporting dates.

Capital expenditures

In the 2016 financial year, EUR 7.5 million was invested in intangible assets and property, plant and equipment and thus EUR 6.2 million less than in the previous year. In addition to the capitalization of development costs, capital expenditures included only minor expenditures for the replacement of office equipment and IT expenses.

Employees

LPKF's basic philosophy is to secure motivated and well-trained employees and tie them to the Group on a long-term basis. Due to the economic situation, new hires were only made where necessary in 2016 and only staff replacements were carried out as a matter of priority. The Group does not expect the current number of employees to increase again as long as there is no sustained improvement in the economic situation. As part of human resources development, economically justifiable internal and external training courses and essential staff training measures were conducted in all areas to ensure that staff is well prepared to cope with future challenges. LPKF trains mechatronic technicians, industrial business assistants, IT specialists, product designers and technical drafters in order to acquire properly qualified young staff. The Group employed 38 trainees at the reporting date (previous year: 37); the number of trainees is expected to remain stable for the next years.

3.4.4 Segment performance

The following table provides an overview of the operating segments' performance:

EUR million		Electronics-Quipment	Development-Quipment	Welding-Quipment	SolarQuipment	Other	Total
External revenue	2016	30.6	22.6	24.0	13.9	0.0	91.1
	2015	29.9	25.5	23.3	8.5	0.1	87.3
Operating result (EBIT)	2016	– 4.4	2.0	– 0.1	– 1.0	– 3.3	– 6.8
	2015	– 0.6	3.3	0.1	– 3.8	– 2.7	– 3.7
Extraordinary items	2016	– 3.5	– 1.3	– 1.0	– 1.4	0.0	– 7.2

The extraordinary items include the write-downs of inventories (EUR 5.9 million), the impairment losses recognized on capitalized development costs (EUR 0.8 million), the restructuring costs (EUR 1.8 million), and the insurance payment for the business interruption in connection with the fire (EUR 1.3 million).

3.5 RESULTS OF OPERATIONS, FINANCIAL POSITION AND NET ASSETS OF LPKF AG

The following explanations aim to provide an overview of the economic development of LPKF AG (single entity). The annual financial statements of LPKF AG are prepared in accordance with the provisions of the German Commercial Code (HGB) as amended to reflect the provisions of the Accounting Directive Implementation Act (BilRUG) and published in the Federal Gazette (Bundesanzeiger). The single entity is managed according to the same principles as the Group, on the basis of the IFRSs. On account of the single entity's large share of the value creation in the Group, LPKF therefore refers to the statements in the "Corporate management" section and in the report on expected developments, which can also be extrapolated for the parent company.

3.5.1 Results of operations

LPKF AG's revenue amounted to EUR 42.1 million in the 2016 financial year

LPKF AG's revenue amounted to EUR 42.1 million in the 2016 financial year and thus remained 31.6% below the previous year's level. This is primarily due to the transfer of the operating business with plastic welding equipment from LPKF AG to LPKF WeldingQuipment GmbH on 1 October 2015. By comparison, first to third quarter revenue for this segment in 2015 was EUR 13.3 million. The remaining operating segments recorded weak performance compared to the previous year. As a result, revenue in the DQ segment was 15.2% down on the prior-year figure, while revenue in the EQ segment stabilized at the previous year's level. The percentage of revenue generated internationally was 84.1% (previous year: 77.6%).

The Company also received insurance compensation arising from the fire in January 2015 during the financial year under review. However, these payments were EUR 0.8 million lower than in the previous year. This compensation included a EUR 1.3 million payment for losses due to the interruption to business. Currency gains and income from the reversal of provisions and valuation allowances were also down on the previous year. Other operating income thus declined from EUR 7.3 million in 2015 to EUR 5.0 million in the financial year under review.

Reporting in accordance with BilRUG means revenue and other operating income are not fully comparable with the previous year's figures.

In particular, the lower revenue figure and subsequently amended product mix caused the material cost ratio to rise from 42.5% the previous year to 46.3%. Write-downs of inventories and scrappages amounted to EUR 0.5 million during the financial year (previous year: EUR 0.2 million).

Staff costs within LPKF AG decreased significantly by EUR 7.3 million due to both the transfer of staff at the Fürth site site in Germany to LPKF WeldingQuipment GmbH and a reduction in the workforce at the Garbsen site site in Germany. Despite the fall in revenue, however, the ratio of staff costs to total revenue rose only slightly to 40.0% (previous year: 39.1%). Although depreciation and amortization of non-current assets fell by EUR 0.8 million as a result of a reduction in investing activities, the item also includes write-downs of current assets totaling EUR 3.2 million, causing the depreciation and amortization rate to rise from 6.2% to 14.8%. Other operating expenses fell by a total of EUR 10.0 million. This is partly due to the significant drop in sales-related expenses caused by the relocation of the plastic welding business operations (approx. EUR 2.6 million). Repair expenses were also significantly reduced by EUR 1.1 million, while third-party work also decreased by EUR 1.8 million. Legal fees, travel expenses and material costs for development were also lowered by EUR 1.6 million through cost-cutting measures.

Overall, the decline in revenue led to a significant reduction in the EBIT margin

Overall, the decline in revenue again led to a significant reduction in the EBIT margin, which slipped to – 22.2% in the financial year after – 16.2% in the previous year. The financial result includes distributions of LPKF Inc. LaserMicronics and LPKF d.o.o. totaling EUR 6.0 million. Due to profit and loss transfer agreements with LPKF SolarQuipment GmbH and LPKF WeldingQuipment GmbH, LPKF AG is also obliged to take on total losses of EUR 1.7 million for the financial year. Earnings before tax were EUR 5.4 million higher than in the previous year, with the Company generating a net loss for the financial year of EUR 5.5 million after reporting a net loss of EUR 7.2 million the previous year.

Income statement of LPKF AG

EUR million	2016	2015
Revenue	42.1	61.6
Change in inventories	0.2	– 2.0
Other own work capitalized	0.0	0.1
Other operating income	4.8	7.3
Cost of materials	19.6	25.3
Staff costs	16.8	24.1
Depreciation / amortization / impairment losses on fixed assets	6.2	3.8
Other operating expenses	13.8	23.8
Operating result	**– 9.3**	**– 10.0**
Financial result	**3.9**	**– 1.0**
Income taxes	0.0	– 3.8
Earnings after taxes	**– 5.4**	**– 7.2**
Other taxes	0.1	0.0
Net loss / income for the year	**– 5.5**	**– 7.2**
Retained earnings brought forward from the previous year	4.3	11.5
Net retained profits	**– 1.2**	**4.3**

Regarding the performance indicators, the expectation is that LPKF AG will essentially develop in line with Group's forecast described in section 8.1.3.

3.5.2 Net assets and financial position

Total assets stood at EUR 82.3 million on 31 December 2016, down on the prior-year figure of EUR 85.8 million. Investments in tangible and intangible assets amounted to EUR 2.1 million in 2016 after EUR 2.6 million the previous year. Intangible assets rose overall as a result of new software licenses. Acquisitions of technical and office equipment remained lower than depreciation. Write-downs and scrappage of inventories and the accelerated destocking of inventory goods led to a decrease in inventories totaling EUR 3.5 million. Trade receivables were EUR 2.5 million higher on the reporting date as a result of higher December revenue and longer-term payment due dates. Receivables from affiliated companies fell slightly compared to the previous year and primarily comprise financial receivables. Cash and cash equivalents rose to EUR 1.5 million after EUR 0.3 million in the previous year. Overall, current assets decreased by EUR 2.4 million. The recognition of deferred assets amounting to EUR 3.9 million was primarily attributable to the net losses for the past two financial years and remained at the previous year's level.

The equity ratio decreased from 46.6% in the prior year to 41.9%

The decrease in equity of EUR 5.5 million to EUR 34.5 million is attributable to the net loss for the year of EUR 5.5 million. The equity ratio decreased from 46.6% in the prior year to 41.9%. Other provisions decreased by a total of EUR 0.9 million compared to the previous year, primarily as a result of the utilization of bonus provisions and provisions for severance payments. Liabilities to banks rose by EUR 4.1 million on the reporting date. The majority of these liabilities have a remaining maturity of up to one year (EUR 19.2 million). Miscellaneous liabilities primarily include liabilities to affiliated companies resulting from both trade payables and financing. At EUR 45.2 million, total liabilities slightly exceeded the previous year's level (EUR 42.4 million).

The Company's net assets and capital structure developed as follows year on year:

	31 Dec. 2016		31 Dec. 2015	
	in EUR million	in %	in EUR million	in %
Non-current assets	41.9	50.9	43.0	50.1
Current assets	40.4	49.1	42.8	49.9
Assets	**82.3**	**100.0**	**85.8**	**100.0**
Equity	34.5	41.9	40.0	46.6
Non-current liabilities	14.6	17.7	15.8	18.4
Current liabilities Income	33.2	40.4	30.0	35.0
Equity and liabilities	**82.3**	**100.0**	**85.8**	**100.0**

Weak revenue during the financial year and the exceptional depression of earnings caused by write-downs had a negative impact on equity. Despite the lower equity ratio, LPKF AG's net assets and financial position are judged to be stable, given that there are undrawn lines of credit as well.

Capital expenditures

Investments totaling EUR 2.1 million primarily consist of software licenses, measurement technology equipment and production and application machines. Reinvestments as a result of the fire in 2015 only play a minor role here.

Employees

LPKF AG had 242 employees at the reporting date, 39 fewer than in the previous year.

Dividend

The sustained ability to pay a dividend is key goal of the LPKF Group. The Company plans to propose to the Annual General Meeting that between 30% and 50% of LPKF's earnings per share be distributed as a dividend in the following year. LPKF may deviate from this aim, especially if it faces an uncertain future due to circumstances such as an economic downturn, or if paying a dividend would jeopardize its ability to finance investments or put the financial position of LPKF AG or the Group at risk.

In view of the development in 2016 and the prospects for the new financial year, the Management Board and the Supervisory Board intend to propose to the Annual General Meeting on 1 June 2017 that no dividend be paid, as in the previous year.

3.5.3 Risk report

The business development of LPKF AG is essentially exposed to the same risks as that of the LPKF Group. These risks are explained in the risk report (section 7) of the combined management report.

3.6 EMPLOYEES

Motivated, highly-qualified staff that identifies with LPKF is the key to success for a technology company like LPKF – especially in economically difficult times. Low levels of sick leave and employee turnover are important indicators of LPKF's success in achieving this goal. At 3.97%, the sick leave percentage in the LPKF Group was below the average for the metal working and electronics industry in Germany (2015: 5.3%). The employee turnover rate in the Group was 15.9% (2015: 9.4%). This increase is due to capacity adjustments that were necessary.

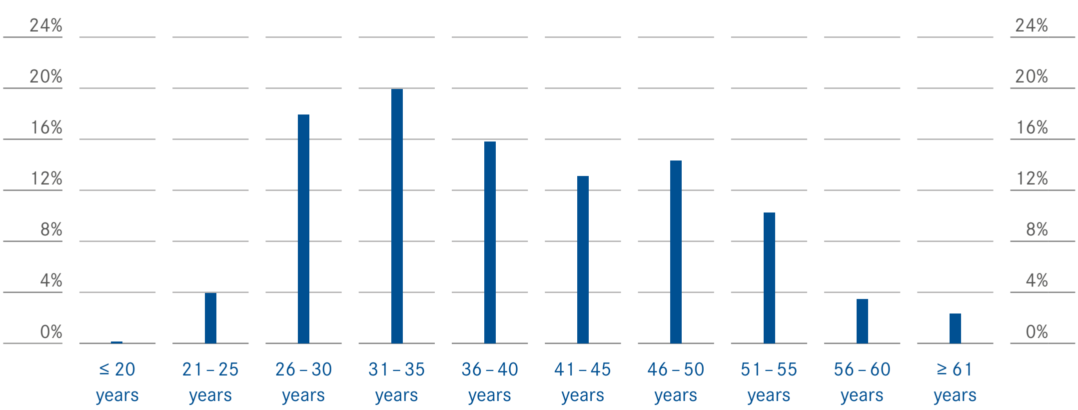
As a result of demographic change, the share of older people in the population as a whole has been increasing compared with the share of younger people for decades now. Life expectancy, which has also been rising for decades, coupled with lower birth rates is largely responsible for these demographic changes.

Demographic shifts also affect the labor market. The decline in births means that in the future fewer and fewer young workers will be available. The proportion of older people in the workforce will grow for this reason alone. Then there is also the shift in the retirement age.

The average age of the workforce at the LPKF Group was 39.0 years

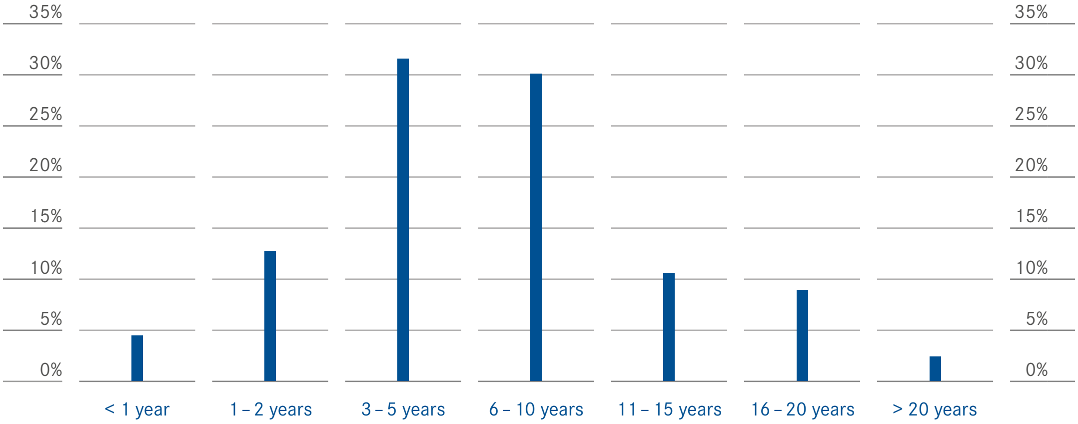
The average age of the workforce at the LPKF Group was 39.0 years (previous year: 39.0). According to information provided by the VDMA, the average age of all employees in the German engineering industry is rising slowly but steadily.

AGE STRUCTURE ANALYSIS IN YEARS, LPKF GROUP (EXCLUDING TRAINEES)



An analysis of the length of service of LPKF Group employees shows that with an average of 6.5 years (previous year: 5.2 years) LPKF as a relatively young enterprise can point to a healthy mix of experienced and new employees.

DISTRIBUTION OF LENGTH OF SERVICE IN YEARS, LPKF GROUP (EXCLUDING TRAINEES)



Based on the current age structure and a balanced mix of years of service, LPKF is positioned well to face the challenges posed by demographic trends.

3.7 OVERALL APPRAISAL OF THE GROUP'S ECONOMIC SITUATION

The 2016 financial year was a remarkable one in many respects for the LPKF Group. Weak revenue development at the start of the year made it necessary to consolidate the business. Among other initiatives, the Group reduced its workforce by 103 FTEs to sustainably reduce its cost base. Extraordinary items from write-downs of inventories, own work capitalized, restructuring measures and insurance compensation were recorded in 2016 that had a negative impact of EUR 7.2 million on EBIT and led to a reduction in equity. Overall, the Group's financial situation worsened in 2016.

There were positive signs at the end of the year to brighten the outlook

However, there were several positive signs at the end of the year to brighten the outlook. The last three quarters of the 2016 financial year were profitable when adjusted for extraordinary items, and the Group even achieved slight revenue growth and moderately positive EBIT adjusted for extraordinary items for 2016 as a whole. The objective of reducing the cost base to a break-even point below EUR 90 million was achieved by consistently implementing cost reduction measures. Orders on hand and incoming orders were significantly above prior-year figures at the year end. Many new products that were not yet or only partially available in 2016 are market ready as of the end of the year.

The Management Board believes that LPKF will get back on a growth trajectory in 2017 and can post positive earnings and achieve an appropriate return on capital employed.

IV. REPORT ON POST-BALANCE SHEET DATE EVENTS

DISCLOSURES ON PARTICULARLY SIGNIFICANT EVENTS
Please refer to the consolidated notes for reportable events after the reporting date.

V. CORPORATE GOVERNANCE DECLARATION

The corporate governance declaration pursuant to Section 289a HGB is part of the combined management report. The declaration is available for the public on LPKF AG's website (http://www.lpkf.com/investor-relations/corporate-governance/declaration-compliance.htm) and included in the corporate governance report on pages 28 – 33 of the annual report.

VI. REPORT ON OPPORTUNITIES

6.1 OPPORTUNITY MANAGEMENT
As a technology company, LPKF does business in a dynamic market environment. New opportunities constantly arise from a changing technology landscape and new market requirements. Systematically identifying and leveraging these opportunities is a major factor in the sustainable growth of the LPKF Group. Opportunity management involves closely monitoring new markets and applications, regularly evaluating market analyses, and reviewing the focus of the product portfolio.

New opportunities constantly arise from new market requirements

In the R&D unit, innovation managers specialize in systematically seeking out new technologies. The responsibility for identifying opportunities in the product groups and markets lies with the product managers and international subsidiaries. Results are regularly reported to the Company's management. If it is likely that opportunities will materialize, they are included in the planning and outlook for the coming years. The opportunities listed below focus on future trends or events that could result in a positive deviation for LPKF from the outlook given in the report on expected developments. Taking into account the existing estimation uncertainty, the opportunities presented below can make a positive contribution to earnings in the single-digit million range.

6.2 OPPORTUNITIES

6.2.1 Further developing the existing product portfolio
LPKF updates the product portfolio on an ongoing basis, aligning this activity with signals from customers, technological progress outside the Company and changing markets. At the same time, it also pursues its own ideas and innovations. The Company thus aims to always be prepared to meet future customer needs while at the same time actively creating new market demand through its own innovative and efficient processes. LPKF ensures its capability to innovate for the future by closely networking its development departments with market research, sales and service, as well as providing a suitable annual R&D budget of approximately 10% of revenue. The continual updating of the product portfolio can result in changes in the product mix, and these changes pose risks as well as providing opportunities.

6.2.2 New technology breakthroughs

LPKF is a market leader in all product groups worldwide

LPKF is a market leader in all product groups worldwide. The chances are excellent for further expansion of market share thanks to LPKF's wide-ranging technological expertise, brand recognition and long-term relationships with customers. In addition to established markets, LPKF additionally concentrates on attractive new markets that promise good growth and income opportunities. Moreover, LPKF aims to open up new markets and further cement its presence in existing markets by developing new products. The purpose of systematic market and technology monitoring is to identify market opportunities. Based on this monitoring, technology studies are conducted that provide an opportunity to register industrial property rights on completely novel solutions, among others.

6.2.3 Takeover of external companies with strategically relevant expertise

LPKF has a broad product portfolio and many ideas for further developing products and uncovering new market opportunities. This is why organic growth is at the forefront of LPKF's corporate strategy. Nonetheless, the Company also pursues opportunities for external growth that could come from acquiring patents or companies with strategically relevant expertise.

6.2.4 Orders as a result of supplanting conventional production methods

The production methods developed by LPKF often have economic and quality advantages compared to conventional production technologies. Above average growth is possible if customers decide to abandon traditional methods in favor of LPKF's equipment. Especially in a rapidly changing market environment, many of LPKF's customers see the need to make larger investments in their own developments and launch new products. This benefits sales of LPKF products to development laboratories. Both ongoing technological progress, in general, and LPKF's intensive development activities are making laser-based machinery more attractive to customers than established technologies, even for mass production.

6.2.5 Independence of individual markets as a result of broad positioning

LPKF's strategy to build on its core competencies and enter different markets has a potentially stabilizing effect against the backdrop of cyclical markets. The various markets served by LPKF undergo sometimes asynchronous and different industry cycles.

6.2.6 Business organization

Going forward, LPKF aims leverage economies of scale even more effectively

The consistent alignment of the corporate structure to the strategy has created one of the key conditions for exploiting opportunities for further growth. The Group's organization and internal processes are continually improved and positioned for profitable growth. Going forward, LPKF aims to profit further from the size of the Group and leverage economies of scale even more effectively.

VII. RISK REPORT

7.1 DESCRIPTION OF THE INTERNAL CONTROL SYSTEM

7.1.1 Overview

The aim is to safeguard the Group's assets and boost its operating efficiency

The internal control system (ICS) comprises the principles, procedures and measures introduced by LPKF's management. They focus on the organizational implementation of management decisions and statutory requirements. The aim of the methods and measures implemented by LPKF is to safeguard the Group's assets and to boost its operating efficiency.

The ongoing refinement of the ICS involves analyzing the Company's functional areas – e. g., during audits, workshops, internal audits and Management Board meetings – and assessing the probability of damage occurring in these areas and the extent of potential damage.

The Management Board organizes the structure of the individual units and constantly adjusts workflow to the findings gathered from the ICS. Among others, this involves strictly separating incompatible activities, implementing the dual control principle in all significant areas internationally and installing controls in the workflows. Examples include signature regulations, approval requirements for significant transactions, and IT access authorizations.

The results of the internal audits are presented to the Supervisory Board. It is stipulated that the findings must be worked through in a timely manner. Follow-up audits ensure that the agreed implementation of the findings is monitored regularly and documented. Implementation is the responsibility of the relevant Management Board member with purview over the respective area.

The risk and opportunity management system is also an integral part of the ICS.

7.1.2 Risk management system

Risk management is pursued actively at LPKF like opportunity management, which is not integrated into the risk management system, but instead is handled separately. In doing so, the Company employs a number of reporting tools.

Risk management serves to safeguard the foundation of business and enhance competitiveness

Risk management at LPKF involves the formulation and implementation of measures that are suitable to identify existing risks, hedge them, reduce their probability of occurring, mitigate them or consciously accept them to a reasonable extent. Risk is defined as potential future trends or events that might result in a negative departure from forecasts or goals. Risk management serves to safeguard the foundation of business and enhance competitiveness by providing a platform for suitably controlling specific risks and managing them transparently. It ensures that risks are identified and controlled proactively. This is a crucial factor for sustainable commercial success because risks are inseparably associated with business activity. The risk management system is integrated with compliance management through creation of a shared position.

An international firm of public auditors performs internal auditing tasks for the entire LPKF Group. These audits are based on a multi-year audit plan that reflects the risk situation of the Group documented by the risk management system and the risk assessment developed by the Management Board. In financial year 2016, audits were conducted at LPKF AG and one subsidiary.

The LPKF Group is exposed to numerous risks as it pursues its global business activities within the rapidly changing conditions affecting its target markets. Risk management, specifically the risk early warning system, is therefore always a fundamental element in the planning and implementation of LPKF's business strategy. Although risks can be limited by taking suitable measures and can be identified rapidly and precisely through an early warning system, they can never be completely excluded and can only be assessed as of a given point in time. LPKF therefore makes use of a number of highly developed management and control systems to measure, monitor, control and handle the risks the Group is exposed to. Group-wide strategic planning and the associated reporting system are particularly important in this context. The Management Board of LPKF AG is responsible for risk policy and the internal control and risk management system. The second- and third-level management staff implement these control functions in each of the Group's organizational units and benefit here from theoretical technical knowledge, practical experience and excellent networking in the relevant topical areas. In this way, the responsible employees can use suitable and effective means to identify new risks quickly and directly where they arise and then report them to the risk manager. A central database is used for reporting. A risk report is submitted to the Supervisory Board and the Management Board on a monthly basis. In addition to regular reporting on identified risks, ad hoc reports must be prepared as needed on all risks that occur unexpectedly. This involves the risk manager coordinating and, if necessary, participating in developing the various risk control measures. The risk manager reports directly to the Management Board. Aspects of risk and opportunity management are also a fixture on the agenda of the weekly meetings of the full Management Board. This procedure has proven its worth time and again in past years. The risk early warning system is reviewed annually by a public auditor, and where necessary also by other external auditors. Internal auditing also reviews the risk management system as part of a multi-year auditing plan, most recently in 2014.

A risk report is submitted to the Supervisory Board and the Management Board on a monthly basis

In order to record and control risks, existing instruments in the context of the risk management process such as the risk management manual and the reporting tools are updated continuously and the daily implementation of the risk management system is documented. Risk management discussions of all types are always recorded in minutes. As in previous years, existing and potential risks were reassessed and the reporting system was reviewed to ascertain its efficiency in managing risks in the 2016 financial year. New risk owners were trained and made aware of risks. A database-supported reporting system has been installed. The quality management system pursuant to DIN EN ISO 9001:2008 and the occupational safety management system pursuant to OHSAS 18001 are also important elements of the risk early warning system and for ensuring structured business processes. The implementation of the recommendations of the German Corporate Governance Code, which also plays an important part in the cooperation between the Supervisory Board and the Management Board, is yet another instrument for limiting and managing risks.

7.1.3 Description of the main features of the internal control and risk management system relevant to the financial reporting process (Section 289 (5) German Commercial Code)

The internal control and risk management system relevant for the financial reporting process is designed to ensure proper financial reporting, which is defined as the compliance by the consolidated financial statements and combined management report with all applicable regulations.

The workflows in the Group are structured around processes and are set up identically for the most part thanks to the use of the same ERP system in key units of the Group. The Company plans to roll out the system to additional units in the Group.

Automatic process controls are integrated into this system and protected from unintentional changes with an IT-based authorization concept.

The dual-control principle is applicable throughout the LPKF Group

The dual-control principle is applicable throughout the LPKF Group. Through the general separation of functions related to administration, execution, accounting and approval – and the delegation of these functions to different members of staff or departments – this approach limits the possibilities for engaging in fraudulent acts. This is a manual control that also underlies the process descriptions, signature regulations, guidelines and work instructions.

The specific functions of the internal control system are the risk management system, Group Accounting, Internal Auditing and Compliance Management, which at LPKF AG are based at the Group's headquarters.

Possible incorrect reporting by subsidiaries and the publication of financial reports containing errors are particular risks documented in the risk management system. These risks are monitored continually. More details on the risk management system are included in section 7.1.2.

The entries recorded at LPKF AG and the subsidiaries provide the data used to prepare the consolidated financial statements. LPKF guarantees the quality of this data by selecting suitable staff and regularly training employees, and enlisting the help of service providers, e.g., in measuring long-term liabilities and determining facts material to accounting by Group Accounting. Before being included in the consolidated financial statements, the data is subject to automatic and manual controls. The consolidated financial statements are prepared in a system separate from the ERP system to which only a limited group of authorized persons has access. It is managed solely at headquarters. In further developing the systems, the focus is on automating standard procedures to the greatest extent possible. The annual financial statements of the parent company and the consolidated financial statements are subject to a statutory audit, one component of which is a check to ensure that the Management Board has met the requirements of Section 91 (2) German Stock Corporation Act for setting up an appropriately structured risk early warning system. The suitability of the risk early warning system for identifying developments that would endanger the Company's status as a going concern at an early stage is also verified.

The position of compliance manager was created to ensure that all business activities comply with the statutory provisions and the values of LPKF. The compliance manager is responsible for stipulating guidelines applicable throughout the Group and compliance with these guidelines, the essential elements of which have been laid down in the Compliance Code.

Based on the organizational, control and monitoring structures defined by the Management Board, the internal control system enables the complete recording and proper presentation of transactions in the Company's accounts.

However, personal judgments, defective controls and criminal acts in particular cannot be fully excluded despite these measures. This could limit the effectiveness of the internal control system, which means that even the strict application of regulations provides no absolute guarantee for the correct, complete and punctual recording of all matters in the accounts.

7.2 SPECIFIC RISKS

The risk management process currently involves dealing in detail with the specific risks listed in the table below which could have a significant impact on the LPKF Group's business, as well as its net assets, financial position and results of operations. Some of the risks changed compared to the previous year.

The following risks in particular are given high priority[1]:

Specific risk	Qualitative probability of occurrence[2]	Possible financial effects[3]
General business risks (esp. macroeconomic risks from sector trends and market acceptance)	Possible	Material
Dependence on individual customers	Less likely	Material (moderate)
Technological developments	Less likely (possible)	Moderate (material)
Patent risks	Less likely (possible)	Moderate (material)
Personnel risks	Possible (less likely)	Moderate
Financial risks	Unlikely	Material

1 Previous year's assessments are shown in parentheses if they have changed

2 Categories: Unlikely = Probability of occurrence less than 5%
Less likely = Probability of occurrence up to 25%
Possible = Probability of occurrence higher than 25% and up to 50%
More likely than unlikely = Probability of occurrence higher than 50%

3 Categories: Moderate = Damage amount up to EUR 5 million
Material = Damage amount higher than EUR 5 million

Other risks which are currently unknown, or which are currently (still) considered negligible, could also have a positive or negative impact on LPKF.

Disclosures on individual risks:

7.2.1 General business risks

Cause

LPKF is operating internationally in an ever faster changing environment. The Company's customers are exposed to considerable cost and competitive pressures as well as curtailed investment budgets. Business in LPKF's target markets is cyclical, with particularly strong fluctuations especially in the electronics industry as well as the automotive and solar industry.

Whereas the automotive industry continued to grow in 2016, some uncertainty was noticeable in the consumer electronics industry. For example, a slowdown in market growth and a loss of market share on the part of major international vendors in favor of emerging Chinese competitors was observed in the cell phone and smartphone market. The solar market grew again with capital expenditure mainly going toward efficiency improvements and reducing end product costs. Among others, the further development of the business with solar scribers is also contingent on the continuation of and further amendments to legal regulations that govern the feed-in fees, e. g., for solar electricity. In China, a large decrease in compensation was approved in financial year 2016. Government regulations, particularly in China, also have a considerable effect on business performance. Often, investment decisions are not made based on economic factors but instead in view of political considerations.

Often, investment decisions are made based political considerations

Economic fluctuations have a strong impact on the investment in production equipment. Especially in markets outside Asia, customers' willingness to expand capacities or introduce new technologies is therefore limited. New investments are often only made when future utilization of such equipment appears assured by concrete orders from customers.

The Group's general business risks also include the increasing share of the project business in the overall operations. Order volumes of several million euros are being negotiated more frequently than in the past in connection with projects. This places special demands on the Group's flexibility to be able to also deal with greater fluctuations in sales volumes. The ability to plan the Company's business performance can also be impacted as a result. In particular the SQ and EQ segments are affected by this.

LPKF is also exposed to risks associated with a rapidly changing technological environment. The availability of high-quality components enables new players to launch cost-efficient competitive products or alternative techniques. For more explanations see section 5.2.4.

The systematic development of new technologies and business segments is generally associated with the risk that the planned business model fails to meet its targets. A risk also exists that new technologies may not be accepted by the market overall or only accepted after a considerable time lag. There is also the risk, especially in connection with new technologies or machine types, that deliveries might be delayed or that formal acceptance procedures might not take place at all or only later. Ensuring the high level of quality required by customers places great demands on development and production processes. Especially systems, components and technologies that have been newly developed from scratch entail a risk of high quality costs.

Product liability risks, in particular in connection with patents and the associated warranty of title mainly arise in the EQ and WQ segments. Furthermore, the risk that recall costs may be incurred is to be pointed out. This risk arises in particular in the business with production services at the subsidiary LaserMicronics GmbH.

Last but not least, the global political situation may also pose risks affecting the development of LPKF's business. The risks involved here include possible changes in laws, e. g., with respect to the import of capital goods to China or in other important markets such as the USA. Recent years have seen the increasing implementation of tariff and non-tariff barriers to trade in China. Furthermore, political crises can have an unfavorable effect on the willingness of government institutions to invest and therefore particularly affect the DQ segment.

Measures

In part, these industry cycles are staggered timewise in different markets such that LPKF's broad market positioning helps to balance matters somewhat. This positioning in the market is part of the business model and is to be retained in the future. In order to expand LPKF's leading role in the various businesses, it is important to have a robust innovation and product management system with state-of-the-art technology and to be in close contact with customers in close proximity to the market. Overall, around 10% of revenue should also be invested in the new and further development of products in the future.

Overall, around 10% of revenue should be invested in the new and further development of products

In order to be able to compensate for fluctuations in the utilization of capacities, LPKF is focusing on flexible structures, for example in production, and increasingly also on the collaboration of LPKF's production sites. In addition, peak workload levels are covered by way of external production service providers and recourse to temporary workers. In the case of lower workload levels, the depth of production can be increased.

In the EQ segment, the new LIDE method was developed to market readiness to reduce dependence on a small number of top revenue-generating products. The product launch for the LIDE method for drilling vias in thin glass (TGV) took place in financial year 2016. This move is aimed at developing a completely new customer base in the IC packaging market. The laser systems required for this purpose are expected to contribute to revenue as early as 2017, although not yet substantially. From 2018 onward, series production of products using TGVs can begin. The demand for laser systems for their manufacture is then expected to grow sharply.

In the SQ segment, a new technology for the digital printing of functional pastes is being developed as well: the LTP method. The first machines are expected to be shipped in 2017. Significant revenue contributions are anticipated starting in 2018. LTP will decrease the SQ segment's dependence on the solar industry.

Expanding quality management and preparations for certification to ISO 9001:2015 are focal points of the Group's strategy, and measures to this end were implemented in the 2016 financial year.

The Company seeks to cover these through insurance policies if there are existent risks from product liability.

One of LPKF's subsidiaries also provides production services for the automotive supply industry. There is a risk in this connection that the Group will be held liable for auto manufacturers' recalls on account of defects. The probability of a loss is deemed to be low, however. This risk is further mitigated by taking out insurance.

Effects on economic position

Despite the measures in place and planned, occurrence of the risks described above is considered possible and any financial effects on the Company are considered material.

7.2.2 Dependence on individual customers

Cause

The distribution of revenue by region shows a clear shift to Asia, China in particular. While it reflects prevailing market conditions, it has resulted in the Group's evolving dependence on international customers that base most of their manufacturing in China. In the SQ segment, larger-scale projects are often completed with a few customers. For some time now, a major customer has dominated significant parts of this business. In the EQ segment, there is also a certain dependence on decisions made on the part of a few major customers for laser-based technologies who then provide their suppliers with corresponding instructions. These instructions can have an impact on LPKF's business with these suppliers.

If the Company were to fail to land individual major projects, this could significantly affect the financial success of this business segment. Due to the ongoing difficult business situation in the solar industry, there is an increased risk of order cancellations and defaults in the SQ segment. There is currently no indication of this.

Measures

A considerable portion of the default risk can be insured

The EQ business again succeeded in considerably widening its customer base in 2016 especially for the de-panneling of electronic components with lasers. In the solar business, the agreed payment terms and other contractual conditions provide a certain level of protection against cancellations and payment defaults. A considerable portion of the default risk can also be insured.

Effects on economic position

Possible order cancellations can have a negative impact on the Group's revenue and earnings if, for example, capacities cannot be wound down fast enough or used by other business units. After an up-and-down year in 2016, current planning assumes revenue growth in 2017 and beyond based on the current order and project situation. However, due to the dependency on customers and projects in the solar business, the utilization of capacities, revenue and earnings are likely to continue fluctuating in the solar business. Taking into account the overall circumstances, this risk is considered less likely to occur than before. Due to the current order situation, any possible loss is categorized as material.

7.2.3 Technological developments

Cause

As a technology company, LPKF primarily markets manufacturing solutions for current technical issues. There is a risk that the demand for LPKF's manufacturing technologies will develop adversely due to changes in end customer markets. In the markets, some of which can be quite cyclic, there is an additional risk when the capacity and willingness to invest in new technology diminishes in response to the state of the economy. The increased appearance of competing techniques can lead to declining revenue and income, in particular if these techniques should prove to be technologically and/or economically advantageous.

The competitive situation and the rapidly changing technological requirements are associated with cross-segment risks. LPKF's success significantly depends on the speed and quality with which new products can be developed to market readiness.

Measures

Permanent follow-up by the Supervisory Board and the Management Board is an integral part of the risk management system to review the sustainable value of new developments and integrate these findings into the product strategy. This follow-up involves the division heads, innovation management and the head of Group strategy. The development of high-quality products in a structured, expeditious flow of development projects is supported by a structured idea generation and development process. In addition to frequently achieving cost benefits by investing in LPKF's technology, LPKF's customers can also enjoy competitive benefits and harness the associated market opportunities. In this way, it has been possible to repeatedly replace established technologies with laser-based processes. LPKF's technologies are also protected by patents.

Effects on economic position

In 2016, LPKF generated the majority of its revenue with fresh products

In 2016, LPKF once again generated the majority of its revenue with fresh products and developed a major innovation, the LIDE technology, to readiness for series production. The planning for the coming years assumes that this success can be continued. On the whole, this is critically important for the LPKF Group. The competitive situation and rapidly changing technological requirements necessitate a flexible and dynamic development process. The occurrence of risks related to technological development is currently considered less likely than before. The possible financial consequences are viewed as being moderate.

7.2.4 Patent risks

Cause

The LPKF Group owns 44 patent families, and most of them are international. LPKF continually applies for new patents thanks to its intense development activities, in addition to acquiring the industrial property rights of third parties. LPKF considers the obtaining of patent rights to be the most effective way of preventing its R&D investments to be devalued by copyists. Existing or new industrial protection rights of third parties cannot be precluded and might have an impact on the financial condition of LPKF. There is also the risk that competitors might successfully challenge LPKF's patents.

Measures

In general, these risks are addressed with comprehensive innovation and product management and close cooperation with internationally active patent attorneys. LPKF is also in close contact with customers and other sources of information and, in this way, tries to identify and counter risks in this area at an early stage. Furthermore, by intensively pursuing R&D activities, LPKF always strives to gain a technological edge over its competitors and possible patent infringers. If successful, this is an effective additional measure of protection against copying and the theft of intellectual property.

Effects on economic position

Due to the significant decline in the importance of the LDS business and the associated patent situation for the LPKF Group, the possible financial consequences in this area can be described as moderate. This risk is currently estimated to be less likely to occur.

7.2.5 Personnel risks

Cause

Demand for qualified technical personnel in both mechanical engineering and manufacturing remains high. LPKF's business performance in 2016 in conjunction with the necessary communication had a mostly negative effect on its employer brand on the market. Due to capacity reductions in 2016, only a small number of jobs were advertised outside the Company. Accordingly, only some 400 applications were received by the German sites. Nonetheless, thanks to its attractive work environment, contacts with universities and the growing level of awareness the Company enjoys in the laser sector, LPKF has not had any significant problems to date attracting qualified staff. Strong demand for internships and traineeships, the number of unsolicited applications received and the relatively short time it takes to fill positions are evidence of this.

Due to the high level of qualifications of LPKF's staff there is a cross-segment risk associated with the loss of key employees with important know-how as a result of head hunting. It was observed that employees were approached more often, particularly as a result of LPKF's business performance in 2016.

Measures

An attractive working environment and development opportunities within the LPKF Group are offered to employees to retain high performers in the Company. Particular value is placed on individual flexibility, compensation that reflects performance and a good working atmosphere. Executives have an important role to play in maintaining employee satisfaction and retaining staff. Leadership issues were the focus in many discussions and meetings, including in events for managers. Although systematic personnel development was not the focus of human resources activities due to LPKF's business performance and capacity adjustments in 2016, continuing professional and personnel development measures aligned with the needs of employees were initiated nonetheless. HR marketing will continue to be important to position LPKF on the labor market as an attractive employer among small- and medium-sized mechanical engineering firms.

Effects on economic position

Demand for qualified technical personnel in mechanical engineering is high

Despite capacity adjustments in 2016, the Company's economic position was affected only slightly due to the staffing measures implemented. In addition, the Company currently enjoys a low level of sick leave compared to industry as a whole. The financial effects can therefore currently be described as moderate. Demand for qualified technical personnel in both mechanical engineering and manufacturing remains high. Thanks to its attractive work environment, contacts with universities and the growing level of awareness the Company enjoys in the laser sector, LPKF has not had any significant problems attracting adequately trained staff. However, there continues to be a cross-segment risk associated with the loss of key employees with important know-how as a result of head hunting. LPKF's business performance in financial year 2016 increased the probability of occurrence of this risk, which is currently classified as possible.

7.2.6 Financial risks

Cause

An unfavorable business trajectory coupled with the lack of access to cash tied up in assets can result in a downturn in the liquidity of the Group. External influences, such as deterioration in the financing environment, a rating change or customer payment difficulties can also adversely affect the liquidity situation. This risk affects all segments. Business performance clearly failed to meet targets in financial year 2016, which had a unfavorable impact on liquidity.

Measures

LPKF reduced its cost base in 2016 and worked hard on optimizing working capital management. The SPRINT project was launched to continue these measures and improve processes. Numerous talks were held the financing banks, during which the initiated measures and their effectiveness were discussed and reviewed. Openness and transparency were essential in this context in order to secure long-term collaboration with the financing partners. The same is true for communication with the capital markets.

The Company uses suitable information sources in an effort to assess financial risks at the level of customers, the relevant markets and economic conditions and, if necessary, to hedge these with credit default insurance.

Effects on economic position

The economic position of the Group can be affected materially by financial risks. The current economic environment is viewed as neutral to slightly negative. The initiated measures had the desired effect. As a result, the financial situation remained stable. LPKF therefore considers it unlikely that such risks will materialize.

7.2.7 Other risks

In addition to the significant risks described above, the Group is also exposed to the following risks, among others:

Exchange rate fluctuations

Cause

The exchange rates between foreign currencies and the euro can undergo major fluctuations. For LPKF, the main fluctuations are those with regard to the US dollar (USD) and the Chinese renminbi (CNY). This risk also includes obligations from hedging relationships entered into that arise from delays in the underlying transaction (e. g., late receipt of USD already sold). As a rule, LPKF invoices in euros. Only for transactions with American customers is billing usually in USD. In these cases, exchange rate volatility can have an indirect effect on LPKF's competitiveness because most of its competitors are not from the eurozone and material costs at LPKF are incurred in euros.

Measures

LPKF closes hedging transactions to protect itself against exchange rate risks

LPKF closes hedging transactions to protect itself against exchange rate risks involving business transactions invoiced in foreign currencies. This part of the risk management is handled by the parent Company in Garbsen, Germany, also on behalf of subsidiaries. In accordance with the risk management strategy, most of the foreign currency cash flow is either used for procuring materials in the dollar countries or hedged by engaging in forward exchange transactions or acquiring put options in foreign currencies.

Effects on economic position

Fluctuations in exchange rates can have a moderately positive or negative effect on earnings. Counter measures are permanently reviewed and implemented to the degree possible. The exchange rate trend of the euro against the US dollar and important Asian currencies, which has been weak for quite some time now, is in principle considered to be very positive for competitiveness and the business in general.

IT risks

Cause
In terms of its information, its international activities and the IT systems used to process it, the Group is potentially exposed to the risk of industrial espionage or disruptions by internal or external perpetrators, just as other innovative companies.

Measures
By implementing redundant IT infrastructures, LPKF protect itself against risks that occur in the event of a systems failure or natural disaster. Security is also ensured by means of a restrictive policy for granting access authorizations to systems and information as well as by maintaining distributed backups of data repositories. The Company uses various IT security technologies to mitigate the risk of unauthorized access to Company data. In addition to technical measures, LPKF also provides training to all employees. IT security measures are evaluated on an ongoing basis by way of audits conducted by external consultants. In this context, LPKF adheres to national and international standards. The results are structured for management and serve as a planning and decision-making tool for further risk management.

Effects on economic position
The performance of many security measures is sometimes costly, but results in LPKF being able to classify the likelihood of occurrence of a risk and possible loss as moderate. A residual risk that cannot be fully managed exists with regard to IT security due to the rapid pace of continuing technical developments.

7.3 ASSESSMENT BY THE MANAGEMENT BOARD OF THE RISK SITUATION AFFECTING THE GROUP

Financial risks have increased in 2016

The macroeconomic environment slightly improved by emerging from a low point after a sustained period of restrained economic growth for LPKF AG in 2016. The sectors relevant to the Company exhibited different trends during the financial year ended. Economic research institutes forecast a slight upward trend for 2017 and the following years, characterized by economic uncertainties. A number of risks relevant to the LDS business materialized in 2016 and previous years, and are therefore no longer relevant in the future. On the whole, planning reliability and the foreseeability of business trends continue to be low in most business segments. Financial risks have increased because of LPKF's business development in 2016. However, the various individual risks only have a limited influence on the overall risk situation of the Group and have not led to any significant changes compared with the previous year.

A review of the overall risk situation of the LPKF Group concluded that there are currently no concrete risks jeopardizing the Group's existence as a going concern.

There is also currently no foreseeable development which could significantly and sustainably harm the profit or loss, cash flows and financial position of the LPKF Group in the future. There is, however, a continued possibility that the effects of a significant economic slowdown, particularly in China, could impede the further development of LPKF. The extent to which a possible change in foreign trade policy in the United States will expose LPKF to risk cannot currently be estimated.

The auditor of the financial statements reviewed LPKF AG's risk early warning system set up pursuant to the German Stock Corporation Act (Aktiengesetz). This review revealed that the existing Groupwide risk early warning system is fit for purpose, meets the requirements of the German Stock Corporation Act and is suitable for detecting developments that jeopardize the Company's continued existence as a going concern at an early stage.

VIII. REPORT ON EXPECTED DEVELOPMENTS

8.1 OVERALL APPRAISAL OF THE GROUP'S PROBABLE PERFORMANCE

8.1.1 Economic environment

The Kiel Institute for the World Economy (IfW) expects global economic growth to rise by 3.5% in 2017 and 3.6% in 2018 after overcoming its downturn last year.

The economic output of developed economies is expected to increase by around 2.1% next year

Economists believe that the upturn in developed economies will gradually intensify as a result of expansive monetary policy, fiscal policy stimuli and slightly rising demand from developing and emerging markets. The economic output of developed economies is expected to increase by around 2.1% this year and next.

After relatively low economic growth last year, the IfW expects a more significant increase in the USA of 2.5% and 2.7% respectively for 2017 and 2018. The primary reason for this is the country's expansive monetary policy, with higher government expenditure and tax cuts. The consolidation of the shale oil industry, which hampered economic development, is also complete. In the eurozone, economists continue to expect moderate economic development with growth rates reaching similar levels to the previous year at around 1.7% for this year and next. Germany remains among Europe's strongest economies, with predicted growth rates of 1.7% and 2.0% respectively for 2017 and 2018. In the wake of good economic performance in 2016 triggered by the Brexit vote, the United Kingdom is expected to experience a considerable slowdown in 2017, with growth predicted to be around 1.2%.

According to economists' forecasts, the economic performance of emerging markets is expected to increase amid continuing risks such as debt denominated in US dollars, which is rising in line with the USD. After economic development in China accelerated in 2016, the IfW once again expects this trend to ease, with predicted growth rates of 6.4% for the current year and 5.9% in 2018. One reason for this is the desire for sustainable growth.

Current economic forecasts expressly refer to the increase in global economic policy risks. These include the change in US President, the United Kingdom's withdrawal from the EU, the development of the oil price and divergent key interest rate trends in the USA and Europe. For example, the drop in orders in the German engineering sector in the last month of last year showed the effects these risks can have. While free international trade and European integration are being called into question against a backdrop of protectionist tendencies, it does not yet seem possible to quantify these developments. As a result, there remains a degree of uncertainty as mentioned in the forecasts.

In addition to the global and regional economy, the business performance of laser technology specialist LPKF AG is impacted by developments in the wider engineering market as well as in the automotive and electronics sectors with a focus on the consumer electronics, solar and plastics processing industries.

With the effects of changing economic conditions already being felt at the end of 2016, the German Engineering Federation (VDMA) is only expecting production growth to increase by 1% in real terms in 2017. Sector revenue is expected to rise slightly from EUR 220 billion to EUR 224 billion. In general, the VDMA believes that German engineering companies remain well positioned internationally due to their high quality and focus on exports.

During the current 2017 financial year, the German Automotive Industry Association (VDA) expects the international passenger car market to continue to grow. New registrations are projected to reach approximately 85 million units this year. According to the VDA's forecasts, China – the largest automotive market in the world – will continue to grow. As the second and third-largest markets internationally, the USA and Western Europe are expected to remain stable this year. German passenger car manufacturers have a market share of 70% in Germany, 50% in Western Europe and 20% in China. Uncertainties have arisen from the Brexit decision, as German automakers export more vehicles to the United Kingdom than any other country, and from the change of president in the USA.

Worldwide installed photovoltaic capacity is expected to rise by around 13% per year

After the solar industry hit a record high in 2016, EuPD Research expects the sector to experience a difficult year in 2017. Growth of 30% last year was primarily based on significant expansion in China, the world's largest solar market. A slight decline in new installations is expected in 2017 after China considerably lowered its expansion target for the period to 2020. According to forecasts from London-based firm Global Data, worldwide installed photovoltaic capacity is expected to rise by around 13% per year until 2025 to 756.1 GW. Capacity increased by around 50% annually between 2006 and 2015.

In the consumer electronics industry, Gartner analysts expect deliveries of smartphones – which now make up around 80% of the global PC market – to rise slightly to 1.893 billion units in 2017 (2016: 1.888 billion units). This market segment is expected to experience significant growth again from 2018 as consumers replace older devices. After experiencing high levels of growth, deliveries recently stabilized due to signs of saturation in important markets such as the USA, Europe, Japan and some Asian regions.

The German Plastics Processing Industry Association (GKV) remains cautiously optimistic about performance in Germany over the next few years after the sector achieved record revenues of almost EUR 60 billion in 2015. In contrast, research company Applied Market Information (AMI) believes the European plastics industry is in a period of stagnation.

8.1.2 Group performance

Economic research institutes forecast a slight upward trend for 2017 and the following years, characterized by economic uncertainties. This creates somewhat improved economic conditions for the future business performance of the international LPKF Group. With an export ratio of 86%, LPKF relies heavily on international trade that is as free as possible. It therefore remains to be seen how protectionist tendencies could lead to export restrictions.

The high degree of diversification reduces dependence on individual market segments

The LPKF Group's high degree of diversification reduces its dependence on individual market segments. The Company expects above-average strong growth in the WQ and SQ segments, with the cutting systems and PCB drilling business in the EQ segment also offering growth potential. The DQ segment is envisaged to remain at roughly the same revenue level seen in 2016.

LPKF expects the EQ segment to grow at an average rate. The Group does not envisage growth in the LDS and Stencil Equipment businesses. Expectations have been reduced to such a low level in the LDS business that this product area is unlikely to have any additional negative effects on earnings.

LPKF expects the new LIDE and LTP technologies still being introduced to the market during the current 2017 financial year to provide fresh stimulus for growth over the next years. LIDE technology can be used to drill holes in glass for interposers produced by chip manufacturers, for example. LTP offers a new alternative to widespread screen printing and will be used for the digital printing of pastes. LPKF sees a variety of applications for both technologies. However, it is difficult to predict how long it will be until customers are ready to convert their production to these new techniques.

8.1.3 Significant indicators

Revenue in financial year 2016 reached EUR 91.1 million, thus exceeding the prior-year figure by 4.4%. Operating income (EBIT) fell by EUR 3.1 million to EUR – 6.8 million, with the EBIT margin declining accordingly to –7.4%, below the previous year's level of – 4.3%. Adjusted for extraordinary items totaling EUR –7.2 million, EBIT stands at EUR 0.4 million with an EBIT margin of 0.5%.

At EUR 105.7 million, incoming orders during the reporting period were 28% up on the previous year's level. Orders on hand at the end of the year, at EUR 27.8 million also were clearly above the previous year's figure of EUR 13.3 million (+110%). The positive trend in incoming orders continued at the start of 2017.

The Management Board anticipates revenue of between EUR 92 million and EUR 100 million for the current 2017 financial year

If the global economy remains stable, the Management Board anticipates revenue of between EUR 92 million and EUR 100 million and an EBIT margin of between 1% and 5% for the current 2017 financial year. This results in planning for EBIT in 2017 between EUR 1 million and EUR 5 million. The Group will focus on providing a foundation for positive business performance through R&D, while efficiency improvements and cost control will continue to play a key role across the entire Group.

The net working capital ratio is expected to fall back to below 35%, which corresponds to net working capital of less than EUR 35 million for the forecast period. This would represent a moderate year-on-year increase. Regarding the error rate, LPKF expects it to improve slightly.

The Company is aiming to continue increasing revenue in the coming years. The Management Board intends to return to generating EBIT margins of at least 10% in the medium term.

IX. RESPONSIBILITY STATEMENT

To the best of our knowledge, and in accordance with the applicable reporting principles, the consolidated financial statements give a true and fair view of the assets, liabilities, financial position and profit or loss of the Group, and the Group management report includes a fair review of the development and performance of the business and the position of the Group, together with a description of the material opportunities and risks associated with the expected development of the Group.

Garbsen, Germany, 21 March 2017

Dr. Ingo Bretthauer   Bernd Lange   Kai Bentz   Dr.-Ing. Christian Bieniek

CONSOLIDATED FINANCIAL STATEMENTS 2016

LPKF LASER & ELECTRONICS AG

CONSOLIDATED FINANCIAL STATEMENTS FOR THE 2016 FINANCIAL IN ACCORDANCE WITH THE INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRSS)

CONSOLIDATED NOTES 2016

CONSOLIDATED STATEMENT OF FINANCIAL POSITION AS OF 31 DECEMBER 2016

Assets in EUR thsd.	Note	31 Dec. 2016	31 Dec. 2015
Non-current assets			
Intangible assets	10		
Goodwill		74	74
Development costs		13,266	11,473
Other intangible assets		1,928	1,991
		15,268	**13,538**
Property, plant and equipment	10		
Land, similar rights and buildings		38,611	39,654
Plant and machinery		4,801	4,885
Other equipment, operating and office equipment		4,929	6,137
Advances paid and construction in progress		0	13
		48,341	**50,689**
Receivables and other assets			
Trade receivables	12	214	257
Income tax receivables	13	0	46
Other assets	13	69	153
		283	**456**
Deferred taxes	15	2,514	2,899
		66,406	**67,582**
Current assets			
Inventories	11		
(System) parts		12,512	15,658
Work in progress		3,179	2,843
Finished products and goods		9,162	11,839
Advances paid		108	752
		24,961	**31,092**
Receivables and other assets			
Trade receivables	12	19,781	13,593
Income tax receivables	13	434	236
Other assets	13	1,770	2,522
		21,985	**16,351**
Cash and cash equivalents	14	3,584	3,795
		50,530	**51,238**
		116,385	**118,820**

CONSOLIDATED STATEMENT OF FINANCIAL POSITION AS OF 31 DECEMBER 2016

Equity and liabilities in EUR thsd.	Note	31 Dec. 2015	31 Dec. 2014
Equity			
Subscribed capital	16	22,270	22,270
Capital reserves		1,489	1,489
Other retained earnings		10,933	10,933
Share-based payment reserve		490	490
Currency translation reserve		1,595	1,945
Net retained profits		17,553	26,374
		54,330	**63,501**
Non-current liabilities			
Provisions for pensions and similar obligations	17	290	352
Other provisions	18	24	52
Non-current liabilities to banks	19	22,630	25,480
Deferred income from grants	3	679	732
Deferred taxes	15	512	488
		24,135	**27,104**
Current liabilities			
Tax provisions	18	178	374
Other provisions	18	3,164	2,954
Current liabilities to banks	19	20,852	15,627
Trade payables	19	3,071	2,278
Other liabilities	19	11,206	6,982
		38,471	**28,215**
		116,385	**118,820**

CONSOLIDATED INCOME STATEMENT FROM 1 JANUARY TO 31 DECEMBER 2016

EUR thsd.	Note	2016	2015
Revenue	1	91,124	87,255
Changes in inventories of finished goods and work in progress		– 2,288	– 181
Other own work capitalized	2	4,902	6,914
Other operating income	3	5,784	7,127
		99,522	**101,115**
Cost of materials	4	31,029	24,896
Staff costs	5	43,895	43,697
Depreciation, amortization and impairment losses	6	8,057	7,152
Other operating expenses	7	23,293	29,087
Operating result (EBIT)		**– 6,752**	**– 3,717**
Finance income	8	6	25
Finance costs	8	832	705
Earnings before tax		**– 7,578**	**– 4,397**
Income taxes	9	1,244	– 916
Consolidated net loss		**– 8,822**	**– 3,481**
Earnings per share (basic)	21	EUR – 0.40	EUR – 0.16
Earnings per share (diluted)	21	EUR – 0.40	EUR – 0.16

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME FROM 1 JANUARY TO 31 DECEMBER 2016

EUR thsd.	Note	2016	2015
Consolidated net loss		**– 8,822**	**– 3,481**
Revaluations (mainly actuarial gains and losses)		– 17	– 6
Deferred taxes		17	– 6
Sum total of changes which will not be reclassified to the income statement in the future		**0**	**– 12**
Fair value changes from cash flow hedges reclassified to the income statement		0	17
Currency translation differences		– 350	1,087
Sum total of changes which will be reclassified to the income statement in the future if certain conditions are met		**– 350**	**1,104**
Other comprehensive income after taxes		**– 350**	**1,092**
Total comprehensive income		**– 9,172**	**– 2,389**

CONSOLIDATED STATEMENT OF CASH FLOWS FROM 1 JANUARY TO 31 DECEMBER 2016

EUR thsd.	Note	2016	2015
Operating activities			
Consolidated net loss		–8,822	–3,481
Income taxes		1,244	–916
Interest expense		832	705
Interest income		–6	–25
Depreciation, amortization and impairment losses		8,056	7,152
Gains/losses from the disposal of non-current assets including reclassification to current assets		78	135
Changes in inventories, receivables and other assets		–5,885	13,332
Changes in provisions		120	–1,115
Changes in liabilities and other equity and liabilities		4,637	–5,735
Other non-cash expenses and income		6,575	138
Interest received		7	19
Income taxes paid		–1,167	–101
Cash flows from operating activities		**5,669**	**10,108**
Investing activities			
Investments in intangible assets		–5,448	–7,790
Investments in property, plant and equipment		–2,023	–5,938
Proceeds from disposal of financial instruments		0	0
Proceeds from disposal of non-current assets		21	24
Cash flows from investing activities		**–7,450**	**–13,704**
Cash flows from financing activities			
Dividend payment		0	–2,672
Interest paid		–832	–705
Proceeds from borrowings		10,000	13,600
Cash repayments of borrowings		–2,916	–13,392
Cash flows from financing activities		**6,252**	**–3,169**
Change in cash funds			
Change in cash and cash equivalents due to changes in foreign exchange rates		27	–134
Change in cash funds		4,471	–6,765
Cash and cash equivalents on 01 January		**–917**	**5,982**
Cash and cash equivalents on 31 Dec.		**3,581**	**–917**
Composition of cash funds			
Cash and cash equivalents		3,584	3,795
Overdrafts		–3	–4,712
Cash and cash equivalents on 31 Dec.	20	**3,581**	**–917**

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY AS OF 31 DECEMBER 2016

EUR thsd.	Subscribed capital	Capital reserves	Other retained earnings
Balance as of 01 Jan. 2016	22,270	1,489	10,933
Consolidated total comprehensive income			
Consolidated net profit/loss	0	0	0
Revaluations (mainly actuarial gains and losses)	0	0	– 17
Deferred taxes on changes recognized directly in equity	0	0	17
Currency translation differences	0	0	0
Consolidated total comprehensive income	**0**	**0**	**0**
Balance as of 31 Dec. 2016	**22,270**	**1,489**	**10,933**

EUR thsd.	Subscribed capital	Capital reserves	Other retained earnings
Balance as of 01 Jan. 2015	22,270	1,489	10,945
Consolidated total comprehensive income			
Consolidated net profit/loss	0	0	0
Reclassification of cash flow hedge reserve to the income statement	0	0	0
Revaluations (mainly actuarial gains and losses)	0	0	– 6
Deferred taxes on changes recognized directly in equity	0	0	– 6
Currency translation differences	0	0	0
Consolidated total comprehensive income	**0**	**0**	**– 12**
Transactions with owners			
Distributions to owners	0	0	0
Balance as of 31 Dec. 2015	**22,270**	**1,489**	**10,933**

Cash flow hedge reserve	Share-based payment reserve	Currency translation reserve	Net retained profits	Total Equity
0	490	1,945	26,375	63,502
0	0	0	– 8,822	– 8,822
0	0	0	0	– 17
0	0	0	0	17
0	0	– 350	0	– 350
0	**0**	**– 350**	**– 8,822**	**– 9,172**
0	**490**	**1,595**	**17,553**	**54,330**

Cash flow hedge reserve	Share-based payment reserve	Currency translation reserve	Net retained profits	Total Equity
– 17	490	858	32,528	68,563
0	0	0	– 3,481	– 3,481
17	0	0	0	17
0	0	0	0	– 6
0	0	0	0	– 6
0	0	1,087	0	1,087
17	**0**	**1,087**	**– 3,481**	**– 2,389**
0	0	0	– 2,672	– 2,672
0	**490**	**1,945**	**26,375**	**63,502**

CONSOLIDATED NOTES 2016

LPKF LASER & ELECTRONICS AG

A. BASIC INFORMATION

LPKF Laser & Electronics AG, Garbsen (the Company) and its subsidiaries (hereinafter the LPKF Group) produce equipment and systems for electronics development and production. New laser-based technologies are aimed at customers in the automotive, electronics and solar industries.

The Company is a stock corporation which was established and is headquartered in Germany. Its registered seat is at:

Osteriede 7
30827 Garbsen

These consolidated financial statements were approved for publication by the Management Board on 21 March 2017.

B. BASIS OF PREPARATION OF THE CONSOLIDATED FINANCIAL STATEMENTS

The consolidated financial statements of LPKF Laser & Electronics AG, Garbsen, have been prepared using uniform accounting policies. They take into account all International Financial Reporting Standards (IFRS) and all interpretations of the International Financial Reporting Interpretations Committee (IFRIC) as applicable on the reporting date and in the EU.

The consolidated financial statements are prepared on the basis of historical cost, limited by the market valuation of available-for-sale financial assets as well as by the measurement of financial assets and financial liabilities (including derivatives) at fair value through profit and loss.

Preparing IFRS consolidated financial statements requires the use of estimates. Furthermore, the application of Group-wide accounting policies requires assessments by management. Areas that permit greater leeway in terms of assessments or exhibit greater complexity, or where assumptions and estimates are of critical significance to the consolidated financial statements, are discussed in the notes under E.

The financial year corresponds to the calendar year. The consolidated financial statements have been prepared in euros. Unless indicated otherwise, all amounts are shown in thousands of euros (EUR thousand).

The following standards that were amended, revised or issued prior to the reporting date were applied in the 2016 financial year:

Standard/interpretation		Mandatory application	Adopted by the EU commission [1]	Effects
IAS 16 IAS 41	Amendments to IAS 16 and IAS 41 – Bearer Plants	01 Jan. 2016	23 Nov. 2015	None
IFRS 11	Accounting for Acquisitions of Interests in Joint Operations	01 Jan. 2016	24 Nov. 2015	None
IAS 19	Employee Contributions	01 Jan. 2016	17 Dec. 2014	None
IAS 16 IAS 38	Clarification of Acceptable Methods of Depreciation and Amortization	01 Jan. 2016	02 Dec. 2015	None
IFRS 5, IFRS 7, IAS 19, IAS 34	Annual Improvements Cycle 2012 – 2014	01 Jan. 2016	15 Dec. 2015	No material effects
IFRS 2, IFRS 3 IFRS 8, IFRS 13, IAS 16, IAS 38, IAS 24	Annual Improvements Cycle 2010 – 2012	01 Jan. 2016	09 Jan. 2015	No material effects
IAS 1	Disclosures in the Notes	01 Jan. 2016	18 Dec. 2015	No material effects
IAS 27	Equity Method in Separate Financial Statements	01 Jan. 2016	18 Dec. 2015	None

1 As of 31 December 2016

Initial application of these pronouncements and amendments did not have any material effects on the current or previous presentation of the Group's net assets, financial position and results of operations.

The following standards that were amended, revised or issued prior to the reporting date were not applied in the 2016 financial year:

Standard/interpretation		Mandatory application	Adopted by the EU commission [1]
IFRS 9	Financial Instruments (July 2014)	01 Jan. 2018	22 Nov. 2016
IFRS 15	Revenue from Contracts with Customers	01 Jan. 2018	29 Oct. 2016
IFRS 16	Leases	**01 Jan. 2019**	Not yet adopted
IFRS 2	Classification and Measurement of Share-based Payment	**01 Jan. 2018**	Not yet adopted
IAS 7	Statement of Cash Flows: Disclosures in the Notes	**01 Jan. 2017**	Not yet adopted
IAS 12	Income Taxes: Recognition of Deferred Tax Assets for Unrealized Losses	**01 Jan. 2017**	Not yet adopted
IFRIC 22	Foreign Currency Transactions and Advance Consideration	01 Jan. 2018	Not yet adopted

1 As of 31 December 2016

The IFRS 9 Financial Instruments standard issued by the IASB on 24 July 2014 is a three-phase project to replace IAS 39 Financial Instruments: Recognition and Measurement. The standard governs the classification and measurement of financial instruments, accounting for the impairment of financial assets and hedge accounting. For EU entities applying IFRSs, the standard is mandatory for financial years beginning on or after 1 January 2018. The LPKF Group does not expect any material effects on the Group's net assets, financial position and results of operations.

Issued by the IASB on 28 May 2014, IFRS 15 Revenue from Contracts with Customers replaces the previous standards governing revenue, IAS 18 and IAS 11. This standard stipulates the timing and amount of revenue recognition. According to these rules, revenue must be recognized when the customer has obtained control over the agreed goods and services and can obtain benefits from these. Specified criteria are used to distinguish between performance obligations that are fulfilled over time or at a point in time. Moreover, additional disclosures are required in the notes to provide users of financial statements with more meaningful and relevant information. For EU entities applying IFRSs, the standard must be applied for financial years beginning on or after 1 January 2018. The LPKF Group is currently analyzing the effects of this standard on the amount and time at which revenue is recognized but it does not expect material changes in revenue recognition. However, additional disclosures will be required in the notes to the financial statements.

IFRS 16 Leases, which was issued by the IASB on 13 January 2016, replaces the former standards and interpretations governing leases (IAS 17, IFRIC 4, SIC-15 and SIC-27) and implements a single model to be used by lessees to account for leases. According to this standard, all leases must be recognized as rights of use and liabilities from lease agreements reported in the statement of financial position at the lessee, except when the lease term is 12 months or less, or the leased object is a low-value asset (each optional). The lessor is required to continue to distinguish between operating and finance leases. The standard is mandatory for financial years beginning on or after 1 January 2019. The EU has not endorsed the standard to date. At this time, the LPKF Group is analyzing the effects resulting from the amendments to the standard on net assets, financial position and results of operations. A slight increase in total assets is likely to occur, because the operating leases currently presented in the notes will have to be accounted for as rights of use, and lease liabilities will have to be recognized in the statement of financial position. Expenses incurred from operating leases to date will no longer be recognized as leasing expenses going forward. The new rules will result in amortization of the rights of use and interest expense, and therefore the LPKF Group expects corresponding changes in the income statement.

BASIS OF CONSOLIDATION

In addition to the Group's parent company, LPKF Laser & Electronics Aktiengesellschaft, Garbsen, the following subsidiaries have also been included in the consolidated financial statements:

Name	Registered seat	Equity interest (previous year) %	Equity EUR thsd.	Result for the financial year ended EUR thsd.
Fully consolidated				
LaserMicronics GmbH	Garbsen / Germany	100.0 (100.0)	1,090.4	73.1
LPKF SolarQuipment GmbH	Suhl / Germany	100.0 (100.0)	7,194.9	0.0
LPKF WeldingQuipment GmbH	Fürth / Germany	100.0 (100.0)	286.9	0.0
LPKF Laser & Electronics d. o. o.	Naklo / Slovenia	100.0 (100.0)	6,624.8	1,656.0
LPKF Distribution Inc.	Tualatin (Portland) / USA	100.0 (100.0)	4,421.9	773.4
LPKF (Tianjin) Co. Ltd.	Tianjin / China	100.0 (100.0)	10,291.6	– 2,166.0
LPKF Laser & Electronics Trading (Shanghai) Co. Ltd.	Shanghai / China	100.0 (100.0)	36.6	– 2.1
LPKF Laser & Electronics (Hong Kong) Ltd.	Hong Kong / China	100.0 (100.0)	1,802.4	– 350.0
LPKF Laser & Electronics K. K.	Tokyo / Japan	100.0 (100.0)	– 1,263.8	389.9
LPKF Laser & Electronics Korea Ltd.	Seoul / Korea	100.0 (100.0)	– 692.0	– 486.6

The equity and earnings figures for the financial year just ended concern the financial statements as of 31 December 2016 and represent the balances pursuant to the local financial statements prior to reconciliation for purposes of groupwide recognition and measurement.

The legal structure of the LPKF Group did not change in the 2016 financial year.

With the authorization of the Annual General Meeting on 28 May 2015, a profit transfer agreement with a five-year term effective retrospectively at the beginning of 2015 is in place between LPKF Laser & Electronics AG and LPKF SolarQuipment GmbH. With the authorization of the Annual General Meeting on 02 June 2016, LPKF WeldingQuipment GmbH signed a profit transfer agreement with LPKF Laser & Electronics AG that became effective retrospectively at the beginning of 2016.

As of 31 December 2016, LPKF AG had ten subsidiaries, which together with the parent company form the basis of consolidation.

C. CONSOLIDATION PRINCIPLES

The consolidated financial statements are based on the financial statements as of 31 December 2016 of the companies included in the consolidated financial statements, which were prepared in accordance with uniform accounting policies.

Subsidiaries include all entities that are controlled by the Group (more precisely: LPKF AG). LPKF AG controls an investee when it has power over the investee, risk exposure or rights to variable returns arise from its investment in the investee and LPKF AG has the ability to use its power over the investee such that this affects the amount of the investee's variable returns. Consolidation of an investee begins on the day on which LPKF AG gains control over the entity. It ends when LPKF AG loses control over the investee.

Subsidiaries acquired are accounted for using the purchase method. The acquisition costs correspond to the fair value of the assets given, the equity instruments issued and the liabilities incurred or assumed at the acquisition date.

Assets, liabilities and contingent liabilities identifiably in connection with a business combination are remeasured upon initial consolidation, irrespective of the scope of the non-controlling interests. The excess of the cost of the acquisition over the Group's interest in the fair value of the net assets acquired is recognized as goodwill. If the cost of acquisition is lower than the fair value of the net assets of the subsidiary acquired, the difference is recognized directly in profit or loss.

Intra-Group transactions, balances and unrealized gains and losses from transactions between Group companies are eliminated. Deferred taxes are recognized on consolidation measures reported in the income statement.

The accounting policies used by subsidiaries were adjusted as necessary to the Group's uniform accounting policies.

If the Group loses either its control or significant influence over an entity, its remaining equity interest is remeasured at fair value and the resulting difference is recognized in profit or loss. The fair value of an associate, joint venture or financial asset is the fair value determined upon initial recognition. In addition, the treatment of any amounts shown in other comprehensive income relating to this entity is analogous to the treatment of transactions by the parent company directly disposing of the respective assets and liabilities. This means that any gain or loss previously shown in other comprehensive income must be reclassified from equity to profit or loss.

D. CURRENCY TRANSLATION

Annual financial statements are prepared in the functional currency of each entity; it is defined as the currency of the economic environment in which the entity mainly operates. The functional currency of subsidiaries is the same as the currency of the country in which the subsidiary is domiciled.

If the annual financial statements of a subsidiary are prepared in a functional currency other than the euro, the assets and liabilities are translated into euros at an average exchange rate at the reporting date and equity is translated at the historical exchange rate. Expenses and income were translated at the average annual exchange rate. The translation differences are recognized directly in equity as a currency translation reserve until the subsidiary is disposed of.

The exchange rates of the material currencies that were applied in the preparation of these consolidated financial statements are listed below:

	Closing rate		Average exchange rate	
1 euro = currency x	31 Dec. 2016	31 Dec. 2015	2016	2015
US dollar	USD 1.0541	USD 1.0887	USD 1.1066	USD 1.1096
Chinese renminbi yuan	CNY 7.3202	CNY 7.0608	CNY 7.3512	CNY 6.9730
Hong Kong dollar	HKD 8.1751	HKD 8.4376	HKD 8.5900	HKD 8.6023
Japanese yen	JPY 123.40	JPY 131.07	JPY 120.31	JPY 134.29
South Korean won	KRW 1,269.36	KRW 1,280.78	KRW 1,284.57	KRW 1,255.74

E. CRITICAL ACCOUNTING AND MEASUREMENT ESTIMATES AND ASSUMPTIONS

All estimates and assessments are continuously updated and are based on historical experience and other factors including expectations of future events that are believed to be reasonable under the circumstances.

The Group makes assessments and assumptions that concern the future. Estimates based on these assessments and assumptions often do not correspond to actual facts in the future. The estimates and assumptions associated with a significant risk of triggering material adjustments to the carrying amounts of assets and liabilities within the next financial year are discussed in the following.

(a) Estimated impairment of goodwill

In accordance with the accounting policy described in note 10.1, the Group tests goodwill for impairment annually and whenever there is a concrete indication of possible impairment. The recoverable amount of cash generating units (CGUs) was determined based on a calculation of their value in use. These calculations must be based on assumptions made by the management on 31 December 2016.

(b) Intangible assets and property, plant and equipment

Material assumptions and estimates refer to determining the useful lives and the recoverable residual values of intangible assets and items of property, plant and equipment. More details regarding useful lives and residual values are presented under note 10, "Non-current assets" in chapter H. "Consolidated statement of financial position".

(c) Provisions

Accounting for provisions involves making assumptions regarding probability, maturity and risk level. Actuarial calculations are used to determine the obligation from defined-benefit pension commitments and termination benefits paid to employees as well as the obligation from a long-term bonus program launched for the first time in 2012. The amount of the pension provisions is essentially dependent on the life expectancies on which it is based, and the choice of discount rate which is redetermined every year. The discount rate is based on the interest rate paid on high-quality corporate bonds in that currency in which the benefits are paid and whose maturities correspond to the pension obligations. Key parameters in the calculation of provisions for anniversary payments and termination benefits are employee turnover and the salary growth factor. Detailed information is provided in note 17 describing pension provisions. An option pricing model is used to calculate the value of the obligation arising from the long-term bonus program settled in cash due to the influence exerted by LPKF's share price. Another material factor is the performance of the EBIT margin, which is derived from the Group's planning. Detailed information is provided in note 18 describing other provisions.

(d) Income taxes

The Group is subject to income tax payments in various countries. Material assumptions are therefore required to determine income tax provisions on a global scale.

There are numerous business transactions and calculations for which the ultimate level of taxation cannot be finally determined during the course of normal business activities. The Company determines the amount of the provisions for expected tax audits based on best estimates of whether and to what extent additional income taxes may become payable. If the final level of taxation of these business transactions deviates from the initial assumptions, this will have an impact on the actual taxes and deferred taxes in the period in which taxation is finally determined.

Deferred tax assets are recognized at the amount at which it is probable that future tax benefits will be realized. The assessment of recoverability is based on five-year planning, probable performance as well as taxable temporary differences. The actual extent to which earnings in future periods must be taxed, and thus the actual extent to which the tax benefits will be usable, may deviate from the assessment at the time the deferred tax assets are recognized.

(e) Fair value of derivative and other financial instruments

The fair value of financial instruments not traded on an active market is determined by applying suitable valuation techniques selected from a large number of methods. The assumptions applied in this context are largely based on the market conditions existing on the reporting date.

(f) Accounting changes

No accounting changes were made in these financial statements.

F. SEGMENT REPORTING

In accordance with the provisions of IFRS 8 Operating Segments, selected information in the annual financial statements is presented by operating segment and region, with segmentation being based on internal reporting to the chief operating decision maker. The chief operating decision maker is responsible for determining the allocation of resources to segments and reviewing their performance. The Management Board of LPKF AG has been defined as the Group's chief operating decision maker. Segment reporting aims to lend greater transparency to both the performance and potential of the Group's individual activities.

Primary segment reporting is based on the following segments:

- DevelopmentQuipment (DQ) comprises products such as circuit board plotters and ProtoLasers, primarily for electronics developers.
- The ElectronicsQuipment (EQ) segment combines production systems of the SMT, PCB, MID (LDS) and IC packaging product groups.
- WeldingQuipment comprises production systems for laser beam welding of plastic components.
- The SolarQuipment (SQ) segment develops and produces LaserScribers for the structuring of thin-film solar cells and laser systems for the digital printing of functional pastes and inks (laser transfer printing, LTP) which are used in production.
- The Other category contains some expense and income items which cannot be assigned to any of the other operating segments.

There is insignificant intersegment revenue. The existing goodwill (EUR 74 thousand) is allocated to the WeldingQuipment segment.

The segment information was determined as follows:

- The segment result (EBIT) is determined taking into account impairment of goodwill, but without taking into account the financial result and taxes.
- The investments and depreciation and amortization including impairment losses refer to property, plant and equipment and intangible assets including goodwill.
- The figures reported are those after consolidation.

EUR thsd.		EQ	DQ	WQ	SQ	Other	Total
External revenue	2016	30,579	22,662	23,985	13,898	0	91,124
	2015	29,934	25,527	23,260	8,484	50	87,255
Operating result (EBIT)	2016	–4,351	1,973	–99	–975	–3,300	–6,752
	2015	–619	3,348	119	–3,853	–2,712	–3,717
Depreciation, amortization and impairment losses (Fixed assets)	2016	3,505	1,752	1,657	1,045	98	8,057
	2015	3,238	1,995	1,114	693	112	7,152
Impairment losses (Inventories)	2016	3,608	1,036	745	1,165	0	6,626
	2015	123	62	0	0	0	185
Other non-cash expenses	2016	625	334	428	394	145	1,926
	2015	304	244	32	120	93	793

The allocation of expenses to the segments was changed in 2016. The prior-period figures were adjusted accordingly.

The impairment losses recognized on inventories are shown under cost of material.

GEOGRAPHICAL SEGMENTS:

Reporting reflects the four main geographical regions in which the Group is active.

EUR thsd.		Germany	Other Europe	North America	Asia	Other	Total
External revenue	2016	12,907	16,468	17,702	42,342	1,705	91,124
	2015	12,626	17,277	18,953	35,626	2,773	87,255
Assets	2016	92,224	5,533	6,044	13,135	0	116,936
	2015	89,392	5,803	7,722	15,903	0	118,820
Capital expenditures	2016	7,018	235	136	82	0	7,471
	2015	12,941	555	192	39	0	13,727

G. CONSOLIDATED INCOME STATEMENT

1. REVENUE

Revenue is recognized when the service has been rendered or the goods and products have been delivered.

One customer accounted for revenue of EUR 11 million. No single customer accounted for more than EUR 10 million in revenue in the previous year.

In addition to the sale of goods, there are no other significant categories of revenue in accordance with IAS 18.35.

2. OTHER OWN WORK CAPITALIZED

Own work capitalized by the Group concerned non-current assets amounted to EUR 4,902 thousand (previous year: EUR 6,914 thousand). This comprises own work for plant and machinery used by Group companies for production as well as prototype development projects capitalized during 2016 which are intended for permanent use in Group operations. Research costs are immediately expensed when they are incurred. Costs incurred in the context of development projects (in connection with the design and test runs of new or improved products) are recognized as intangible assets if the criteria of IAS 38.57 are met. Other development costs which do not meet these criteria are expensed on an accrual basis. Previously expensed development costs are not recognized as assets in subsequent reporting periods. Development costs recognized as intangible assets are amortized on a straight-line basis over their useful lives – up to a maximum of three years – from the time they become usable.

3. OTHER OPERATING INCOME

EUR thsd.	2016	2015
Income from insurance payments	2,164	2,961
Income from currency translation differences	1,044	1,718
Research and development grants	648	309
Income from the reversal of provisions	392	899
Reversal of deferred item income from grants	63	66
Income from the reversal of write-downs	25	224
Income from the disposal of non-current assets	18	26
Other	1,430	924
	5,784	**7,127**

Income from insurance payments mainly resulted from compensation for the loss suffered by the fire in Garbsen. Research and development grants are recognized in accordance with IAS 20 and exclusively concern government grants – in some cases with the involvement of private project companies. They are granted for costs actually incurred in connection with a specific purpose during the financial year (expenditure grant). Payments are made in line with project progress.

Grants received for capitalized development costs and other assets which have been recognized as deferred income are reversed on an accrual basis in accordance with the useful life of the associated capitalized development costs and other assets. The same applies to a grant for building costs in Suhl totaling EUR 943 thousand.

4. COST OF MATERIALS

EUR thsd.	2016	2015
Cost of (system) parts and purchased goods	29,927	24,362
Cost of purchased services	1,102	534
	31,029	**24,896**

The cost of materials includes EUR 6,262 thousand in impairment losses recognized on inventories (previous year: EUR 185 thousand).

5. STAFF COSTS AND EMPLOYEES

EUR thsd.	2016	2015
Wages and salaries		
Expenses for wages	36,345	36,299
Other	956	808
	37,301	**37,107**
Social security costs and pension costs		
Employer’s contribution to social security	6,139	6,137
Pension costs	208	227
Employer's liability insurance association	247	226
	6,594	**6,590**
	43,895	**43,697**

The item, social security costs and pension costs, includes contributions of EUR 2,223 thousand (previous year: EUR 2,328 thousand) to Germany's statutory pension scheme. There were ongoing pension payments of EUR 17 thousand (previous year: EUR 17 thousand) arising from pension obligations in financial year 2016 (also see note 17).

The workforce is distributed as follows:

	As of the reporting date		Annual average	
	31 Dec. 2016	31 Dec. 2015	2016	2015
Production	164	168	168	182
Sales	136	148	144	152
Development	159	179	173	174
Services	88	108	99	107
Administration	153	175	165	174
	700	**778**	**749**	**789**

6. DEPRECIATION, AMORTIZATION AND IMPAIRMENT LOSSES

Depreciation, amortization and impairment losses on non-current assets are shown in the statement of changes in non-current assets (note 10). An impairment loss of EUR 780 thousand was recognized on capitalized development costs in the reporting year (previous year: EUR 308 thousand).

7. OTHER OPERATING EXPENSES

EUR thsd.	2016	2015
Travel, meals/entertainment	3,030	3,455
Consumables, development and purchased development services	2,098	2,766
Rent, ancillary rental costs, leases, land and building costs	2,480	2,432
Repairs, maintenance, operating materials	2,137	3,282
Advertising and sales expenses	2,343	3,191
Third-party work	1,766	2,211
Sales commissions	1,332	865
Legal and consulting costs	933	1,439
Vehicle costs	799	761
Trade fair costs	794	997
Insurance, contributions, duties	779	834
Expenses for warranties	735	564
Telephone, postage, telefax	681	744
Exchange rate losses	601	1,619
Voluntary benefits, training and further education	462	926
Investor relations	440	434
Financial statements preparation, publication, auditing costs	314	284
Addition to allowance on receivables and bad debts	293	507
Bank charges	209	250
Supervisory Board remuneration incl. reimbursement of expenses	182	274
Office supplies, books, software	173	240
Other	712	1,012
	23,293	**29,087**

The item "repair, maintenance and operating materials", in the previous year was depressed by expenses incurred in connection with the loss suffered by the fire at the Garbsen site.

In 2016, total research and development costs or the effect on profit or loss were EUR 11,419 thousand (previous year: EUR 9,870 thousand). Besides EUR 4,044 thousand for materials and other costs (previous year: EUR 5,339 thousand), they also contain EUR 7,375 thousand (previous year: EUR 4,531 thousand) in additional costs for staff as well as depreciation, amortization and impairment losses, among other things.

8. FINANCIAL RESULT

EUR thsd.	2016	2015
Finance income		
Other interest and similar income	6	25
Finance costs		
Interest and similar expenses	– 832	– 705
	– 826	**– 680**

The other interest income arose from overnight and time deposits totaling EUR 6 thousand (previous year: EUR 19 thousand). At EUR 832 thousand (previous year: EUR 684 thousand), the other interest expense was incurred in connection with long-term loans as well as short-term money market loans.

Borrowing costs that are directly attributable to the acquisition or production of a qualifying asset are capitalized as part of the cost of that asset. Other borrowing costs are recognized as an expense in the period in which they are incurred.

9. INCOME TAXES

Actual and deferred taxes are reported in the income statement as tax expense or tax income unless they affect items recognized directly in equity. In this case, the taxes are recognized directly in equity.

EUR thsd.	2016	2015
Corporate income tax and solidarity surcharge	800	775
Trade tax	19	151
	819	**926**
Of which related to prior period	0	26
Deferred taxes	425	– 1,842
	1,244	**– 916**

The German entities of the LPKF Group are subject to trade tax of 15.1% or 15.4%, depending on the applicable trade tax assessment rate. As in the previous year, a corporate income tax rate of 15.0% plus a solidarity surcharge of 5.5% on corporate income tax applies. Foreign income taxes are calculated on the basis of the laws and regulations applicable in the individual countries. The income tax rates applicable to the foreign entities vary between 16.5% and 40.0%.

The corporate tax rates applicable in the respective countries were used to calculate the deferred tax assets and tax liabilities in connection with the preparation of the consolidated financial statements.

Reconciliation of estimated and actual tax expense:

EUR thsd.	2016	2015
Consolidated profit/loss before income taxes	– 7,578	– 4,397
Anticipated tax expense 30.0% (previous year: 30.0%)	– 2,273	– 1,319
Effect of different tax rates	– 27	– 169
Effect from unrecognized deferred tax assets	3,434	128
Effect from remeasurement of deferred tax assets	0	503
Tax-free income	– 122	– 200
Trade tax additions and deductions	18	29
Tax effect of non-deductible operating expenses	148	121
Prior-period tax effects	41	26
Other differences	25	– 35
Effective tax expense – 16.4% (previous year: 20.8%)	**1,244**	**– 916**

The tax rate applied for the reconciliation for 2016 and 2015 presented above corresponds to the corporate tax rate of 30% that is to be paid on taxable profits by the Company in Germany in accordance with German tax law.

The effect from unrecognized deferred tax assets results from the non-recognition of deferred tax assets on tax loss carryforwards in the amount of EUR 3,613 thousand (previous year: EUR 128 thousand) on the one hand and from the offsetting effect of utilizing previously unrecognized tax losses and temporary differenced in the amount of EUR 179 thousand (previous year: EUR 0 thousand) on the other.

H. CONSOLIDATED STATEMENT OF FINANCIAL POSITION

ASSETS

10. FIXED ASSETS

The following statement of changes in fixed assets shows the changes in the individual categories:

FIXED ASSETS 2016

	Cost					
EUR thsd.	Balance as of 01 Jan. 2016	Currency differences	Addition	Reclassi-fication	Disposal	Balance as of 31 Dec. 2016
Intangible assets						
Goodwill	74	0	0	0	0	74
Development costs	31,079	0	4,796	0	0	35,875
Other intangible assets	10,346	0	652	0	49	10,949
	41,499	**0**	**5,448**	**0**	**49**	**46,898**
Property, plant, and equipment						
Land, similar rights and buildings	48,050	82	268	5	0	48,405
Plant and machinery	11,465	– 27	1,163	210	627	12,184
Other equipment, operating and office equipment	13,628	– 12	592	– 202	153	13,853
Advances paid and construction in progress	13	0	0	– 13	0	0
	73,156	**43**	**2,023**	**0**	**780**	**74,442**
	114,655	**43**	**7,471**	**0**	**829**	**121,340**

The following table shows the corresponding figures for the previous year:

FIXED ASSETS 2015

	Cost					
EUR thsd.	Balance as of 01 Jan. 2015	Currency differences	Addition	Reclassi-fication	Disposal	Balance as of 31 Dec. 2015
Intangible assets						
Goodwill	74	0	0	0	0	74
Development costs	24,901	0	6,178	0	0	31,079
Other intangible assets	8,957	2	1,611	0	224	10,346
	33,932	**2**	**7,789**	**0**	**224**	**41,499**
Property, plant, and equipment						
Land, similar rights and buildings	44,021	258	2,218	1,553	0	48,050
Plant and machinery	9,634	88	1,793	530	580	11,465
Other equipment, operating and office equipment	13,330	115	1,779	– 3	1,593	13,628
Advances paid and construction in progress	1,945	0	148	– 2,080	0	13
	68,930	**461**	**5,938**	**0**	**2,173**	**73,156**
	102,862	**463**	**13,727**	**0**	**2,397**	**114,655**

	Depreciation, amortization and impairment losses					Residual carrying amounts	
	Balance as of 01 Jan. 2016	Currency differences	Addition	Disposal	Balance as of 31 Dec. 2016	Balance as of 31 Dec. 2016	Previous year
	0	0	0	0	0	74	74
	19,606	0	3,003	0	22,609	13,266	11,473
	8,355	0	712	46	9,021	1,928	1,991
	27,961	**0**	**3,715**	**46**	**31,630**	**15,268**	**13,538**
	8,396	14	1,384	0	9,794	38,611	39,654
	6,580	– 21	1,371	547	7,383	4,801	4,885
	7,491	– 20	1,586	133	8,924	4,929	6,137
	0	0	0	0	0	0	13
	22,467	**– 27**	**4,341**	**680**	**26,101**	**48,341**	**50,689**
	50,428	**– 27**	**8,056**	**726**	**57,731**	**63,609**	**64,227**

	Depreciation, amortization and impairment losses					Residual carrying amounts	
	Balance as of 01 Jan. 2015	Currency differences	Addition	Disposal	Balance as of 31 Dec. 2015	Balance as of 31 Dec. 2015	Previous year
	0	0	0	0	0	74	74
	18,258	0	1,348	0	19,606	11,473	6,643
	7,127	3	1,449	224	8,355	1,991	1,830
	25,385	**3**	**2,797**	**224**	**27,961**	**13,538**	**8,547**
	6,995	32	1,369	0	8,396	39,654	37,026
	5,793	75	1,279	567	6,580	4,885	3,841
	7,162	68	1,706	1,445	7,491	6,137	6,168
	0	0	0	0	0	13	1,945
	19,950	**175**	**4,354**	**2,012**	**22,467**	**50,689**	**48,980**
	45,335	**178**	**7,151**	**2,236**	**50,428**	**64,227**	**57,527**

10.1 Intangible assets

Software

As an intangible asset, purchased software is recognized at cost less straight-line amortization.

Goodwill

As a rule, the goodwill arising from business combinations (capitalized differences arising from acquisition accounting) is assumed to have an unlimited useful life. The carrying amount of the goodwill is compared to the recoverable amount at every reporting date. The goodwill is written down if its carrying amount exceeds its recoverable amount. It is assigned to a cash generating unit for an impairment test. Based on the WeldingQuipment segment, a detailed planning period of five years and an appropriate rate of return on capitalization are applied. Based on this, there was no impairment loss on goodwill in 2016, just as in the previous year.

Development costs

Own capitalized development costs are also reduced over their useful life using straight-line amortization. Borrowing costs are not capitalized. Instead, they are expensed in the period in which they are incurred unless they relate to qualifying assets pursuant to IAS 23. The item is broken down by segment as follows:

EUR thsd.	2016	2015
ElectronicsQuipment	7,526	7,783
DevelopmentQuipment	2,108	2,451
WeldingQuipment	2,747	1,200
SolarQuipment	885	39
	13,266	**11,473**

Both the residual carrying amounts and the useful lives of the intangible assets are tested for impairment, at a minimum, as of the end of every financial year. Pursuant to IAS 36, intangible assets are written down if the recoverable amount of the respective asset has dropped below its carrying amount. Capitalized development costs not yet available for use are tested for impairment annually. In addition to amortization, impairment losses of EUR 764 thousand were recognized in 2016 due to the discontinuation of the LDS development projects (previous year: EUR 308 thousand).

Reviews to determine whether write-ups are required for intangible assets written down in the past are conducted as of every reporting date; this does not concern the goodwill. No write-ups were necessary during the reporting year.

Intangible assets subject to amortization are deemed to have the following useful lives:

	Years
Software	3
Development costs	3

10.2 Property, plant and equipment

Property, plant and equipment is measured at cost less accumulated straight-line depreciation. Borrowing costs are not capitalized. Instead, they are expensed in the period in which they are incurred unless they relate to qualifying assets pursuant to IAS 23. Land is not depreciated. The residual carrying amounts and the useful lives of each item of property, plant and equipment are tested for impairment, at a minimum, as of the end of every financial year. Property, plant and equipment is tested for impairment if certain events or changes in circumstances indicate that the given carrying amount may no longer be recoverable.

Property, plant and equipment is written down in accordance with IAS 36 if the recoverable amount of the respective asset has dropped below its carrying amount. The recoverable amount is the higher of its value in use and fair value less costs to sell. Corresponding write-ups are made if the reasons for an earlier write-down no longer apply.

Production costs cover the costs of materials and related overheads as well as the manufacturing costs and related overheads.

They are deemed to have the following useful lives:

	Years
Buildings	33 or 25
External facilities	10
Plant and machinery	3 – 10
Other equipment, operating and office equipment	3 – 10

Bank loans totaling EUR 14,430 thousand (previous year: EUR 17,046 thousand) are secured by land and buildings.

Leases are classified as finance leases when substantially all of the risks and rewards of ownership are transferred to the lessee under the terms of the lease. All of the other leases are classified as operating leases.

At the inception of finance leases, the relevant assets are capitalized at the lower of the fair value of the leased property and the present value of the minimum lease payments and depreciated over their expected useful lives, analogous to the treatment of comparable own assets, or over the term of the contract, whichever is shorter. At this time, no assets have been recognized as finance leases.

11. INVENTORIES

Inventories are recognized at the lower of cost and net realizable value at the reporting date.

The costs of conversion of inventories include costs directly related to the units of production (such as production costs and directly attributable material costs). They also include a systematic allocation of fixed and variable production overheads that are incurred in converting materials into finished goods. Borrowing costs are not capitalized. Instead, they are expensed in the period in which they are incurred unless they relate to qualifying assets pursuant to IAS 23. Inventories are measured using the weighted average cost formula. Inventories were written down below cost to their net realizable value and scrapped by EUR 6,626 thousand (previous year: EUR 185 thousand).

Some inventories are subject to customary collateral such as reservations of title.

12. TRADE RECEIVABLES

EUR thsd.	2016	2015
Nominal amount of receivables	20,665	14,478
Specific valuation allowances incl. currency losses	– 670	– 628
Receivables after valuation allowances, discounts and currency losses	**19,995**	**13,850**

Trade receivables are measured at fair value on addition and subsequently at amortized cost using the effective interest rate method less impairment losses. An impairment of trade receivables is recognized if there is objective evidence that a receivable may not be fully recoverable on becoming due. The amount of the impairment is measured as the difference between the carrying amount of the receivable and the present value of the estimated future cash flows from this receivable, discounted at the effective interest rate. Impairment losses are recognized directly in equity and shown in an impairment loss item under trade receivables. Trade receivables are derecognized upon offsetting against previously recognized impairment losses if they are unrecoverable, e. g., if the given debtor is insolvent. Items recognized in foreign currencies are measured at the average exchange rate as of the reporting date.

In the reporting period, no revenue from construction contracts was recognized applying the percentage of completion method. As of 31 December 2015, one receivable from construction contracts in the amount of EUR 331 thousand was recognized. This amount was paid in early 2016.

The residual carrying amount of the trade receivables is EUR 214 thousand (previous year: EUR 257 thousand) and concerns receivables with remaining maturities of more than one year.

The following table describes the counterparty credit risk from trade receivables and receivables from borrowings and other assets as of 31 December 2016:

			Not impaired but past du since				
EUR thsd.	Carrying amount as of 31 Dec.	Of which not impaired and not past due	less than 30 days	between 30 and 60 days	between 60 and 90 days	between 90 and 360 days	more than 360 days
2016	**22,067**	16,873	3,144	265	68	821	226
2015	**15,822**	9,196	4,012	933	508	548	3

There is no indication that the recoverability of receivables has suffered if they are neither past due nor impaired.

Valuation allowances recognized on trade receivables and borrowings in EUR thsd.	2016	2015
Balance on 1 Jan.	**628**	**536**
+ Additions	69	502
– Reversals (allowances not required)	25	224
– Uses (allowances required)	2	187
+/– Currency differences (foreign currency receivables)	0	1
Balance on 31 Dec.	**670**	**628**

There were proceeds of EUR 21 thousand from derecognized receivables in the 2016 financial year (previous year: EUR 0 thousand).

13. OTHER ASSETS AND INCOME TAX RECEIVABLES

With the exception of derivatives, the other assets and current tax receivables are measured at cost. Derivatives are measured at their fair value, non-current tax receivables at the present value of the future rights to reimbursement.

EUR thsd.	2016	2015
Input tax receivables	503	666
Income tax receivables	434	282
Deferred income	437	703
Other	899	1,306
Total	**2,273**	**2,957**

Rights to reimbursement of corporate income and trade taxes are reported in tax receivables. Corporate income tax receivables with a remaining maturity of more than one year amount to EUR 0 thousand (previous year: EUR 46 thousand).

14. CASH AND CASH EQUIVALENTS

Cash and cash equivalents comprise cash on hand of EUR 5 thousand (previous year: EUR 5 thousand) and bank balances of EUR 3,579 thousand (previous year: EUR 3,790 thousand); they are reported at their nominal value. Cash and cash equivalents in foreign currencies are translated at the respective reporting date exchange rate.

15. DEFERRED TAXES

Deferred taxes are determined using the liability method pursuant to IAS 12. Accordingly, deferred taxes are recognized for all temporary differences between the tax base of the assets and liabilities and their carrying amounts in the consolidated statement of financial position. Deferred tax assets are recognized only if it is probable that adequate earnings will be available in future periods to offset the tax benefits. Income tax liabilities are netted against income tax receivables within the same fiscal territory if maturity and type are matched.

The income taxes are calculated in accordance with applicable laws and regulations.

The capitalized deferred tax assets encompass deferred taxes on intercompany profits. The deferred tax liabilities largely concern capitalized development costs. The deferred taxes consist of the following:

Deferred tax assets

EUR thsd.	2016	2015
Tax loss carryforwards	4,220	3,666
Intangible assets	227	145
Trade receivables	0	99
Provisions	293	294
Elimination of intercompany profits and other deductible temporary differences	1,443	1,835
Other	32	25
Offsetting with deferred tax liabilities	**–3,701**	**–3,165**
Total	**2,514**	**2,899**

Deferred tax liabilities

EUR thsd.	2016	2015
Capitalized development costs	3,980	3,442
Property, plant and equipment	135	118
Trade receivables	86	92
Other	12	1
Offsetting with deferred tax liabilities	– 3,701	– 3,165
Total	**512**	**488**

Within the next twelve months, EUR 1,927 thousand (previous year: EUR 2,070 thousand) in deferred tax assets and EUR 97 thousand (previous year: EUR 93 thousand) in deferred tax liabilities will be realized.

For entities which in the reporting period or in the previous year made a tax loss, deferred tax assets in the amount of EUR 1,675 thousand (previous year: EUR 1,709 thousand) are recognized because planning assumes the achievement of taxable profits. In these cases it is assumed that new products will be marketed successfully or that realignment in the respective region will result in cost savings. The amount for tax losses not yet used and temporary differences for which no deferred tax assets were recognized in the statement of financial position, was EUR 13,603 thousand (previous year: EUR 1,786 thousand).

No deferred tax liabilities were recognized on EUR 968 thousand (previous year: EUR 1,199 thousand) in temporary differences related to investments in subsidiaries and branches.

EQUITY AND LIABILITIES

16. SUBSCRIBED CAPITAL

Share capital

The Company's share capital amounts to EUR 22,269,588.00. It is fully paid-in and denominated in 22,269,588 no-par bearer shares with an interest in capital of EUR 1.00 per share.

The capital reserves comprise only a capital reserve pursuant to Section 272 (2) no. 1 German Commercial Code.

There is no ban on dividend distributions with respect to net retained profits, since sufficient revenue reserves are available.

Authorized capital

With the resolution adopted by the Annual General Meeting on 5 June 2014, the Management Board is authorized to increase the share capital once or repeatedly until 4 June 2019 with the approval of the Supervisory Board by up to a total of EUR 11,134,794.00 by issuing up to 11,134,794 new no-par value bearer shares in return for contributions in cash or in kind (authorized capital). Shareholders shall generally be granted a subscription right in that connection.

However, the Management Board is authorized with the approval of the Supervisory Board to disapply the pre-emptive rights of shareholders

- to exclude fractional amounts from shareholders' pre-emptive rights;
- if the new shares are issued in return for cash contributions and the issue price of the new shares is not significantly lower than the stock exchange price of the shares currently listed when the issue price is finally determined. The number of shares issued while thus disapplying shareholders'

pre-emptive rights may not exceed a total of 10% of the share capital, neither at the time when this authorization takes effect nor when it is exercised. Other shares that are issued or were sold during the period in which this authorization is in effect while disapplying shareholders' pre-emptive rights in direct or corresponding application of section 186(3) sentence 4 of the Stock Corporation Act (Aktiengesetz, AktG) are to be counted toward this upper limit of 10% of the share capital. Shares that are issued to service option rights and/or conversion rights or conversion obligations from convertible bonds or bonds with warrants or profit participation rights are also to be counted toward this limit if such debt securities or profit participation rights are issued during the period in which this authorization is in effect while disapplying shareholders' pre-emptive rights in corresponding application of section 186(3) sentence 4 AktG;

- if the capital increase is carried out in return for contributions in kind for the purpose of acquiring entities, business divisions, equity investments, other assets related to an intended acquisition or in connection with mergers or for the purpose of acquiring industrial property rights, including copyrights and know-how or rights to use such rights;
- if it is necessary to grant subscription rights for new shares to the bearers or creditors of bonds with warrants and convertible bonds or profit participation rights with option rights or conversion rights and/or conversion obligations that were or will be issued by the Company or companies in which the Company holds a direct or indirect majority interest in the volume to which they would be entitled after exercising the option rights or conversion rights or after conversion obligations are fulfilled;
- if the new shares are issued to individuals who are in an employment relationship with the Company or its affiliated companies. The number of shares issued while disapplying shareholders' pre-emptive rights may not exceed a proportionate interest in the share capital in the total amount of EUR 200,000.00.

In any case, the authorization to disapply shareholders' preemptive rights is limited insofar as after exercising the authorization the sum of shares issued while disapplying shareholders' pre-emptive rights in exchange for contributions in cash or in kind under this authorized capital may not exceed a total of 10% of the share capital, neither at the time that this authorization takes effect nor when it is exercised. The following count toward the aforementioned 10% limit:

- treasury shares that are sold during the period in which this authorization is in effect while disapplying shareholders' pre-emptive rights, as well as
- new shares that are to be issued on the basis of convertible bonds or bonds with warrants or profit participation rights issued during the period in which this authorization is in effect while disapplying shareholders' pre-emptive rights.

The Management Board is authorized with the approval of the Supervisory Board to determine the contents of the share rights, the further details of the capital increase, and the terms and conditions under which the shares are issued, in particular the issue price.

The Supervisory Board is authorized to revise the Articles of Association accordingly after utilization of the authorized capital or the expiration of the period for utilizing the authorized capital.

The authorization to increase the share capital was not exercised before the reporting date.

Treasury shares

The Management Board was authorized by resolution of the Annual General Meeting on 28 May 2015, subject to the Supervisory Board's prior approval, to buy back treasury shares until 27 May 2020 corresponding to up to 10% of the Company's share capital either on the date the resolution was adopted or on the date the authorization is exercised, whichever is higher; to use the treasury shares so acquired for all statutory purposes; and, in particular cases, to disapply shareholders' right to tender or subscribe such shares, respectively, in connection with buybacks and subscriptions. This authorization was not utilized as of the reporting date.

17. PROVISIONS FOR PENSIONS AND SIMILAR OBLIGATIONS

The following obligations are recognized for this item in the consolidated financial statements:

a) Retirement benefits
b) Anniversary payments and benefits similar to pensions

a) Retirement benefits

Germany has a statutory defined-contribution national pension scheme for employees that pays pensions contingent on income and contributions made. Except for the payment of its contributions to the statutory pension insurance entity, the Company has no other benefit obligations. As part of the Company pension plan and based on a shop agreement, some of the Group's employees have also taken out policies with a private insurer or a benevolent fund. In this case, too, the Company has no other benefit obligations above and beyond the cost of contributions that are reported in current staff costs.

The pension provisions reported in the statement of financial position comprise only defined-benefit obligations to former Management Board members of the parent company for which fixed retirement benefits have been stipulated. The plan is financed through payments to a fund and to insurance companies. The promised benefits comprise payments for retirement pensions, disability pensions and widow's and orphan's pensions. Once the age threshold has been attained by reaching the end of the 65th year of life, or if eligibility to receive a disability pension is established prior to reaching the end of the 65th year of life, a commitment is made to pay the beneficiary a monthly pension payment for life. The widow's pension paid to a surviving wife amounts to 60% or 70% of the relevant retirement pension entitlement. The weighted average term of the defined benefit plans is 17.5 years.

There is longevity and interest rate risk with regard to the pension provision. Reinsurance policies were obtained for hedging purposes and pledged to the beneficiaries. The fair value amounts are reported in the offsetting and reconciliation of the excess of plan assets over post-employment benefit liability.

The carrying amount in the statement of financial position of the net liabilities (assets) for defined benefit plans in accordance with IAS 19 corresponds to the present value of the defined benefit obligation (DBO) on the balance sheet date less the fair value of the plan assets. The DBO is calculated annually by an independent actuary using the projected unit credit method. The DBO's present value is determined by discounting the expected future cash outflows at the interest rate of high-quality corporate bonds. The resulting revaluations (mainly actuarial gains and losses) in connection with the remeasurement of net liabilities (assets) are recognized directly in other comprehensive income (OCI) due to the amendment of IAS 19.

The following amounts were reported in the statement of financial position for defined benefit plans:

EUR thsd.	2016	2015
Present value of the defined benefit obligation at beginning of period	**668**	**709**
Current service cost	0	0
Interest expense	15	14
Pension payments	– 17	– 17
Actuarial gains (–) and losses (+)	89	– 38
Present value of the defined benefit obligation at end of period	**755**	**668**
Plan assets		
Reinsurance coverage	– 288	– 267
Securities	– 463	– 485
Deficit (net liability) / excess (net asset) shown in the statement of financial position	**4**	**– 84**

Development of net liabilities / assets:

EUR thsd.	2016
Net assets at beginning of period	– 84
Total amount in the income statement	– 2
Total of the revaluations recognized in OCI	106
Benefit payments	0
Employer contributions	– 16
Net liabilities at end of period	**4**

All defined benefit plans are covered by plan assets; there are no unfunded plans. The fair value of the plan assets developed as follows:

EUR thsd.	2016	2015
At beginning of period	752	723
Interest income from plan assets	17	15
Expected return on plan assets without interest income	– 17	15
Payments from plan assets	– 17	– 17
Funded by the employer	16	16
At end of period	**751**	**752**

The plan assets are made up as follows:

	2016		2015	
EUR thsd.	Absolute	Percentage	Absolute	Percentage
Equity securities	0	0%	0	0%
Debt securities	463	62%	485	64%
Other	288	38%	267	36%
	751	**100%**	**752**	**100%**

The debt securities include mixed fund shares that are primarily invested in fixed-income securities. As in the previous year, the plan assets do not contain any financial instruments.

The following amounts were recognized in the income statement:

EUR thsd.	2016	2015
Current service cost	0	0
Interest income from plan assets	17	15
Interest expense related to the liability	– 15	– 14
Total effect on earnings in the income statement	**2**	**1**

The provisions for pensions were determined based on the following assumptions:

%	2016	2015
Discount rate as of 31 December	1.50	2.30
Future salary increases	0.00	0.00
Future pension increases	1.75	1.75
Expected return on plan assets	1.50	2.30
Employee turnover	0.00	0.00

The determination of the expected return on the plan assets was based on the estimated return on the assets, taking the changes in the yields of non-current fixed-income instruments into account. The allocations to plans for post-employment benefits and pension payments payable in the financial year ending 31 December 2016 are estimated to total EUR 33 thousand.

The undiscounted pension payments based on the average life expectancy of 17.5 years result in the following maturity analysis:

31 Dec. 2016 in EUR thsd.	up to 1 year	more than 1 and up to 5 years	more than 5 and up to 10 years	Total
Retirement benefits	17	68	202	287

Regarding possible changes in the significant actuarial assumptions made, the following sensitivities were determined:

Basic values	
Discount rate	1.50%
Pension trend	1.75%
DBO	EUR 755,399

Sensitivities	Revalued DBO	Change in percent of the DBO
Discount rate plus 0.5%	EUR 694,849	– 8.02%
Discount rate minus 0.5%	EUR 823,741	9.05%
Pension trend plus 0.25%	EUR 779,294	3.16%
Pension trend minus 0.25%	EUR 732,532	– 3.03%

b) Anniversary payments and benefits similar to pensions

One Group company is obligated to pay its employees a benefit equal to three months of an employee’s salary based on the most recently paid salary when employment is terminated due to the employee reaching the maximum age threshold. In addition, the company is required to pay a benefit calculated based on the attainment of a certain number of years of service with the company. The company, which is included in the consolidated financial statements, meets these obligations itself as soon as they come due. These obligations are measured annually by an independent actuary. No plan assets are maintained for this purpose. The amount of the obligation is therefore reported in the statement of financial position under provisions for pensions.

Payments totaling EUR 46 thousand are expected in the following five years.

The amounts recognized in the statement of financial position are comprised as follows:

EUR thsd.	2016	2015
Present value of the defined benefit obligation at beginning of period	**352**	**276**
Current service cost	28	23
Interest expense	6	6
Benefit payments	– 9	– 2
Benefit changes	0	– 13
Actuarial gains (–) and losses (+)	– 92	62
Present value of the defined benefit obligation at end of period	**285**	**352**

The following amounts were recognized in the income statement:

EUR thsd.	2016	2015
Current service cost	28	23
Interest expense related to the liability	6	6
Total amount in the income statement	**34**	**29**

Regarding possible changes in the significant actuarial assumptions made, the following sensitivities were determined:

Basic values	
Discount rate	1.75%
Salary trend	3.00%
DBO	EUR 285,301

Sensitivities	Revalued DBO	Change in percent of the DBO
Discount rate minus 0.5%	EUR 308,762	8.22%
Discount rate plus 0.5%	EUR 264,238	– 7.38%
Salary trend minus 0.5%	EUR 264,358	– 7.34%
Salary trend plus 0.5%	EUR 308,374	8.09%

18. TAX PROVISIONS AND OTHER PROVISIONS

Provisions are recognized for legal or constructive obligations resulting from past events if it is probable that settling the obligation will lead to an outflow of Group resources and that a reliable estimate of the amount of the obligation can be made. Provisions are recognized at their estimated settlement value in accordance with IAS 37.

The tax provisions concern the following:

EUR thsd.	2016	2015
Corporate income tax and solidarity surcharge	116	242
Trade tax	62	132
	178	**374**

Statement of changes in provisions

EUR thsd.	Balance as of 01 Jan. 2016	Use	Currency differences	Reversals	Addition	Balance as of 31 Dec. 2016
Pension provisions and similar obligations	352	26	–	90	54	290
Tax provisions	374	258	4	4	62	178
Bonus	594	594	–	–	353	353
Warranty and guarantee	1,640	740	–	276	1,375	1,999
Other	772	620	–	31	715	836
Total	**3,732**	**2,238**	**4**	**401**	**2,559**	**3,656**

The provisions for guarantees and warranties cover potential statutory or financial obligations under guarantee and goodwill cases. Other provisions mainly include provisions for severance payments, litigation and share-based payment plans settled in cash in accordance with IFRS 2. With the exception of a portion of the provision for severance payments, all provisions stated are due within one financial year.

In 2012, a long-term incentive program (LTI) was launched in which a selected group of LPKF Group executives can participate. The beneficiaries are entitled to a long-term bonus, Which is paid to the beneficiaries depending on the long-term bonus allotment granted to each individual, the average EBIT margin of the LPKF Group during a four-, five- or six-year performance period and the performance of LPKF's share price. The program does not stipulate settlement by granting of equity instruments. The first prerequisite for payment of the bonus is an investment in LPKF shares to be made and held throughout the entire duration of the long-term bonus plan. The beneficiaries must also have an unterminated employment contract as of 20 July of the year in which the payment is made.

At plan inception, a preliminary number of phantom stocks corresponding to the allotment value is specified, which represents the starting point for calculating the bonus payment. At the end of the performance period, the final number of phantom stocks is determined. The performance period amounts to at least four years, but can be extended to five, or no more than six, years upon request by an individual beneficiary. The final number of virtual shares is determined based on an in-house measure of the Company's success, the EBIT margin. If the target is exceeded or the actual figure falls short of the target, the preliminary number of phantom stocks at the time of the allotment is increased or decreased accordingly. The payment amount is determined by measuring the value of the phantom stocks using the average XETRA closing quote for LPKF shares on the 30 trading days prior to 21 July after the end of the four-, five- or six-year performance period. The amount of the payment is limited to no more than 300% of the individual allotment value.

Reporting of share-based compensation transactions settled in cash is governed by IFRS 2 “Share-based Payment.” The expense expected to arise from the long-term bonus program is estimated at fair value at each reporting date using a Monte Carlo simulation. The expected total expense from the program is distributed pro rata temporis across the time period up to the first possible exercise date. On this basis, the amount of the provision in the Group for financial year 2016 is EUR 0 thousand (previous year: EUR 12 thousand). Mainly due to the impact the consolidated net profits generated in 2014, 2015 and 2016 had on the average EBIT margin applicable to all tranches’ performance periods, a total of EUR 6 thousand was reversed in the reporting period and EUR 71 thousand in the previous year.

The following parameters were used in the option price model (modified Black Scholes (Merton) model) for determining the fair value as of 31 December 2016:

	Tranche 2, 2013	Tranche 3, 2014	Tranche 4, 2015	Tranche 5, 2016
Expected volatility	47%	47%	47%	47%
Risk-free interest rate	0.00% p.a.	0.00% p.a.	0.00% p.a.	0.00% p.a.
Expected remaining maturity	2 years and 7 months	3 years and 7 months	4 years and 7 months	5 years and 7 months
Price of the LPKF share on 30 December 2016	EUR 6.95	EUR 6.95	EUR 6.95	EUR 6.95
Initial price of the LPKF share	EUR 12.10	EUR 15.02	EUR 8.08	EUR 6.18
Number of phantom stocks at the allotment date	3,822	4,803	10,359	11,938

Separate plan terms were introduced for the members of the Management Board in 2014. The main difference is the programs’ terms, which begin on 1 January of each year for the members of the Management Board instead of on 21 July. The following parameters were used in the option price model (modified Black Scholes (Merton) model) for determining the fair value for the Management Board program as of 31 December 2016:

	Tranche 1, 2014	Tranche 2, 2015	Tranche 3, 2016
Expected volatility	47%	47%	47%
Risk-free interest rate	0.00% p.a.	0.00% p.a.	0.00% p.a.
Expected remaining maturity	3 years	4 years	5 years
Price of the LPKF share on 30 December 2016	EUR 6.95	EUR 6.95	EUR 6.95
Initial price of the LPKF share	EUR 18.25	EUR 10.97	EUR 7.72
Number of phantom stocks at the allotment date	4,110	11,395	0

Recognition of the expected volatility is based on the historical volatility of the previous two years. The resulting volatility is rounded to full percentage points.

19. LIABILITIES

Upon initial recognition, financial liabilities are measured at fair value after deduction of transaction costs. They are subsequently measured at amortized cost. Any difference between the disbursement amount (after deduction of transaction costs) and the repayment amount is amortized over the term of the loan using the effective interest method.

The breakdown of the liabilities by remaining maturities follows from the statement of changes in liabilities below:

Type of liability in EUR thsd.		Total amount	Liabilities with remaining maturities of: up to 1 year	1 to 5 years	more than 5 years	Collateralized amounts	Type of collateral
Liabilities to banks	2016	43,482	20,852	19,584	3,046	14,430	*,**
	2015	41,107	15,627	20,380	5,100	17,046	*,**
Trade payables	2016	3,071	3,071	0	0	0	–
	2015	2,278	2,278	0	0	0	–
Other liabilities	2016	11,206	11,206	0	0	0	–
	2015	6,982	6,982	0	0	0	–
	2016	**57,759**	**35,129**	**19,584**	**3,046**	**14,430**	
	2015	**50,367**	**24,887**	**20,380**	**5,100**	**17,046**	

* Land charge, assignments of the receivable

** Security assignment

The loans are earmarked for financing new construction, purchases of real property, investments to expand capacities and development projects.

I. OTHER DISCLOSURES

20. STATEMENT OF CASH FLOWS

The statement of cash flows is derived from the consolidated financial statements using the indirect method; pursuant to IAS 7, it presents the changes in cash flows broken down by inflows and outflows for operating activities, investing activities and financing activities. Cash comprises cash on hand and demand deposits. Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

21. EARNINGS PER SHARE

According to IAS 33, basic earnings per share are determined by dividing the consolidated net profit for the year attributable to the shareholders of LPKF Laser & Electronics AG by the weighted number of shares outstanding during the financial year. There are currently no transactions triggering dilution.

	2016	2015
Number of shares, undiluted	22,269,588	22,269,588
Number of shares, diluted	22,269,588	22,269,588
Consolidated net profit/loss (in EUR thsd.)	–8,822	–3,481
Basic earnings per share (in EUR)	–0.40	–0.16
Diluted earnings per share (in EUR)	–0.40	–0.16

22. DIVIDEND PER SHARE

The Management Board and the Supervisory Board will propose to the Annual General Meeting on 1 June 2017 that it resolve to carry the net accumulated losses of LPKF Laser & Electronics AG in the amount of EUR 1,201,183.01 for the 2016 financial year (previous year: net retained profits of EUR 4,333,645.77) forward to new account.

23. TRANSACTIONS WITH RELATED PARTIES

There are no reportable business relationships with parties related to the LPKF Group.

As of the reporting date, LPKF AG had EUR 214 thousand in liabilities to members of the Supervisory Board (previous year: EUR 214 thousand).

For the rest, there are no other receivables from or liabilities to LPKF Group companies, nor were any payments or benefits granted to related parties. Notes 27 and 28 provide details on the corporate bodies of LPKF AG.

24. GERMAN CORPORATE GOVERNANCE CODE

The Declaration of Compliance by the Supervisory Board and the Management Board required under Section 161 German Stock Corporation Act on the application of the recommendations of the Government Commission of the German Corporate Governance Code, as well as the disclosures of any noncompliance with the recommendations, were made available to the shareholders on the Company's website (http://www.lpkf.com/investor-relations/corporate-governance/declaration-compliance.htm).

25. OTHER DISCLOSURES

Other financial liabilities

Short- and mid-term leases for land and buildings are in place for the offices of LPKF (Tianjin) Co. Ltd., LPKF Laser & Electronics (Hong Kong) Ltd., LPKF Laser & Electronics K.K., LPKF Laser & Electronics Korea Ltd. and for LPKF SolarQuipment GmbH at the Mainz site and for a production hall in Suhl. Furthermore, auto leases are in place at LPKF LaserMicronics GmbH, LPKF SolarQuipment GmbH, LPKF WeldingQuipment GmbH and the parent company.

The existing auto leases are classified as operating leases. The lease payments are determined by the term of the given lease and the car's mileage. There are no other provisions or agreements with respect to the extension of maturities or favorable purchasing options. Total future lease payments broken down by maturity are:

EUR thsd.	2016	2015
Lease payments included in the net profit/loss for the period	612	689
up to 1 year	459	445
more than 1 year and up to 5 years	478	326

All future rental payments due under building and office leases are broken down by maturity as follows:

EUR thsd.	2016	2015
up to 1 year	438	575
more than 1 year and up to 5 years	99	251

There are no other significant financial obligations.

Financial Instruments

The financial instruments reported in the statement of financial position (financial assets and financial liabilities) as defined in IAS 32 and IAS 39 comprise specific financial assets, trade receivables, cash, trade payables as well as certain other assets and liabilities under agreements.

1. Non-derivative financial instruments

IAS 39 makes a general distinction between non-derivative and derivative financial instruments and classifies non-derivative financial instruments into the following categories:

- Financial assets or liabilities at fair value through profit or loss;
- Held-to-maturity investments;
- Loans and receivables;
- Available-for-sale financial assets

The “financial assets or liabilities at fair value through profit or loss” category has two sub-categories: Financial assets that have been classified as held for trading from inception, and those that are designated upon initial recognition as at fair value through profit or loss. A financial asset is allocated to this category if it was acquired principally for the purpose of selling it in the near term or was designated as such by management. Derivatives also belong to this category unless they qualify as hedges.

There are no non-derivative financial instruments that are designated as “financial assets or financial liabilities at fair value through profit or loss” or “financial instruments held to maturity.”

Loans and receivables primarily concern loans to third parties, receivables, other assets as well as cash and cash equivalents. The initial measurement is at fair value plus transaction costs, subsequent measurements at amortized cost using the effective interest method.

The financial instruments are classified as non-current assets if management does not intend to sell them within twelve months of the reporting date.

Settlement date accounting is used for reporting purchases and sales of previously recognized assets. Financial assets are derecognized when the rights to the cash flows from the financial assets have expired or were transferred and the Group has transferred substantially all of the risks and rewards of ownership.

Impairment is assumed if payment is substantially delayed or insolvency proceedings have been opened.

2. Derivative financial instruments

The Group uses various derivative financial instruments to hedge future transactions and cash flows. Particularly derivatives such as forwards, options and swaps are used to that end. Special hedge accounting rules may be applied under IAS 39 if certain conditions are met. The hedging relationship between the hedged item and the hedging instrument must be documented, and its effectiveness must be evidenced. The accounting principles of IAS 39 shall be used if the requirements for application of the special hedge accounting rules do not apply.

The existing forward contracts and options do not qualify for hedge accounting pursuant to IAS 39.71 ff. All these derivatives are therefore designated as held for trading (a subcategory of the category, “assets and liabilities at fair value through profit or loss”) and recognized at fair value in the statement of financial position. Fair value changes are recognized in profit or loss. The issuing banks notified the Group of the fair values (market values). The measurement took current ECB reference prices and forward premiums or discounts into account. If the fair value is positive, these instruments are recognized in current assets, otherwise under current liabilities. The current liabilities contain one forward transaction in USD with a negative fair value of EUR – 36 thousand.

3. Disclosures pursuant to IFRS 7

Carrying amounts, reporting amounts and fair values by measurement category

			IAS 39 carrying amount			
EUR thsd.	Measurement category pursuant to IAS 39	Carrying amount 31 Dec. 2016	Amortized cost	Fair value recognized in equity	Fair value through profit or loss	Fair value 31 Dec. 2016
Assets						
Cash and cash equivalents	LaR	3,584	3,584			3,584
Trade receivables	LaR	19,995	19,995			19,995
Other assets	LaR	856	856			856
Derivative financial assets						
Derivatives	FAHfT					
Equity and liabilities						
Trade payables	FLAC	3,071	3,071			3,071
Liabilities to banks	FLAC	43,482	43,482			43,311
Other interest-free liabilities	FLAC	1,587	1,587			1,587
Derivative financial liabilities						
Derivatives	FLHfT	36			36	36
Of which accumulated by IAS 39 measurement category						
Loans and receivables;	(LaR)	24,435	24,435			24,435
Assets held for trading	(FAHfT)					
Financial liabilities measured at amortized cost	(FLAC)	48,140	48,140			47,969
Liabilities held for trading	(FLHfT)	36			36	36

LaR	Loans and Receivables
FLAC	Financial Liabilities Measured at Amortized Cost
FAHfT	Financial Assets Held for Trading
FLHfT	Financial Liabilities Held for Trading

			IAS 39 carrying amount			
	Measurement category pursuant to IAS 39	Carrying amount 31 Dec. 2015	Amortized cost	Fair value recognized in equity	Fair value through profit or loss	Fair value 31 Dec. 2015
	LaR	3,795	3,795			3,795
	LaR	13,850	13,850			13,850
	LaR	1,287	1,287			1,287
	(FAHfT)	11			11	11
	FLAC	2,278	2,278			2,278
	FLAC	41,107	41,107			38,389
	FLAC	1,504	1,504			1,504
	FLHfT					
	(LaR)	18,932	18,932			18,932
	(FAHfT)	11			11	11
	(FLAC)	44,889	44,889			42,171

Because of short remaining maturities, the fair values of cash and cash equivalents, current receivables, trade payables as well as current financial assets and liabilities closely correspond to the respective carrying amounts. The carrying amount of the derivative financial instruments corresponds to their fair value (Level 2 of the fair value hierarchy).

The financial instruments designated as financial assets held for trading in the amount of EUR 0 thousand (previous year: EUR 11 thousand) and as financial liabilities held for trading in the amount of EUR 36 thousand (previous year: EUR 0 thousand) have been allocated to Level 2 of the fair value hierarchy. Level 2 requires availability of a stock or market price for a similar financial instrument or calculation parameters based on data from observable markets. The measurement takes current ECB reference prices and forward premiums or discounts into account based on a discounted cash flow method.

There were no financial instruments that had to be classified to Level 3 of the fair value hierarchy.

The net gains / losses from financial instruments are as follows:

EUR thsd.		2016	2015
Loans and receivables	(LaR)	408	26
Assets and liabilities held for trading	(FAHfT) + (FLHfT)	0	– 23
Financial liabilities measured at amortized cost	(FLAC)	832	684
		1,240	**687**

The net gains / losses from loans and receivables include changes in allowances, gains and losses on derecognition / disposal, payments received, reversals of write-downs on loans and receivables as well as currency translation.

Net gains and losses from financial assets and liabilities held for trading contain changes in the fair value of the derivative financial instruments not subject to hedge accounting as well as gains and losses on maturity during the reporting period.

Net gains and losses from financial liabilities recognized at amortized cost comprise gains and losses on disposal and currency translation. Total interest expense using the effective interest method was EUR 832 thousand.

There are no significant counterparty credit risks by customer group or geographical region. Loans and receivables are securitized in part through credit insurance or bank guarantees (LC). For the rest, the maximum exposure to lending risks corresponds to the carrying amount of the aforementioned receivables by class.

Maturity analysis as of 31 December

Trade payables EUR thsd.	Carrying amount as of 31 Dec.	up to 6 months	6 months up to 1 year	between 1 year and 5 years	more than 5 years
2016	3,071	3,071	0	0	0
2015	2,278	2,278	0	0	0

Financial obligations and loans EUR thsd.	Carrying amount as of 31 Dec.	up to 6 months	6 months up to 1 year	between 1 year and 5 years	more than 5 years
2016	43,482	19,446	1,405	19,584	3,047
2015	41,107	14,200	1,427	20,380	5,100

Other interest-free liabilities EUR thsd.	Carrying amount as of 31 Dec.	up to 6 months	6 months up to 1 year	between 1 year and 5 years	more than 5 years
2016	1,587	1,587	0	0	0
2015	1,504	1,504	0	0	0

Derivative financial instruments EUR thsd.	Carrying amount as of 31 Dec.	up to 6 months	6 months up to 1 year	between 1 year and 5 years	more than 5 years
2016	36	36	0	0	0
2015	11	11	0	0	0

4. Hedging policy and risk management

Risk management principles

The assets, liabilities and planned transactions of LPKF Laser & Electronics AG are exposed, in particular, to risks from fluctuations in foreign exchange rates and interest rates. The aim of financial risk management is to limit these risks. Depending on the nature of the risk, this primarily involves the use of derivative financial instruments. These instruments are exclusively used for hedging, i. e. they are not used for trading or speculative purposes.

Risk management is handled by the Management Board, which fixes the general guidelines for risk management and determines the relevant procedures. It is implemented by the technical departments and subsidiaries subject to compliance with authorized business guidelines and coordinated by the Group Risk Officer.

The material risks from financial instruments and the attendant risk management system of the LPKF Group are disclosed below.

Currency risks

The currency risks to which the LPKF Group is exposed mainly arise from receivables, liabilities, cash and future transactions in foreign currencies. Assets recognized in currencies with declining exchange rates decline in value whereas liabilities reported in currencies with rising exchange rates increase in value. From the Group's point of view, only the difference between income and expense in a foreign currency is exposed to risk.

As a rule, risks are only hedged if they have an impact on the Group's cash flows. Foreign currency risks that have no impact on the Group's cash flows are not hedged. These include risks from the translation of the assets and liabilities reported in the annual financial statements of foreign subsidiaries into euros, the Group's reporting currency. Most invoices related to operations are written in euros; sales in North America are invoiced in USD. Cash flows in JPY and other foreign currencies are required in some cases.

To the extent possible, the Group pays for its procurement in USD, thus following a natural hedge philosophy. In net terms, however, this does give rise to USD cash inflows. Foreign currency forward contracts or currency options are used to hedge foreign currency inflows contracted for up to 12 months. Foreign currency hedges cannot fully offset the negative effects of the euro's continued strength against the US dollar on the Group's competitive position.

Changes in the fair value of the derivatives used to hedge currency risks that arise from foreign exchange rates and changes in the hedged item in the statement of financial position during the same period are virtually balanced in the income statement.

The disclosure of market risks requires sensitivity analyses pursuant to IFRS 7. They show the effects of hypothetical changes in the relevant risk variables on performance and equity. Currency risks arising from changes in the USD exchange rate have priority for LPKF in this respect. The periodic effects are determined by relating the hypothetical changes in the risk variables to the holdings of financial instruments as of the reporting date. The assumption is that the value of the holdings as of the reporting date is representative for the whole year. Differences from foreign-currency translation of the annual financial statements of foreign subsidiaries into euros, the Group's functional currency, are not taken into account.

The currency sensitivity analysis is based on the following assumptions:

Interest income or expenses associated with financial instruments are either reported directly in the functional currency or translated into the functional currency by way of derivatives. This means that the figures analyzed cannot have material consequences.

Pursuant to IFRS 7, the analysis only shows the effects of exchange rate changes on financial instruments held by the Group as of the reporting date.

If the euro had risen by 10% against the USD dollar, earnings before income taxes would have been reduced by EUR 89 thousand. A 10% decline in the euro would have raised earnings (before income taxes) by EUR 50 thousand.

Interest rate risks

Interest rates give rise to cash flow risks that affect cash and cash equivalents. An increase in interest rates by 25 basis points yields a gain of EUR 9 thousand while a decrease in interest rates by 25 basis points yields a loss of EUR 7 thousand. Given low interest rates, the sensitivities are determined using a hypothetical change by 25 basis points. The low interest rate sensitivities relative to cash funds largely stem from low-interest cash funds.

The long-term loans obtained to finance buildings are subject to fixed interest rates, as are the other interest-bearing liabilities.

Other price risks

LPKF is not exposed to other price risks.

Liquidity risks

The liquidity risk concerns the risk of not being able to satisfy existing or future payment obligations for lack of cash. This is centrally managed within the LPKF Group. The liquidity risk is minimized through continuous liquidity planning. In addition to existing cash and cash equivalents, credit lines are also available from various banks. The European companies optimized their liquidity peaks by way of cash pooling. All other companies carry out their ongoing cash management locally. LPKF is continually reviewing whether to expand cash pooling to other international companies. If large amounts of funds are required, reviews are performed to determine whether to utilize local financing or financing via LPKF AG. Long-term bank loans were used to finance the buildings in Garbsen, Suhl and Fürth.

Credit risks

The LPKF Group's operating business and certain of its financing activities expose it to default risks. Receivables from the operating business are monitored on an ongoing basis in decentralized fashion by the segments and subsidiaries. Default risks are accounted for by appropriate allowances.

The maximum default risk is reflected in the carrying amounts of the assets reported in the statement of financial position (including derivative financial instruments with positive fair values). Trade receivables are also securitized by EUR 632 thousand in payment commitments from banks (letters of credit). This leaves solely the credit risk of the chattel mortgagor. In addition, EUR 4,791 thousand in trade receivables is hedged through credit default insurance. The deductible for customers insured under a credit limit is 32%; for customers insured under a discretionary limit, it is 54%.

Capital management disclosures

The Group's capital management serves to secure the Company's existence as a going concern and pursue opportunities for growth with the aim of continuing to funnel profits to its shareholders and pay other interested parties that to which they are entitled. Maintaining an the best possible capital structure to reduce capital costs is another objective. To maintain or modify its capital structure, depending on the given situation the Group adjusts dividend payments to its shareholders; repays capital to its shareholders; issues new shares; or sells assets in order to discharge liabilities. The capital available comprises equity of EUR 54,330 thousand and borrowings of EUR 62,606 thousand.

26. DISCLOSURES PURSUANT TO SECTION 315A GERMAN COMMERCIAL CODE (HANDELSGESETZBUCH)

The requirements of Section 315 a German Commercial Code for the preparation of consolidated financial statements according to IFRS, as applicable in the EU, have been fulfilled. In addition to IFRS disclosure obligations, LPKF also publishes details and explanations required under the German Commercial Code.

27. DISCLOSURES ON MANAGEMENT BOARD REMUNERATION

The following individuals have been appointed as members of the Company's Management Board:

Dr. Ingo Bretthauer (CEO) (Chairman)	Sales, Marketing, Services, Strategy, Investor Relations, Legal Affairs
Dipl.-Ing. Bernd Lange (CTO)	Research, Development, Patents
Dipl.-Oec. Kai Bentz (CFO)	Finance, Controlling, Risk Management, Human Resources, Organization/IT
Dr.-Ing. Christian Bieniek (COO)	Production, Purchasing, Logistics, Quality Management, Administration

The remuneration of the Management Board is performance-based and consists of a fixed component and variable performance-based components. Details regarding the remuneration system and individual disclosures are presented in the remuneration report, which is part of the Group management report.

The current members of the Management Board were paid total remuneration of EUR 1,108 thousand (previous year: EUR 1,462 thousand) for their activities in the 2016 financial year. Of this amount, EUR 991 thousand (previous year: EUR 981 thousand) was fixed remuneration, EUR 103 thousand (previous year: EUR 98 thousand) were benefits and EUR 0 thousand (previous year: EUR 369 thousand) was variable remuneration or recognized as a provision. The remuneration of the Management Board's active members represents short-term benefits as defined in IAS 24.17 (a). The contributions of EUR 14 thousand (previous year: EUR 14 thousand) are post-employment benefits as defined in IAS 24.17 (b).

Expenses of EUR 0 thousand (previous year: EUR 0 thousand) relating to the setting-up of provisions for share-based payments as defined in IAS 24.17 (e) were recognized for members of the Management Board in the financial year just ended. The fair value at the allotment date was EUR 0 thousand.

Commitments to members of the Management Board upon termination

The Company has not made any pension commitments to the current members of its Management Board. Pension contracts were closed with the members of the Management Board, Kai Bentz and Bernd Lange; the Company makes contributions toward these contracts. Contributions of EUR 14 thousand (previous year: EUR 14 thousand) were paid in the financial year In connection with post-employment benefits as defined in IAS 24.17 (b). No provisions for pensions are required in this case.

Post-contractual non-competition agreements have been made with the members of the Management Board in the event their activities as such are terminated, irrespective of whether it is an ordinary or extraordinary termination. Under these agreements, the Company shall pay remuneration equivalent to 50% of the respective individual's most recent average base salary for the 12-month term of the post-contractual non-competition agreement unless the individual in question is retiring.

If a member of the Management Board dies while in office, the fixed monthly remuneration shall be paid to the heirs for a six-month period. No other provisions and commitments have been made with respect to the ordinary or extraordinary termination of a member of the Management Board.

Total remuneration of former members of the Management Board

Provisions were recognized for EUR 511 thousand (previous year: EUR 520 thousand) in pension commitments (pension plan, disability pension and widow's pension) toward former members of the Management Board and their survivors. A total of EUR 17 thousand (previous year: EUR 17 thousand) in pensions was paid to a former member of the Management Board in 2016.

28. DISCLOSURES ON SUPERVISORY BOARD REMUNERATION

Dr. Heino Büsching (Chairman)	Lawyer / tax consultant at CMS Hasche Sigle Partnerschaft von Rechtsanwälten und Steuerberatern mbH, Hamburg, Germany
Bernd Hackmann (Deputy Chairman)	Consultant to technology companies previously: Chief Executive Officer of LPKF Laser & Electronics AG Chairman of the Supervisory Board of Viscom AG, Hannover, Germany Member of the Supervisory Board of SLM Solutions Group AG, Lübeck, Germany
Prof. Dr.-Ing. Erich Barke	Retired professor of Leibniz University Hannover, Germany previously: President of Leibniz University Hannover, Germany Member of the Supervisory Board of the following companies: Esso Deutschland GmbH, Hamburg, Germany ExxonMobil Central Europe Holding GmbH, Hamburg, Germany hannoverimpuls GmbH, Hannover, Germany Solvay GmbH, Hannover, Germany

Each member of the Supervisory Board receives fixed basic remuneration for each full financial year of membership on the Supervisory Board that is specified by resolution of the Annual General Meeting and is payable after the end of the financial year. The Chairman of the Supervisory Board receives double and the Deputy Chairman receives one-and-a-half times the amount of the fixed basic remuneration. By resolution of the 2011 Annual General Meeting, the fixed basic remuneration of each member of the Supervisory Board was set at EUR 40 thousand effective 1 January 2011. The fixed remuneration from 1 January 2017 was set at EUR 32 thousand by resolution of the Annual General Meeting on 2 June 2016.

By resolution of the Annual General Meeting on 2 June 2016, there will no longer be any performance-based remuneration starting with the financial year beginning on 1 January 2016.

According to the consolidated financial statements certified on 22 March 2017 by Pricewaterhouse-Coopers GmbH Wirtschaftsprüfungsgesellschaft, Hannover, the (basic) consolidated earnings per share amount to EUR – 0.40 per share. This results in variable remuneration of EUR 0 thousand for the 2016 financial year. Variable remuneration of EUR 6 thousand was paid to the Supervisory Board for the 2015 financial year.

The remuneration of the Supervisory Board's active members solely concerns short-term benefits as defined in IAS 24.17 (a). Further disclosures regarding the remuneration of the Supervisory Board, particularly individual disclosures, are set forth in the remuneration report, which is part of the Group management report.

29. DISCLOSURE OF REPORTED SHAREHOLDINGS IN THE COMPANY

The following entities and persons have notified us that their shareholdings exceeded the 3% threshold in 2016:

Mr. Jörg Bantleon, Germany, notified us in accordance with Section 21 (1) WpHG that his share of the voting rights in LPKF Laser & Electronics AG, Garbsen, Germany, on 16 December 2016 had exceeded the threshold of 15% and on that date was 15.02% (representing 3,345,808 voting rights). Of these, 5.02% (1,118,808 voting rights) are attributable to Bantleon Bank AG, Zug, in accordance with Section 22 WpHG.

Bantleon Bank AG, Zug, Switzerland, notified us in accordance with Section 21 (1) WpHG that its share of the voting rights in LPKF Laser & Electronics Aktiengesellschaft, Garbsen, Germany, on 27 October 2016 had exceeded the threshold of 3% and on that date was 3.24% (representing 721,528 voting rights). Of these, 3.24% (721,528 voting rights) are directly attributable to it in accordance with Section 21 WpHG.

Mr. Jörg Bantleon, Germany, notified us in accordance with Section 21 (1) WpHG that his share of the voting rights in LPKF Laser & Electronics AG, Garbsen, Germany, on 16 September 2016 had exceeded the threshold of 10% and on that date was 10.00% (representing 2,227,000 voting rights). Of these, 10.00% (2,227,000 voting rights) are directly attributable to it in accordance with Section 21 WpHG.

All other notifications of voting rights in accordance with the German Securities Trading Act concerned cases in which the interest in the voting shares had fallen below the 3% threshold. They have been published at http://www.lpkf.com/investor-relations/share/notification-of-voting-rights.htm

30. AUDITOR FEES INVOICED IN THE FINANCIAL YEAR JUST ENDED

The Company is obligated under the German Commercial Code (Section 314 (1) no. 9) to disclose the Group auditor's fees for auditing the annual financial statements invoiced during the financial year:

EUR thsd.	2016	2015
Audits of financial statements	125	110
Other services	0	4
	125	**114**

31. EVENTS AFTER THE REPORTING PERIOD
There were no significant events after the end of financial year 2016.

Garbsen, Germany, 21 March 2017

LPKF Laser & Electronics Aktiengesellschaft

The Management Board

Dr. Ingo Bretthauer	Bernd Lange	Kai Bentz	Dr.-Ing. Christian Bieniek

AUDITORS' REPORT

We have audited the consolidated financial statements prepared by LPKF Laser & Electronics Aktiengesellschaft, Garbsen, Germany, comprising the income statement, statement of comprehensive income, statement of financial position, statement of cash flows, statement of changes in equity, and the notes to the consolidated financial statements, together with the Group management report, which is combined with the Company's management report, for the financial year from 1 January to 31 December 2016. The preparation of the consolidated financial statements and the combined management report in accordance with the IFRSs, as adopted by the EU, and the additional requirements of German commercial law pursuant to Section 315a (1) HGB ("Handelsgesetzbuch": German Commercial Code and supplementary provisions of the articles of incorporation) is the responsibility of the Company's Management Board. Our responsibility is to express an opinion on the consolidated financial statements and the combined management report based on our audit.

We conducted our audit of the consolidated financial statements in accordance with Section 317 HGB and German generally accepted standards for the audit of financial statements promulgated by the Institut der Wirtschaftsprüfer (Institute of Public Auditors in Germany) (IDW). Those standards require that we plan and perform the audit such that misstatements materially affecting the presentation of the net assets, financial position and results of operations in the consolidated financial statements in accordance with the applicable financial reporting framework and in the combined management report are detected with reasonable assurance. Knowledge of the business activities and the economic and legal environment of the Group and expectations as to possible misstatements are taken into account in the determination of audit procedures. The effectiveness of the accounting-related internal control system and the evidence supporting the disclosures in the consolidated financial statements and in the combined management report are examined primarily on a test basis within the framework of the audit. The audit includes assessing the annual financial statements of the companies included in the consolidated financial statements, the determination of the companies to be included in the consolidated financial statements, the accounting and consolidation principles used and significant estimates made by the Company's Management Board as well as evaluating the overall presentation of the consolidated financial statements and the combined management report. We believe that our audit provides a reasonable basis for our opinion.

Our audit has not led to any reservations.

In our opinion, based on the findings of our audit, the consolidated financial statements comply with the IFRSs as adopted by the EU, and the additional requirements of German commercial law pursuant to Section 315a (1) HGB, and supplementary provisions of the articles of incorporation, and give a true and fair view of the net assets, financial position and results of operations of the Group in accordance with these provisions. The combined management report is consistent with the consolidated financial statements, complies with legal requirements, as a whole provides a suitable view of the Group's position and suitably presents the opportunities and risks of future development.

Hannover, Germany, 21 March 2017

PricewaterhouseCoopers GmbH
Wirtschaftsprüfungsgesellschaft

Jens Wedekind Wirtschaftsprüfer [German Public Auditor]	Prof. Dr. Mathias Schellhorn Wirtschaftsprüfer [German Public Auditor]

INCOME STATEMENT
SINGLE-ENTITY FINANCIAL STATEMENTS OF LPKF LASER & ELECTRONICS AG FROM 1 JANUARY TO 31 DECEMBER 2016

EUR thsd.	2016	2015
Revenue	42,102	61,577
Changes in inventories of finished goods and work in progress	213	– 1,959
Other own work capitalized	0	92
Other operating income	4,795	7,335
	47,110	**67,045**
Cost of materials		
Cost of raw materials, consumables and supplies, and of purchased merchandise	19,610	25,328
Staff costs		
Wages and salaries	14,334	20,438
Social security costs and pension costs of which for pensions: EUR 140 thousand; Previous year: EUR 140 thousand)	2,487	3,663
Depreciation, amortization and write-downs		
Amortization and write-downs of intangible fixed assets and depreciation and write-downs of tangible fixed assets	3,082	3,840
Write-downs of currents assets to the extent that they exceed the usual write-downs	3,154	–
Other operating expenses	13,768	23,782
	56,435	**77,051**
Income from equity investments (of which from affiliated companies: EUR 5,959 thousand (previous year: EUR 1,517 thousand)	5,959	1,517
Other interest and similar income (of which from affiliated companies: EUR 248 thousand; Previous year: EUR 35 thousand)	248	50
Expenses from loss absorption	1,685	2,109
Interest and similar expenses (of which to affiliated companies: EUR 0 thousand (previous year: EUR 8 thousand)	623	474
Taxes on income	82	– 3,883
Earnings after taxes	**– 5,508**	**– 7,139**
Other taxes	26	49
Net loss for the year	**– 5,534**	**– 7,188**
Retained earnings brought forward from the previous year	4,333	11,521
Net retained losses/profits	**– 1,201**	**4,333**

BALANCE SHEET AS OF 31 DECEMBER 2016
SINGLE-ENTITY FINANCIAL STATEMENTS OF LPKF LASER & ELECTRONICS AG

Assets in EUR thsd.	31 Dec. 2016	31 Dec. 2015
Fixed assets		
Intangible assets		
Software	1,210	793
Rights of use	33	37
	1,243	**830**
Property, plant and equipment		
Land, similar rights and buildings	18,232	18,959
Plant and machinery	2,481	2,537
Other equipment, operating and office equipment	3,927	4,537
	24,640	**26,033**
Financial assets		
Shares in affiliated companies	15,804	15,804
	15,804	**15,804**
	41,687	**42,667**
Current assets		
Inventories		
Raw materials, consumables and supplies	7,924	10,047
Work in progress	926	1,288
Finished products and goods	3,522	3,957
Advances paid	13	595
	12,385	**15,887**
Receivables and other assets		
Trade receivables (of which due within more than one year: EUR 214 thousand; Previous year: EUR 258 thousand)	6,469	3,923
Receivables from affiliated companies (of which due within more than one year: EUR 9,000 thousand (previous year: EUR 0 thousand)	15,165	17,151
Other assets (of which due within more than one year: EUR 0 thousand; Previous year: EUR 46 thousand)	677	1,437
	22,311	**22,511**
	34,696	**38,398**
Cash-in-hand, bank balances and checks	1,535	258
	36,231	**38,656**
Deferred income	**275**	**419**
Deferred taxes	**3,857**	**3,869**
Excess of plan assets over pension liability	**240**	**232**
	82,290	**85,843**

BALANCE SHEET AS OF 31 DECEMBER 2016
SINGLE-ENTITY FINANCIAL STATEMENTS OF LPKF LASER & ELECTRONICS AG

Equity and liabilities in EUR thsd.	31 Dec. 2016	31 Dec. 2015
Equity		
Subscribed capital	22,270	22,270
Capital reserves	2,186	2,186
Revenue reserves		
Statutory reserve	41	41
Other retained earnings	11,200	11,200
	11,241	**11,241**
Net retained profits/losses	– 1,201	4,333
	34,496	**40,030**
Provisions		
Provisions for pensions	0	0
Other provisions	2,489	3,368
	2,489	**3,368**
Liabilities		
Liabilities to banks (of which due: within one year: EUR 19,204 thousand (previous year: EUR 13,895 thousand) more than 1 year: EUR 14,560 thousand (previous year: EUR 1,609 thousand)	33,764	29,656
Payments received on account of orders	221	606
Trade payables	1,304	889
Liabilities to affiliated companies	9,221	10,579
Other liabilities (of which from taxes: EUR 238 thousand; Previous year: EUR 240 thousand) (of which from social security: EUR 7 thousand (previous year: EUR 0 thousand)	748	712
	45,258	**42,442**
Deferred taxes	**47**	**3**
	82,290	**85,843**

GLOSSARY OF TECHNICAL TERMS

EBIT
Earnings Before Interest and Taxes.

EBIT MARGIN
Operating profit as a percentage of revenue.

FTE
(Full-time equivalent) A labor comparison metric, FTE expresses the workforce in terms of the compensable workload handled by a full-time employee (i. e. working a standard, full-time schedule).

HDI CIRCUIT BOARD
(High-density interconnect circuit board) A HDI circuit board is a highly compact PCB, where widths and spacing between conductive paths and contact pads are reduced to structural sizes of <100 μm.

IC (INTEGRATED CIRCUIT)
An IC is a set of electronic circuitry attached to a thin piece of semiconductor material typically only a few millimeters in size. The piece of semiconductor material is often referred to as a “chip”.

ICP (IC PACKAGING)
The encapsulation of a semiconductor chip (see entry for IC) including its contact pins is commonly referred to as a “package”. Apart from protecting the integrated circuit (IC) on the chip itself, the package is used to attach the chip to a circuit board and connect it with the various components on the board. A great many types of IC packages are in common use.

IC SUBSTRATE
An IC substrate is a small, multi-layered special PCB constructed from a number of materials depending on the application. The IC substrate connects the variously-sized contacts on chips and circuit boards in an extremely compact form factor. Alongside organic laminates, ceramics or other specialized starting materials are also used.

LDS METHOD
(Laser direct structuring) A laser-based manufacturing process for three-dimensional circuit carriers, otherwise known as molded interconnect devices (MIDs), made of plastic, which also handle mechanical functions.

LIDE
(laser-induced deep etching) High-precision method for machining glass. LIDE enables the creation of ultra high-precision holes and structures in glass at very high speeds, and also includes the TGV method.

LTP METHOD
(Laser transfer printing) A method for digitally printing functional pastes as an alternative to screen printing.

RAPID PROTOTYPING
A method for the chemical-free manufacture of prototype printed circuit boards in in-house laboratories.

STENCILLASERS
Laser systems for cutting fine, highly precise openings in a stainless steel stencil. Stencils are used for the precision printing of solder paste onto printed circuit boards – a vital technique for today’s closely packed PCBs.

THIN FILM SOLAR PANELS
Thin film solar panels are manufactured by coating a sheet of glass or a film with extremely thin layers. A laser divides each layer into strips to enable the series connection of cells in the finished module.

TGV METHOD
(Through-glass-via) A laser method for creating ultrafine holes in glass (see LIDE).

FINANCIAL CALENDAR

22 March 2017	Publication of the 2016 annual financial report
11 May 2017	Publication of the three-month report
01 June 2017	Annual General Meeting
15 August 2017	Publication of the half-yearly financial report
14 November 2017	Publication of the nine-month report

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