

Consolidated Financial Statements **2002**



At a Glance

KBA Group in Figures					
	2002*	2001*	2000	1999	1998
Values in million €					
Order intake	1,084.5	1,197.9	1,375.7	1,043.4	975.7
Order level as of 31. 12.	832.9	1,102.2	1,252.2	963.9	858.2
Sales	1,353.8	1,304.0	1,087.4	949.8	821.5
Earnings before interest and taxes (EBIT)	46.3	58.8	51.3	45.4	30.9
Profit from ordinary activities	43.2	62.3	59.0	49.8	39.6
Net profit	28.1	40.0	52.6	51.1	40.4
Balance-sheet total	1,240.6	1,334.1	751.2	685.1	618.0
Intangible assets, property, plant and equipment	283.0	257.5	159.8	137.4	133.6
Equity (without dividend payments)	467.6	437.1	322.4	280.1	236.3
Investment in intangible assets, property, plant and equipment	51.7	81.4	57.1	38.6	35.2
Depreciation on intangible assets, property, plant and equipment	45.0	38.5	33.7	31.7	29.7
Personnel: annual average	7,539	7,424	6,729	6,492	6,324
Cash flows from operating activities	6.3	- 39.8	62.7	63.7	55.9
Dividend and bonus paid per ordinary/scrip share in €	0.50	0.67+0.33	0.62+0.13	0.61	0.61
Dividend and bonus paid per preferred/scrip share in €	-	-	0.67+0.13	0.66	0.66

*under International Financial Reporting Standards



Contents

2	Foreword
4	Supervisory Board's Report
6	KBA Shares
8-44	Management Report
8	Market Environment
10	Group Performance
12	Assets, Finances and Earnings
16	Business Operations
20	Key Regions
22	Risk Management
25	Corporate Governance
26	Human Resources and Welfare
30	Research and Development
34	Production, Organisation, Information Technology
38	Investment and Ecology
40	Resource Management and Logistics
42	Outlook for 2003

45-80	Financial Statements for the KBA Group
46	Balance Sheet to 31 December 2002
47	Income Statement for 2002
48	Statement of Changes in Shareholders' Equity
49	Cash Flow Statement
50-80	Notes to the Financial Statements
77	Supervisory Board
77	Management Board
78	Proposal for the Utilisation of Net Profit
79	Auditors' Report
80	Key Financial Dates / Contacts

Koenig & Bauer Group

We manufacture and sell web offset and flexo presses for printing newspapers, commercial web offset presses for printing brochures, books and telephone directories, publication rotogravure presses for printing catalogues and magazines, conventional and digital sheetfed offset presses for printing books, stamps, magazines and packaging, security presses for printing banknotes, and peripheral systems for automating paper logistics and enhancing counterfeit protection.

Dear Shareholders and Business Friends,



This annual report is the first one we have issued since we adopted international financial reporting standards (IFRS, formerly IAS). The 2001 figures quoted in the report have been converted accordingly for ease of comparison.

We also merged our security and web press activities into one division, web presses and special presses, in order to align product disclosure with internal accounting procedures.

Group turnover in 2002 totalled €1,353.8m (2001: €1,304m), around €100m above our projection for the year and the highest figure in our 185-year history. Group earnings stood at €43.2m.

However, the downturn in the global economy over the past two years made its mark in the form of rapidly declining investment in the print media, most noticeably among publishers of newspapers and commercials. Although turnover by our web and special press division, cushioned by higher sales of security presses and the shipment of big newspaper press lines, was just 2.4% down at €734.8m, the volume of new orders shrank by 25.4% to €508.5m. As production capacity outstripped market demand, price competition in the web sector intensified and this also affected the bottom line.

Sheetfed offset sales easily outstripped our web press business. Despite the slide in demand for presses in general, our sheetfed offset division in Radebeul near Dresden posted a double-digit increase in sales for the ninth year in succession. The annual total, at €619m, was 12.2% up on the previous year's figure, while the volume of incoming orders swelled by 11.6% to €576m.

The performance of Koenig & Bauer shares reflected the overall market trend, which was heavily influenced by economic, political and psychological factors. On 30 December our shares were valued at €13.80, a good 38% below their opening price at the beginning of the year and average for the first-tier and mid-caps indices. A succession of negative announcements by the media industry, and the print sector's heavy dependence on export markets, also acted as a brake on the share price.

Our employee share scheme introduced in 2002 was taken up by some 70% of the workforce. Factoring in bonus issues and dividends, KBA shares are now worth 103.6% compared to their initial listing price in the small-caps index in April 1999, and have thus outperformed other shares in the industry. Nonetheless we still consider them to be undervalued relative to company assets, and a large number of analysts are of the same opinion.

With poor growth rates predicted for the current year, especially in Germany and the EU, and with the war in Iraq casting its shadow on the global economy, prospects for a fundamental recovery in the graphic arts industry are bleak. We have therefore extended short-time work, which was initially limited until the end of February, to the end of September, and continue to implement other cost-cutting initiatives.

If the order intake for sheetfed offset presses remains at its present high level and a number of big web press contracts can be booked within the next few weeks, we believe a single-figure drop in total sales for 2003 to be realistic. Even though a floundering economy and the risks associated with the current political crisis make it difficult for us, at present, to predict Group results for 2003 with any degree of accuracy, we believe the measures we have initiated will enable us to stay in the black.

In a market environment such as this our performance in 2002 compared favourably with that of many other industry players. At our annual shareholders' meeting on 26 June in Würzburg we shall recommend transferring €9m of net retained profits to other revenue reserves, in accordance with our company charter, and propose a 50-cent dividend. The remaining €0.9m will be reinvested.

On behalf of the management board I would like to thank all our staff for their loyal and zealous pursuit of Group targets.

I would also like to thank you, our shareholders and customers, for the confidence and trust you have placed in us and for the support you have shown in a troubled economic climate.

Würzburg, 9 April 2003
Koenig & Bauer AG
Management Board



Reinhart Siewert, president

Dear Shareholders,



In the 2002 fiscal year the supervisory board and its committees closely and continuously monitored the activities of the Koenig & Bauer management board, duly fulfilling the obligations and functions allotted to us by law and the statutes. Maintaining and co-ordinating our monitoring and advisory functions between our plenary sessions is part of my job as chairman, with the support of the committees. Regular quarterly meetings were held at which KBA management gave the supervisory board a thorough briefing on the economic situation at Koenig & Bauer and within the Group, and also on fundamental matters of corporate management, policy, strategy and planning. Discussions centred on investment, rationalisation, the product range, risk management, market developments and personnel policy. In addition Reinhard Siewert and I regularly discussed details of key executive decisions and specific business matters.

A widespread loss of confidence in the markets and an unwillingness to commit funds to new plant negatively influenced the economic climate and outlook for the entire year. The effects on business activities were explained in detail to the supervisory board and published in the interim reports.

Board members devoted particular attention to the new Corporate Governance Code introduced last year for companies based in Germany, and adopted the Code guidelines in the board's rules of procedure with effect from 1 January 2003.

At its meeting on 26 November 2002 the supervisory board followed the recommendations of the personnel committee and appointed Albrecht Bolza-Schünemann to succeed Reinhart Siewert as president of Koenig & Bauer, and Claus Bolza-Schünemann to succeed Albrecht as deputy president. Reinhart will retire from the management board after the AGM on 26 June 2003 and, pending shareholders' approval, will become a member of the supervisory board. We would like to express our appreciation of the signal contribution he has made towards shaping and directing the company's fortunes during his long years of service on the management board and, more specifically, since becoming president in 1995.

The financial statements, management reports and method of accounting for the Parent and the Group to 31 December 2002 were examined by Bayerische Treuhandgesellschaft AG – the auditors appointed at the AGM – and awarded the auditor's certificate unreservedly.

In my capacity as chairman of the supervisory board I attended the audit meeting between management and the auditor. The financial statements, management reports and auditors' reports for Koenig & Bauer and for the KBA Group were subsequently discussed in detail by the supervisory board's audit committee, with the auditors furnishing the results of their audit and detailing the main points. All the relevant statements and reports were distributed to the members of the supervisory board well in advance of the audit meeting. The audit committee's findings were then submitted to and approved by the supervisory board.

After conducting its own examination the supervisory board raised no objections to the financial statements or management's proposal for the utilisation of net profit, and at its meeting on 9 April 2003 officially approved the year-end financial statements. The management reports for the

Parent and the Group were also examined and approved, as was the proposal for the utilisation of net profit.

The supervisory board wishes to thank all the KBA directors and staff for their unflagging commitment to the success of the company and the Group.

Würzburg, 9 April 2003

Koenig & Bauer AG

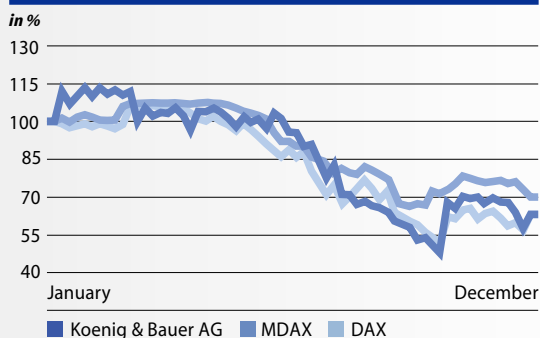
Supervisory Board



Peter Reimpell, chairman

KBA SHARES

Performance in 2002



Key Data on Koenig & Bauer Ordinary Shares

	2002	2001
Earnings per share	€ 1.75	€ 2.49
Price-earnings ratio	7.9	9.4
Highest price	€ 27.30	€ 29.00
Lowest price	€ 11.00	€ 15.80
Closing price	€ 13.80	€ 23.30
Market capitalisation in m	€ 220.8	€ 372.8
Cash flow per share	€ 0.39	-€ 2.49
Dividend + bonus	€ 0.50	€ 1.00
Free float	58.4 %	58.4 %



In the Maelstrom of Market Malaise

2002 was an *annus horribilis* for the stock markets, with no sign of the hoped-for recovery. A languishing economy, with business confidence shaken by serial bankruptcies and downward adjustments in performance projections, went hand in hand with mounting uncertainty on the political front. Accounting scandals and market rigging destroyed the faith of many investors in the value of shares.

In the course of the year the 30 first-tier companies listed on the German stock exchange, Dax, lost 44% of their value. The mid-caps index lost around 30%. In view of the continuing economic and political instability, prognoses for 2003 issued by market analysts in mid-February offered little prospect of a significant and stable recovery of key indices until the second half of the year.

Koenig & Bauer shares suffered the same fate as the rest of the stock market. At the beginning of the year, boosted by the conversion of preferred shares to ordinary shares in mid-December 2001, they climbed to €27.30. But from March onwards, with Group prospects affected by the market slowdown, they experienced a steady decline along with the other shares listed in Germany. By 30 December 2002 their value, with dividend, had sunk to €13.80, 38.4% down on their opening price at the beginning of the year and in line with the general direction of the first-tier and mid-caps indices.

Prospects Good for Long-Term Gain in Value

Despite the disappointing performance of KBA shares in 2002, which was exacerbated by the pervading gloom in the e-media and print industry, over the past four years our ordinary shares have outperformed both the first-tier and the mid-caps indices. Since being listed in the mid-caps index on 26 April 1999 (=100%), and taking into account the issue of bonus shares and the payment of dividends, their price has risen to 103.6%, which is above the industry average.

Nonetheless, they are selling at a big discount on our net asset value. With earnings per share of €1.75 (2001: €2.49) under IAS 33, at the AGM we shall propose a dividend of 50 cents per share (2001: 67 cents + 33 cents bonus per share) – a dividend yield of 3.6% on the year-end quotation.

Employee Participation

In 2002, for the first time, Koenig & Bauer employees were offered the chance to buy KBA shares at a preferential price of €15.84 per share, 12 or 18 shares per person. Almost 70 per cent of our workforce signed up for the first issue, an indication of how closely they identify with the company. The scheme will be repeated to promote staff participation.

Towards Greater Transparency

Deutsche Börse, the German stock exchange, responded to the failure of the Neuer Markt and to the business (mal)practices of certain corporations by issuing standards of transparency for all the companies listed in its indices. Effective from 24 March this year these comprise the prime standard, which carries an obligation to fulfil rigorous international transparency regulations and to publish accounts in English, and the domestic standard, which, as the name implies, is nationally oriented and carries no such obligation. In December 2002 Koenig & Bauer submitted a request for admission to the prime standard and has since been accepted. This has no effect on our listing: KBA will remain in the mid-caps index, which has been whittled down from 70 to 50 companies.

Although we stepped up our investor relations activities, analysts' assessments of Group performance and prospects during the year remained heavily coloured by the softening economy and ranged from "outperformer" to "neutral".

Since going public we have worked hard to address a mounting demand in capital markets for greater transparency in corporate communications. With the adoption of international financial reporting standards (IFRS, formerly IAS), the issue of quarterly reports and the publication of updates on the KBA web site we already comply with most of the transparency criteria specified in the German Corporate Governance Code.

MARKET ENVIRONMENT 2002



Ad Slump Impacts on Media

In many countries 2002 was a difficult year for members of the media in general and of the graphic arts industry in particular. While the economic performance of individual regions and market sectors varied considerably, on the whole printers' advertising volumes and income were disappointingly low, especially in the EU and North America. Press manufacturers' production capacity and pricing capabilities suffered accordingly.

At the beginning of the business year the leading economic research institutes in Germany predicted 1%-plus growth in GDP (gross domestic product). In

the course of the year, however, it became increasingly evident that Germany would once again trail the other members of the euro zone with a growth rate of just 0.2%. Projections for the present year range from 0.6% to a maximum of 1%. This sluggishness, and the slump in advertising income it has brought, are adversely affecting both investment and employment in the media. According to the Printing and Media Industries Federation, the German print sector experienced a drop in employment of almost 6%, while statistics issued by the German Machinery and Plant Manufacturers' Association reveal that new investment fell by 30%.

The new products and processes demonstrated on our stand at the Ipex international trade fair in Birmingham, UK, were a magnet for trade visitors

Patchy Performance in Foreign Markets

For the German press engineering industry, which exports around 80% of its products, developments in the global economy are of central significance. The situation in certain export markets was very much better than in the domestic market. In its annual review the International Monetary Fund (IMF) revealed that global GDP had risen by 2.8%. The euro zone, however, was near the bottom of the ladder with growth of just 0.9%.

The review also showed that GDP in the USA, the world's biggest single market for printing presses, rose by 2.2% (2001: 0.3%). This was accompanied by a slight lift in newspaper advertising, and a number of American newspaper publishers invested in new technology. KBA also benefited from an unusually high level of investment by packaging printers in sheetfed presses, though demand for commercial presses remained weak.

Once again, with the exception of Japan, which continued to battle with deflationary pressures, the Asia-Pacific economies experienced the strongest growth. As in previous years, the highest growth rate – more than 7% according to official statistics – was posted by China. KBA profited from this growth with an exceptionally high volume of sales, primarily of sheetfed presses, to Chinese printers.

Upswing Delayed

The direct link between the state of the economy on the one hand and, on the other, advertising revenue and the volume of print produced means that future investment in the print and e-media industry depends to a large extent on a sustained economic recovery. Expectations were dashed in 2002 and there was little indication that circumstances would improve in the new year. The loss of impetus in the US economy, which traditionally plays a key role as an engine of growth in the global economy, is also proving to be surprisingly obstinate. Hopes of a significant upturn in international markets and central stock exchanges in the short term faded in the first months of the year as the threat of war in Iraq increased together with the uncertainties caused by a higher oil price. We therefore do not expect demand to improve before 2004.

GROUP PERFORMANCE



Business Mirrors Demand

The economic slowdown in developed industrial nations severely affected demand for web and special presses. For example, there was a big decline both in the number of large newspaper projects put up for tender and in demand for commercial web presses. Sales in new markets of smaller newspaper press lines like our single-width Comet and of commercial presses

like our 16-page Compacta 215 were unable to compensate.

However, sales of sheetfed presses, especially medium- and large-format versions, remained buoyant. Security presses and related systems were also largely unaffected by economic conditions.

Modest Order Intake

Altogether the KBA Group booked orders to the value of €1,084.5m. The shortfall of 9.5% compared to the previous year (€1,197.9m) was smaller than that posted by our competitors. Although sales were slow in the first three months, most notably of web presses which are one of our main products, the Ipex international trade fair in Birmingham, UK, which took place in April, helped to push up sales of sheetfed presses in the second quarter and also brought two big orders from Switzerland for the first two triple-width newspaper presses.

In the second half of the year further orders for newspaper and commercial web presses – among them a big installation for the USA and a directory press for Japan – plus a high volume of incoming orders for sheetfed presses enabled us to withstand the slide in the market. But excess capacity among printing companies provoked even fiercer price competition in both sectors. Sales of newspaper and commercial web presses, in particular, were badly hit, and press manufacturers' margins received a buffeting in consequence. The situation was exacerbated by the fact that increases in the cost of materials and labour could not be passed on to the consumer.

Higher Turnover

Group turnover grew by 3.8% to €1,353.8m (2001: €1,304m) and was thus more than €100m above the projected figures published in spring 2002. Profits from the Swiss security press sales organisation we acquired in summer 2001 were included in full for the first time and largely outweighed the slump in demand for web presses. The rise in turnover compared to 2001 was generated by a double-digit jump in sales of sheetfed presses, which contributed around 46% of Group turnover. Sheetfed presses are now the biggest earner within our extensive product range.

Group Sales
in million €

2002	255.8	Domestic	2001	255.8
	1098.0	Foreign		1048.2
	81.1	Export level in %		80.4
	1353.8	Total		1304.0

Group Orders/Backlog
in million €

2002	1084.5	Order intake	2001	1197.9
	832.9	Order backlog		1102.2

Shrinking Backlog

The increase in turnover, combined with a drop in new bookings of almost 10%, caused the volume of orders on hand to shrink 24.4% to €832.9m by the end of the year (2001: €1,102.2m). The four-month backlog in sheetfed production is more or less normal, but the level of plant utilisation for newspaper and commercial web presses is well below the optimum 80%, partly because a number of bigger projects will not approach completion until 2005 and so have no impact on employment at present. In view of the long lead times for web presses we therefore initiated measures in the second half of the year to downsize capacity in line with the reduction in plant utilisation.

ASSETS, FINANCES AND EARNINGS



"An ongoing dialogue with investors and analysts on Koenig & Bauer's strategic alignment and future objectives is the focus of our communications in financial markets."

Reinhard Siewert, president

Market Climate Weighs on Earnings

This annual report is the first to be published following our adoption of international financial reporting standards (IFRS). The income statement was converted to the cost of sales format, which means that expenses and earnings are now disclosed according to their function.

Despite the downturn in the market the KBA Group booked the highest turnover in its history – a 3.8% rise to €1,353.8m (2001: €1,304m). This was due partly to the completion of big newspaper projects carried over from 1999 and 2000 and partly to rapidly expanding sales of sheetfed offset presses.

The higher volume of turnover lifted gross margins after manufacturing costs to 22.3% or €301.9m, compared to 21.6% and €281.1m in 2001.

However, higher costs for research and development, and for the handling and acquisition of smaller contracts in more remote regions, meant that this higher volume was not reflected in earnings before interest and taxes (ebit), which were carried at €46.3m (2001: €58.3m). Similarly, a drop in plant utilisation at our web press production sites in the wake of softening demand meant that additional labour costs arising from industry-wide wage agreements could not be passed on to consumers.

3.2% Rate of Return

The financial result was well below the previous year's figure. This was caused by a decrease in customer down payments and an increase in liabilities to -€3.4m (2001: €3.6m), attributable in part to the integration of Karat Digital Press. Profits from ordinary activities were 30.7% down at €43.2m (2001: €62.3m). The rate of return for the Group was thus 3.2% (2001: 4.8%), a respectable figure in the present market environment.

With market prospects subdued, any medium-term contributions to profits will primarily be generated by implementing additional cost-cutting measures. Steps initiated in 2002 to downsize capacity and cost structures will therefore be intensified in the current year.

Group Assets and Capital Structure*Assets in %*

3.2	Deferred tax assets	4.1
24.0	Non-current assets	20.4
68.2	Current assets ./. funds	67.9
4.6	Funds	7.6
2002		2001

Equity and Liabilities in %

3.9	Deferred tax liabilities	4.3
21.5	Provisions	19.9
37.7	Equity	32.8
36.9	Liabilities and dividends	43.0
2002		2001

Integration of Karat Digital Press GmbH

In the first half-year Karat Digital Press GmbH, a former joint-venture enterprise with our pre-press partner Scitex Corp., was merged with Koenig & Bauer AG, giving rise to additional expenses largely related to high development costs for the 74 Karat digital offset press. Since players in this market are reluctant, at present, to invest in new machinery, these costs could not be offset by sales and, along with proportionate write-offs of product development costs, had a detrimental effect on income. Net profit for the year, allowing for deferred taxes, fell to €28.1m (2001: €40m). Earnings per share were €1.75, compared to €2.49 the year before.

Balance Sheet Still Strong

Despite this decline in profitability the Group balance sheet remains strong. The balance-sheet total at 31 December was €1,240.6m, 7% down on the previous year (€1,334.1m), largely owing to a reduction in short-term balance-sheet items.

The much higher balance-sheet total compared to the previous year (€931.9m under German business law) was occasioned by differences in accounting policies under IFRS and the fact that payments received on account can no longer be deducted from inventories, but must be listed as liabilities.

The continuing upgrade of production equipment, the disclosure of new products worth €4m on the asset sheet and the integration of Karat Digital Press enhanced the value of non-current assets by €26.3m to €298.4m, with an equity capital backing of around 157%.

Current assets shrank by €105.2m to €902.7m (2001: €1,007.9m). Streamlining inventory management reduced the volume of stored components from €498.5m to €388.6m. However, the benefits were offset to some extent by an increase in trade receivables, which in 2002 jumped €39.3m to €384.4m. Alongside a higher turnover this reflected a growing demand for customer financing and the expansion of our sheetfed offset business.

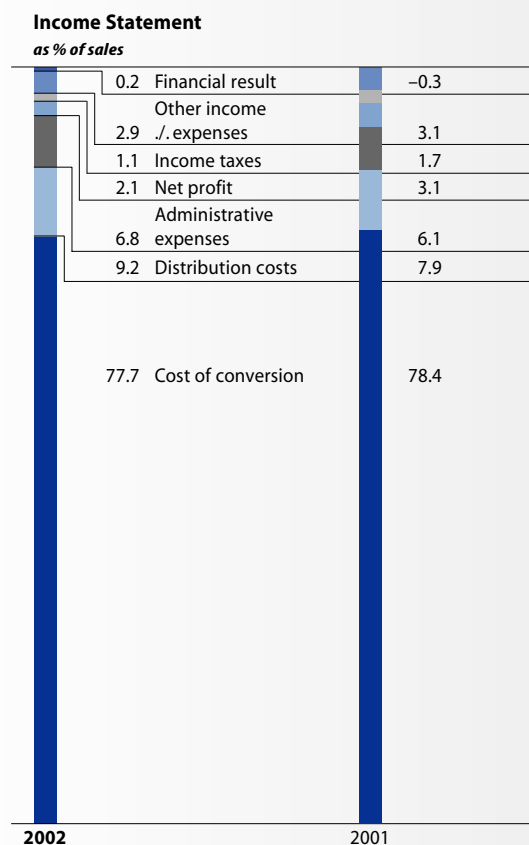
Equity and liabilities were also affected by an increase in equity capital, which after allowing for a total dividend

payment in 2003 of €8m stood at €467.6m (2001: €437.1m). Measured against the balance-sheet sum, capital ratio improved from 32.8% to 37.7%. Further essential changes related to a €107.6m decrease in liabilities to €449.9m. These included a rise in loans to €132.9m (2001: €109.5m), against a €103.8m plunge in customer down payments. At €266.4m, provisions, including pension obligations, were roughly on a par with the figure for 2001 (€265m). The increase in pension provisions compared to the previous year under German business law arose from the different method of measurement used: international accounting regulations, for example, stipulate that future salary and career trends must be included in the calculations.

Financing from Own Resources Positive Again

A €39.8m outflow from day-to-day business in 2001 was followed last year by a €6.3m inflow. This was largely attributable to a reduction of €76.7m in working capital, bringing it down to €523.6m.

Ongoing investment resulted in a negative free cash flow of €41.1m in 2002 (2001: -€132.1m). On balance, financing investments and day-to-day business led to a €48.7m drop in funds (2001: -€82.1m). Financing activities included the repayment of debts to the sum of €7.5m, as opposed to €50m borrowings the previous year.



BUSINESS OPERATIONS



"Our printing technology and systems competence enhance our customers' competitive profile."

Andreas Mössner, executive vice president, sheetfed offset sales and marketing

Walter Schumacher, executive vice president, web press sales, marketing and service

Strong Sheetfed Sales Offset Weak Web Sales

In the 2002 business year the security press division was incorporated in the web press division to harmonise internal and external reporting procedures as per IAS 14.31. The new division, web presses and special presses, embraces newspaper, commercial, rotogravure and directory web presses, plus banknote and security presses.

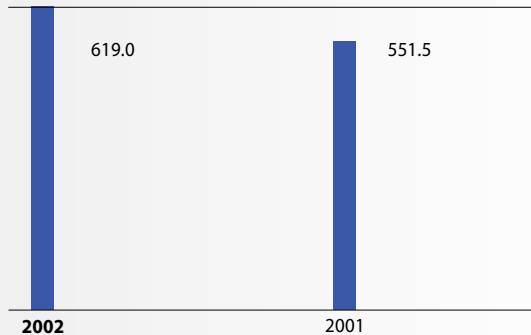
There was a sharp contrast in the performance of our two main divisions in 2002. While our sheetfed operation achieved double-digit growth in sales and order intake, a widespread reluctance among newspaper and commercial printers to invest in new kit caused a big drop in web press orders and turnover.

Double-Digit Growth in Sheetfed Offset Sales

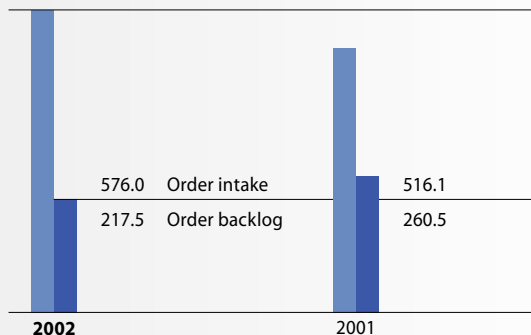
Sheetfed presses generated turnover of €619m (2001: €551.5m), a jump of 12.2%. Our sheetfed offset division in Radebeul has thus posted two-figure growth rates for nine years running. The volume of new orders climbed 11.6% to €576m (2001: €516.1m). A big jump in shipments reduced the backlog of orders at year's end to €217.5m, a good 16.5% below the previous year's figure of €260.5m, but nonetheless sufficient to maintain production for the first four months of the current year. The volume of new orders remained satisfyingly high.

The main reason for this continued growth in a challenging environment is our strong position in the markets for packaging and books (which are less cyclical), large-format presses, more complex and sophisticated press configurations, and for new processes, eg ecological printing, printing on corrugated and printing with hybrid inks. The digital offset sector, with its preponderance of small printshops, was hit hard by the economic recession. Nevertheless, following the merger in 2002 of Karat Digital Press with Koenig & Bauer and the integration of the 74 Karat in the production workflow at our Radebeul facility, we see plenty of potential for expanding sales beyond the USA and western Europe, the present markets. The launching of a coater version brought a big surge in sales of this B2 press for short-run colour, notably in the Middle East and North Africa.

**Sales
Sheetfed Offset Presses**
in million €



**Order Intake/Backlog
Sheetfed Offset Presses**
in million €



Our success last year in the Far East, Australia, North Africa and Latin America, and the expansion of market share in Europe and America, furnish a springboard for future growth in the sheetfed offset market. Extending our product range into smaller formats with our Genius 52 conventional press and 46 Karat digital offset press, and the launch of a super-large format press – the Rapida 205 – at Drupa 2004, will enable us to address a broader customer base and reaffirm our pole position in large format.



700 print professionals from 21 countries attended an Oktoberfest at our Radebeul facility in September

Poor Demand for Web Presses

The web and special press division suffered from newspaper and commercial printers' dependence on advertising income, which declined by varying degrees from one region to another. Although turnover, at €734.8m, was just 2.4% down on 2001 (€752.5m), this figure was boosted by contracts carried over from previous years. The market downturn was more truly reflected in a 25.4% slump in new orders to €508.5m, from €681.8m.

The biggest contracts for newspaper presses were placed by publishers in the USA (Kansas City Star), Switzerland (Tamedia in Zurich and Espace Media Groupe in Bern), Canada (Metroland Printing near Toronto) and Iceland (Morgunbladid in Reykjavik), but very few big



We are optimistic that new kit for commercial web offset, publication rotogravure and newspaper production will help stimulate investment in the printing industry

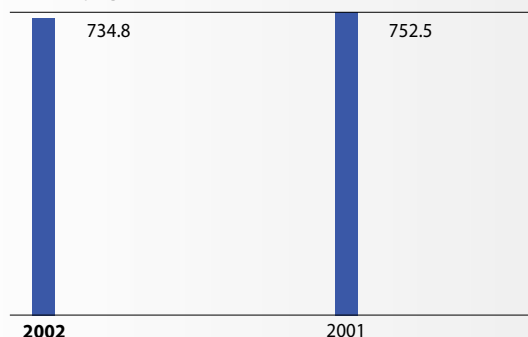
projects came up for tender in the domestic market and the rest of the EU. Sales of commercial web offset and publication rotogravure presses included a big gravure press line for France, the first 64-page commercial press in Scandinavia, for a customer in Finland, and 16-page Compacta 215 press lines for the Czech Republic, Turkey and Mexico. In many countries, overcapacity in the commercial market due to a slide in print sales culminated in a price war and a mounting number of bankruptcies.

Over the past two years or so more and more printers and publishers have shelved or postponed their plans to invest in new equipment, and by 31 December 2002 the backlog of orders for web and special presses had shrunk 26.9% to €615.4m (2001: €841.7m). With the market

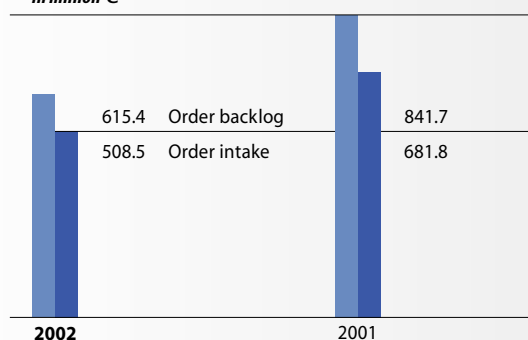
outlook clouded by political uncertainties we do not expect the situation to improve in the short term. However, we are confident that new products like our waterless Cortina press will stimulate investment in smaller press lines.

In the security press sector, new products and systems for quality control, counterfeit prevention and the preservation of banknotes played an increasingly significant role in generating sales alongside traditional machines.

Sales Web and Special Presses in million €



Order Intake/Backlog Web and Special Presses in million €



KEY REGIONS



Overseas Sales Up – European Sales Down

Economic stagnation in Germany pushed the proportion of domestic turnover to total turnover down to a historic low of 18.9%, from 19.6% in 2001, though the volume of domestic sales remained unchanged at €255.8m. Order bookings for both newspaper and commercial web offset presses were also down, the latter a consequence of overcapacity in the marketplace. Sales of sheetfed presses remained steady, and here we were able to corner a bigger share of the market.

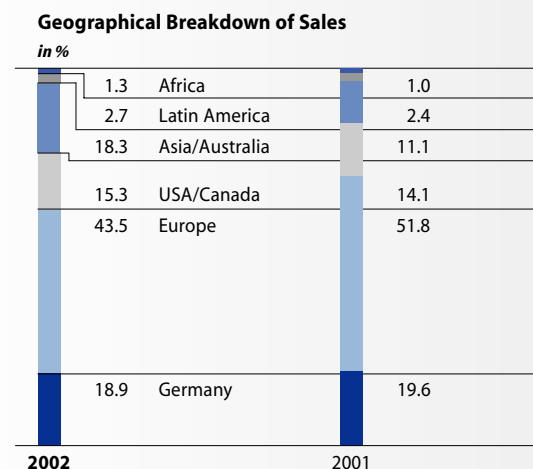
Group turnover in the **rest of Europe** was €589.2m, well below the previous year's figure of €675.7m. Here, too, the economic downturn was largely to blame. Our sheetfed division, however, not only maintained a high volume of bookings in Italy, France, Spain and the UK but also stepped up sales in Austria, the Benelux states, Russia, Ukraine and other East European markets. Incoming orders for web presses included two big contracts from Switzerland for our new triple-width newspaper press and the first order, from Russia, for a single-width Comet.

To expand our sales and service network in key Scandinavian markets we established a new 50.2% subsidiary, KBA Nordic A/S, which is based in Denmark with branches in Finland and Sweden. At the beginning of the year we also increased our stake in Print Assist AG, our Swiss agency, from 33.3% to 100%. In the Netherlands we appointed Wifac bv in Mijdrecht our sole agent for the sale and servicing of KBA sheetfed presses, alongside our established web agency, Van Dijk Grafische Machines. Wifac made its name as a prominent provider of pre-press equipment. We are confident that this move will enable us to strengthen our presence in the Dutch sheetfed offset market in line with our standing in the web press sector.

But growth in KBA sales was generated almost exclusively outside Europe. In North America we defied the ongoing economic slowdown to post a double-digit jump in turnover compared to 2001 and booked a larger volume of orders for both sheetfed offset and newspaper presses. The **USA** and **Canada** accounted for 15.3%, or €207.1m, of total turnover, up from 14.1% (€183.4m) the previous year. Our subsidiaries KBA North America, Inc., Sheetfed Division, in Williston, Vermont, and KBA North America, Inc., Web Press Division, in York, Pennsylvania, were merged in a holding company (and 100% Koenig & Bauer subsidiary), KBA North America Inc., based in Wilmington, Delaware.

Turnover in **Latin America** also grew in 2002, mainly as a result of shipments to Brazil and Mexico, and totalled €36.8m or 2.7% of Group turnover (2001: €31.3m). Sales in **Africa** climbed to €16.9m, from €12.9m in 2001. Expanding beyond our established markets, South Africa and Egypt, we also sold sheetfed presses to Algeria, Tunisia and other North African states.

Asia – and above all the People's Republic of China – once again proved to be a region of high growth. The shipment of big newspaper press lines to Singapore and a rapidly expanding trade in sheetfed presses for China pushed up our sales in Asia by almost €100m to €243.5m (2001: €144.5m). The Far East thus accounted for 18% of total turnover in 2002 (2001: 11.1%) – well ahead of North America, the world's biggest single market for printing



presses. Our sales and service subsidiary in China, with branches in Beijing, Guangzhou, Hong Kong and Shanghai, will strengthen our presence in 2003 with the addition of another new outlet, KBA Printing Machinery (Shanghai) Co. Ltd., in the Shanghai special economic zone. Our subsidiary KBA Asia Pacific Sdn. Bhd. in Kuala Lumpur, Malaysia, opened a sheetfed sales and service branch in Singapore to serve the high-growth markets outside China and Japan.

2002 also saw the establishment of a new sales subsidiary, KBA Australasia Pty Ltd. in Sydney, **Australia**, covering New Zealand and the Pacific rim as well. The new subsidiary sold its first KBA sheetfed presses and a newspaper press line, all to Australian printers, within a few months of starting up in business. Turnover, which in 2002 came to €4.5m, will be appreciably higher in 2003 and will continue to rise in years to come.

RISK MANAGEMENT



Controlling Group Risk

Entrepreneurial activity is inseparably associated with risks and rewards. The purpose of risk management within the KBA Group is to control and limit the risks and reap the rewards.

The risk management system introduced in 1999 was developed and perfected in 2002. It is an integral component of business processes and thus closely linked with planning, management and controlling.

Risk management procedures are defined in a set of principles applied throughout the Group, and ensure a uniform documentation, assessment and systematic control of existing and potential risks. An analysis of pertinent risks and a description of the remedial or anticipatory action taken is included every quarter in our reporting procedures. In addition the management board is instantly alerted to any change in risk potential.

All our subsidiaries submit regular progress reports comparing their achievements with the targets they have been set. Risks to Group finances, assets and profits can thus be detected at an early stage and countermeasures initiated.

The efficacy of our risk management system is monitored by our internal auditing department and its implementation confirmed by external auditors. The findings are incorporated in our risk management system. The following risks are of particular relevance to KBA's future success:

Economic and Industry-Related Risks

As a globally active press manufacturer the Koenig & Bauer Group has been directly affected by the downturn in the global economy and the subsequent drop in sales of capital equipment. Weakening demand has engendered fierce competition on pricing, financing and delivery conditions. To counter these risks we conduct in-depth market analyses, offer customised press configurations and focus our research and development activities on market-driven technologies and processes. Above and beyond this, in 2002 we also stepped up our activities in key markets, specifically in Asia, Australia, China and Scandinavia, by establishing and expanding our sales and service subsidiaries.

Market and Business Risks

Intense competition and overcapacity in certain regions and sectors have led to a succession of mergers, which in turn has diminished our customer base while enhancing customers' negotiating power. This has been reflected in higher quality and service expectations and downward pressure on prices.

We address pricing pressures with effective cost management, moves to promote customer loyalty, product differentiation and processes, and the development of new markets. The financial and technical risks inherent in the acquisition of major contracts are limited by project management and the relevant project controller.

Delivery time frames have been cut by streamlining engineering processes, reducing internal throughput times, optimising materials logistics and uniting our plant utilisation and production control systems.

The knowledge and experience gained during each new project is applied in the downstream workflow, bringing a continuous enhancement in product and service quality.

A careful vetting of suppliers, in tandem with rigorous quality management, helps minimise risks arising from the late delivery or substandard quality of outsourced goods. To contain price risks relating to goods procurement we keep a close watch on the market and issue performance benchmarks for suppliers.

Financial Risks

Financial risks basically include loss of liquidity, loss of receivables outstanding, currency risks and risks incurred through the use of financial instruments.

Group liquidity is safeguarded and controlled through ongoing financial analysis and planning. Debts are monitored regularly as part of debt management. Potential risks in corporate financing are thus detected at an early stage so that remedial measures can be taken.

More and more customers are requesting alternative financing schemes, so we have substantially expanded our activities in this area. The risks accompanying an increase in customer financing are passed on to refinancing and credit insurance agencies.

The transfer of sales activities to regions outside the euro zone has resulted in a larger number of contracts being concluded in foreign currencies, especially in US dollars. Currency fluctuations between the euro and the dollar or the Japanese yen are linked to competitive risks. However, since the biggest press manufacturers are all concentrated in Europe, we believe these risks are manageable. Close collaboration between our sales and finance departments enables us to actively manage risks from currency fluctuations and significantly reduce or eliminate them by using derivatives.

Risks linked to changes in short-, medium- and long-term interest rates are monitored on an ongoing basis and actively limited, while opportunities offered by fluctuations in interest rates are sensibly exploited.

Other Risks

Other risks relate to IT systems, human resources planning, product launches and litigation.

We guard against these risks within the areas in which they arise. For example, in 2002 internal data security within and among Group enterprises was improved with new encoding systems. A firewall was installed to guard against malicious external interference.

Personnel risks are managed by employing contract workers, outsourcing more work during production peaks and by providing further training for employees.

The risks and rewards associated with the introduction of new products and processes are assessed using market analyses and customer surveys. The launch of our new waterless offset newspaper press, the Cortina, was preceded by exhaustive test runs and feasibility studies.

Business-related risks are covered by specific reinsurance agreements and the appropriate provisions.

Total Risk

In comparison to the previous year the total risk potential has increased in line with economic and competitive risks. However, the measures described above represent a deliberate and controlled means of hedging such risks. At present no risks have been revealed that could threaten the continued existence of the KBA Group.

CORPORATE GOVERNANCE



Implementing Germany's Corporate Governance Code

At the end of February 2002 a government commission unveiled a blueprint for a new German Corporate Governance Code. The purpose of the Code is to harmonise the rules governing corporate management and supervision, make the national principles of corporate governance more transparent, eliminate issues that have drawn fire in international markets and restore investors' confidence in the management of publicly traded companies in Germany.

Later in the year the legislature passed a Transparency and Publicity Law, creating a legal basis for the issue of a joint declaration of compliance by management and supervisory boards. With effect from the 2002 business year, §161 of Germany's Company Law obliges all listed companies to state openly whether they intend to comply with the recommendations contained in the Corporate Governance Code or, where full compliance is held to be impractical, to disclose on which points they will deviate from the recommendations. We welcome the chance this new Code offers the market of regaining the faith of investors repelled by accounting scandals and market rigging.

The basic recommendations contained in the Code were incorporated in our mode of operation some time ago. In 1999 we started issuing quarterly reports, in 2001 we embraced the principle of one share, one vote by converting non-voting preferred shares into ordinary voting shares and in 2002 we adopted IFRS accounting procedures. Two years ago we started transmitting the AGM live via the internet, and shareholders and their representatives can also download additional information from our home page.

The interaction of the various executive organs also complies in essence with the principles laid down in the Code. For example, our Company president regularly contacts the chairman between the scheduled meetings to discuss topical issues relating to business performance and strategy. The supervisory board appoints committees to investigate issues central to the board's business.

In the course of the current year we shall comply with the recommendations contained in the Code concerning provision for D&O liability insurance and the introduction of an age limit for members of the executive. We believe this recent legislation will promote an open, more understandable corporate culture.

HUMAN RESOURCES AND WELFARE



"Our management philosophy is anchored in personal initiative coupled with team spirit."

KBA guiding principles

Adapting to the Market Climate

Human resources management in 2002 was largely dictated by the decline in the volume of new orders, which in the second half of the year impacted on the backlog of orders for web presses. Although the first six months were relatively busy thanks to some big contracts from previous years, plummeting demand made itself felt in no uncertain terms as the year progressed. Bulging order books at our sheetfed offset plant, however, kept our Radebeul facility running at full capacity. On 31 December 2002 the Group payroll stood at 7,391, slightly down on the previous year (7,561). This figure includes an additional 124 employees taken over following the integration of Karat Digital Press in Radebeul and the termination of some 400 temporary contracts by mid-year.

Utilising Flexible Work Practices

The payroll was pared by terminating loan and temporary contracts and by expanding flexitime. Overtime accounts were steadily reduced and from the beginning of September working hours at our web press facilities were cut by 20% through the introduction of short time. In addition a voluntary redundancy scheme was introduced and pre-retirement part-time work utilised more fully. In return most of the apprentices who completed their training were offered employment contracts, albeit initially for a limited period.

Expanding Performance-Related Remuneration

The performance-related executive remuneration system introduced in 2001 at all our Parent operations, and based on mutually agreed personal and corporate targets, was expanded to include group work by wage-earning employees. In addition all our members of staff have a direct interest in company performance through profit-sharing and employee share schemes.

The introduction of group work in Radebeul was completed in 2002. More than three-quarters of the staff there are now paid by performance. Group work based on individual and team accountability was also expanded in Würzburg and Frankenthal, with manufacture and assembly currently in the transition phase. Here our key criteria are timeliness and quality, allied with our annual corporate goals. The targets for managerial staff are linked to company profits and the achievement of individually defined goals. Among other things this has resulted in progressively fewer glitches and delays, and improved communication and collaboration among the individual production departments.

In 2002, for the first time, employees were offered the chance to buy company shares at a discount. Each employee was entitled to purchase up to 18 shares, using the benefits accrued from the profit-sharing scheme for 2001, which was a record year. More than two thirds of the workforce took advantage of this offer.

Average Group Payroll

2002	517	Apprentices/ students	510
	2,744	Salaried office staff	2,715
	4,130	Wage-earning industrial staff	4,336
	7,391	Total	7,561
2001			

Focusing on Personnel Advancement

Once again, further training for our specialist and managerial staff ranked high on the list of priorities for our human resources activities. A three-year development programme for production executives drew to an end but training for new and junior executives continued. A special recruitment campaign was launched at universities and this included sponsorships and support for final-year students writing their theses.

Ongoing Enhancement

Our ideas management scheme, which was overhauled in 2001, was hugely successful once again, with around 1,500 suggestions submitted. This enabled us to achieve an even bigger cost saving than in the previous year. Promotional campaigns motivated staff to make more active use of ideas management as an instrument of continual improvement.

Enlarging our Pension Scheme

The creation of a single pension scheme for the Parent company's entire payroll represented a milestone in our company welfare scheme. Following the inclusion of all the staff at our Radebeul sheetfed offset division the Würzburg pension fund initiated payments to the company's 78 pensioners as well. An employer-financed private pension scheme was also launched in collaboration with Gesamtmetall (employers' union) and IG Metall (trade union). KBA supports private pension plans by contributing up to 20% of the total premium. In November 2002 advisory sessions were held at all our facilities.

Heroic Flood Defence

When the Elbe overflowed its banks in August last year our Radebeul management and staff rose magnificently to the occasion. In less than two days they erected a dam 300 metres long to keep the floodwater away from the production halls. Thanks to their heroic efforts, and the invaluable support provided by emergency services from all over Germany and from across the border in Poland, no plant or buildings suffered any significant damage. However, 80 active and retired members of the workforce incurred flood damage to private property. An appeal launched by the works council and company management prompted a wave of solidarity not only among employees at our other facilities but also among customers, suppliers and friends. Some €580,000 in donations was collected and distributed unbureaucratically to the flood victims. Management and staff in Radebeul thank all concerned for the help and donations received.

Continued High Level of Apprentice Training

Investment in training new staff is a basic essential for creating innovative products and delivering services to the satisfaction of our customers worldwide. At KBA, young people can qualify in a wide variety of technical professions – as a press operator, media designer, energy electronics engineer, electromechanic or metalworking mechanic – as well as in management and administration. The outstanding performance of our apprentices in the regional examinations set by the Chambers of Industry and Commerce in Ludwigshafen, Radebeul and Würzburg



In 2002 more than two-thirds of our workforce took advantage of our new employee share scheme

are evidence of the high standard of training they receive. For the third time our Radebeul facility was awarded a certificate of excellence for the quality of its training programme. In 2002 Koenig & Bauer trained 433 apprentices, of whom 123 completed their final year. 106 of these were given employment contracts.

The company sickness benefit fund offered its 12,528 members (2001: 11,618) active preventive care in addition to its standard services, and also organised courses targeting apprentices and younger employees.

Last year 140 members of staff were awarded long-service bonuses. 88 completed 25 years of service, 50 celebrated their 40th and two their 50th jubilee.

A Big Thank-you

The 2002 business year brought a series of challenges for the workforce and their representatives alike. We would like to thank all our staff for the energy and initiative they have shown in mastering these challenges, and for their constructive collaboration and support.

RESEARCH AND DEVELOPMENT



"Our objectives is to furnish printers with the means to achieve a better quality print faster, more cost-effectively and more ecologically."

Claus Bolza-Schünemann, executive vice president, web press engineering and project management

Innovation to Fight Stagnation

Innovation is all the more crucial in an economic downturn because it enables us to escape the trap of competing purely on price, strengthen our market standing and attract new business by offering genuine technological advances. In 2002 we invested heavily in the development of new technologies, products and processes for both our business divisions (web/special presses and sheetfed presses), while continuing to enhance our existing product range. At the end of 2002 a total of 890 members of staff were employed in R&D, process technology, engineering and project management at the Parent company. This is almost 16% of the active workforce, apprentices excepted.

Promoting Alliances

Over the years, through close collaboration with manufacturers in the pre-press, peripherals, finishing and consumables industries, and an ongoing dialogue with universities and other institutions, we have established a formidable reputation as an engine of innovation in production processes and as a driving force for more efficient, flexible and rationalised print production. This has enabled us to expand our share of the market.

Examples of successful joint R&D projects for sheetfed presses include inline coating using hybrid inks, direct offset on fine corrugated, environmental accreditation for all our conventional and UV Rapida presses and, in collaboration with Metronic, the Genius 52 waterless offset press for small-format short-run colour. Web press R&D activities focused on our compact Cortina waterless newspaper offset press and a new generation of ultra-wide rotogravure presses.

New Dimensions in Sheetfed Offset

Fierce competition in the market for standard print products has engendered a move towards more individual and thus more sophisticated, often lengthier, press configurations. Here the aim of print entrepreneurs is to operate more cost-effectively by integrating as many printing and coating features as possible in one machine, so that clients can be offered a broader, more imaginative range of products. The superiority of the technology and processes that KBA Radebeul has developed to address specific customer demands has made us a defining player in medium- and large-format sheetfed offset.

The installation in South Africa of the world's first medium-format press for five-colour perfecting plus inline coating was followed at the end of the year by the shipment to a US customer of a Rapida 142 almost 38 metres long, configured with eight printing units, two coaters, an intermediate dryer and automatic conversion between straight and perfecting printing. At present only KBA can offer technological masterpieces such as these. The same applies to the first eight-colour Rapida 162a for four-colour perfecting in size 7, whose inauguration at a German printing plant in summer 2002 prompted a succession of new orders for similar press lines. The integration of a coater in our 74 Karat digital offset press has also proved popular in the market.

Most of the work carried out by our Radebeul development engineers in 2002 was in preparation for the world's biggest trade fair for the print industry – Drupa 2004 in Düsseldorf. We shall be defending our position at



The world's first double-width waterless newspaper press went into operation at reiff zeitungsdruk, Offenburg, in autumn 2002

the cutting edge of technology with a variety of new modules for optimising the workflow, new features in all format classes and the debut of our new Rapida 205 for a sheet size of 1,520mm x 2,050mm.

New Ideas for Web Presses

In the web and special press division, the successful testing and sale of the world's first 6-across newspaper offset press, a Commander, to publishing houses in Switzerland demonstrated the unparalleled competence of our development engineers. The press features a number of innovations, eg for cutting makeready and maintenance



Almost 16% of our active workforce is employed in R&D, process technology, engineering and project management

work and enhancing print quality, which can be incorporated in our other newspaper press types as well.

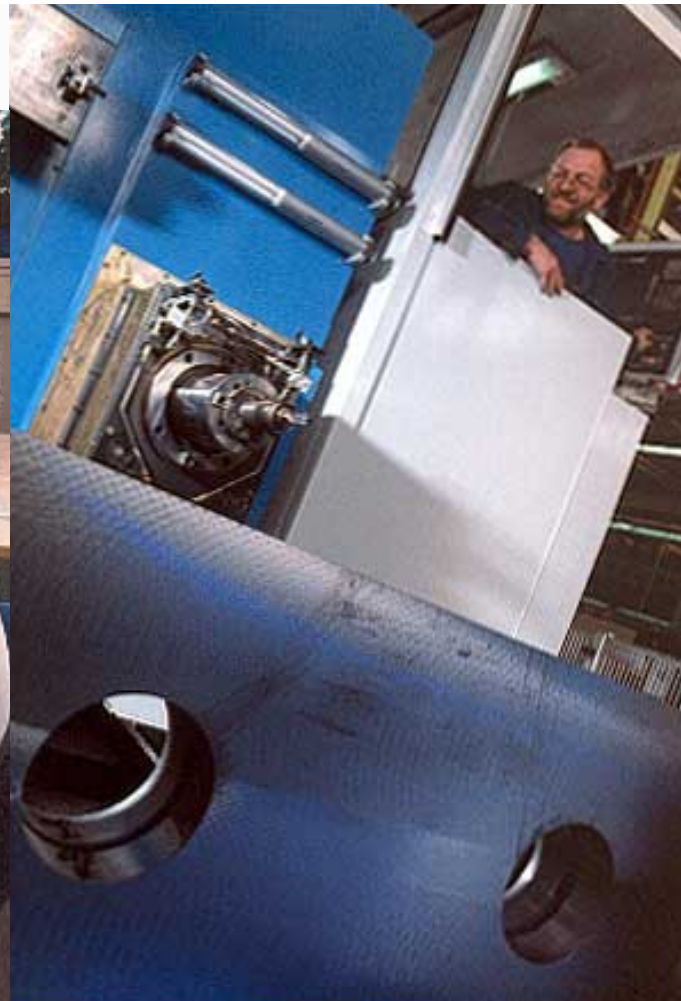
The inauguration of the first double-width Cortina four-high tower press for waterless newspaper offset at reiff zeitungsdruk, Offenburg, last autumn represented a further milestone in this major project. At the beginning of April we held an open house in Offenburg to promote the Cortina as a mature product and ideal tool for the international print market.

The development of the TR12B, a new publication rotogravure press for a record web width of 4.32m, underscored our role as a technological leader and

pioneering force in the global marketplace. The first press lines were sold to a German customer earlier this year. Our commercial web offset engineers in Würzburg and Frankenthal are also working on a new product line scheduled for launching at Drupa 2004.

Research on security presses, traditionally a key market for Koenig & Bauer, centred on systems for enhancing quality control and counterfeit prevention.

PRODUCTION, ORGANISATION, INFORMATION TECHNOLOGY



"We are driven by a determination to ensure that the quality targets we define are implemented 100 per cent in our own manufacturing processes. Which is why we were the first press manufacturer worldwide to achieve ISO 9001 accreditation."

Peter Marr, executive vice president, web press production and purchasing

Flexibility the Focus of Production Strategy

Just-in-time manufacture by small, flexible units which maintain a customer-supplier relationship with each other is a strategic goal in realigning production to create a location-based works structure. Smaller batches, manufactured by semi-autonomous work groups, help cut throughput times and increase turnover. Our production islands were set priority targets of cost-efficiency and timeliness, while job scheduling and processing were rationalised to reduce inventories and, at the same time, delivery time frames.

Embedding Production in a Trade Network

The transition to the new works structure was completed early last year. Basically this means that each production site focuses on a core competence, which promotes a more efficient utilisation of resources. Our main factory in Würzburg, for example, specialises in the manufacture and machining of large components for web presses, while our Frankenthal plant supplies the KBA Group with rollers and folders. Our entire security press production line is being transferred to our Austrian subsidiary, KBA-Mödling near Vienna, which has discontinued the production of printing units for web presses and now concentrates on expanding security press activities and supplying sheetfed offset subassemblies to our Radebeul plant. KBA-Berlin produces reelstands for our web press operations. Manufacturing and final assembly facilities at our Radebeul plant were expanded.

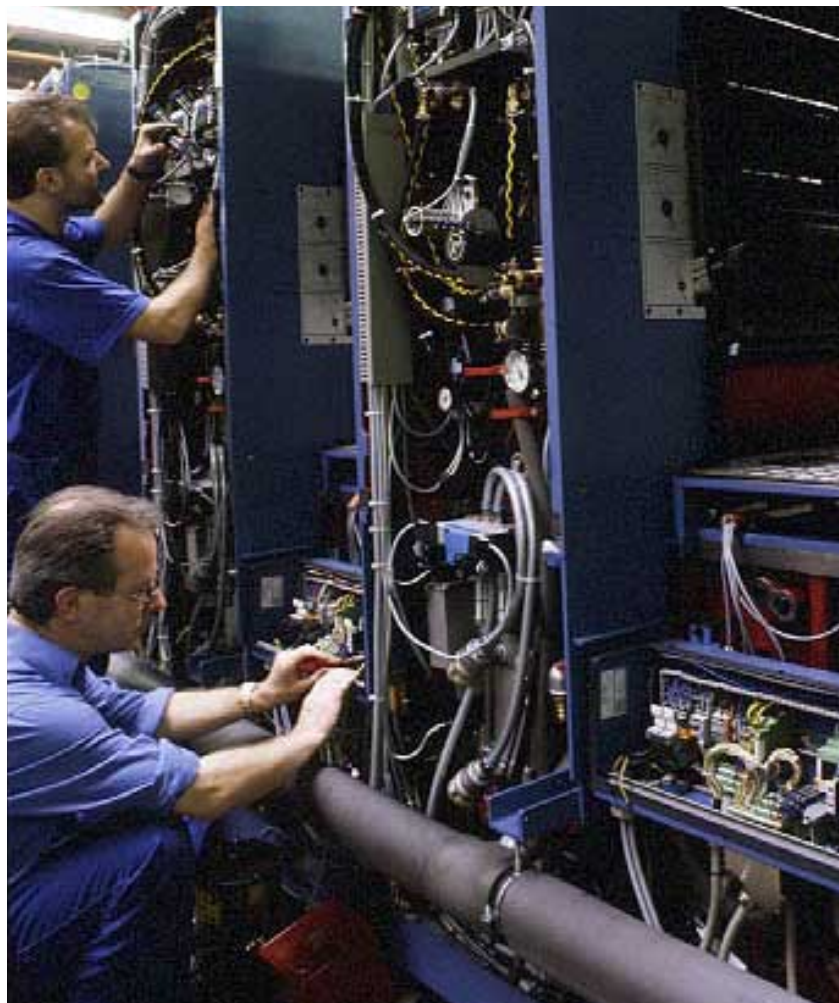
Cutting Lead Times

Intensive executive and staff training and the delegation of scheduling management to the manufacturing level and assembly islands enabled us to shorten the lengthiest production chains and to cut production times for key components and subassemblies. This, together with the delegation of accountability to the semi-autonomous work groups at the production islands, was instrumental in shortening delivery and commissioning times in line with market demand.

A move in the market towards smaller projects and customised configurations also means that contracts must be completed much faster than before. The construction of a new production hall in Würzburg, which was started in July 2002 and is slated for completion in the middle of this year, addresses this issue and represents a major component in our concept for developing the factory and optimising the materials flow and production chain.

Enhancing Workflow Organisation

Improving workflow organisation and defining more precisely the demarcation lines between the organisational units are major factors in implementing a location-based works structure. Clear delimitations are indispensable for a production flow based on profit centres and the delegation of accountability, accompanied by agreements on operational targets, variable executive compensation and performance-related remuneration of the semi-



The group-work system introduced at our Radebeul sheetfed offset operation has substantially enhanced productivity. This photo was taken during final assembly

autonomous work groups. In future, group targets will be monitored on a rolling basis to improve work sequences. Preparations for internal performance reviews also included the documentation and evaluation of internally provided IT services, with efficiency gains and greater customer orientation anticipated from the creation of an internal market.

In March 2002 our Radebeul plant once again achieved ISO 9001 accreditation and implemented the next stage of our production strategy. This has made the interplay of processes, sequences and the different production areas more transparent, enabling us to handle contracts much more efficiently.



Each of our production sites now focuses on a specific core competence, promoting a more efficient utilisation of resources

Expanding our Information Technology Network

Information technology plays a key role in the exchange of data among our various facilities. To enhance the co-ordination of Group-wide applications an IT management board manned by representatives from each of the Parent's facilities was established alongside a steering committee to monitor its activities. A plan for the medium-term documentation of IT activities was also drawn up.

Networks were expanded to handle a big increase in the volume of data generated by the use of 3-D CAD and a product-data management system. KBA-Mödling was the first of our foreign subsidiaries to be integrated in the central SAP system.

INVESTMENT AND ECOLOGY



Greener Products and Processes

The development of ecological printing and finishing processes and the conservation of natural resources during the production and operation of printing presses were, once again, the nub of our activities in 2002.

Our entire range of Rapida sheetfed presses has already been awarded eco-certification by the Trade Association for Printing and Paper Processing and by allied European organisations. This has been reflected in higher sales among environmentally aware print entrepreneurs.

Waterless Offset for Sheet and Web

We are also enhancing web press ecology, for example by eliminating or reducing the volume of alcohol used with commercial presses, improving solvent recovery in publication rotogravure and developing waterless offset processes for newspaper presses like the Cortina. The first press of this type commenced beta-testing in autumn 2002 at a newspaper publishing house in Germany.

In 2002, as in previous years, cutting production times was one of our prime objectives in installing new machining centres

Waterless offset, which is also the process used in our 46 and 74 Karat digital sheetfed presses and in our new small-format conventional press, the Genius 52, offers substantial ecological benefits: it slashes start-up waste, eliminates the need for environmentally sensitive dampening additives and supports the use of process-free ctp plates.

Ongoing Emissions Reduction

But effective environmental protection begins with the workflow in our own production halls. Here we continued to make good progress in 2002. Preventive measures included the extraction and filtering of aerosols and exhaust emissions directly at source, a wider use of sealed circuits for cooling lubricants and the introduction of a recycling system for oily cleaning rags. In addition around 8,000m² of production floor space was sealed to prevent possible contamination of groundwater and subsoil by hazardous substances.

To cut down the volume of solvents used in spraying the side frames we started switching from multiple- to single-application paints.

Further action was taken to reduce and sort waste more effectively. Investment in new buildings centred on making workplaces more ergonomic and on limiting noise and dust emissions. We improved working conditions in the foundry at our Würzburg facility by installing noise insulation and automated conveyor lines.

Investment Matches Depreciation

With plant utilisation at our web press facilities hit by the economic downturn, new investment concentrated on enhancing cost efficiency and cutting lead times. Investment in intangible Group assets, property, plant and equipment totalled €51.7m (2001: €81.4m). €43.3m (2001: €66.8m) was spent on upgrading machinery and equipment, furniture and fixtures. Depreciation stood at €45m (2001: €38.5m).

A new one-stop machining centre for large and often complex prismatic components was commissioned at our Würzburg plant. The pallet-changing system connected to it has boosted productivity by allowing new work pieces to be inserted without interrupting operation. Two new CNC boring mills for large components were also installed.

In July the foundation stone was laid of a new production hall for the serial manufacture and assembly of impression cylinders in Würzburg. It will come on stream in a few months time. The steel and sheet-metal store will be moved to the new hall to enable the cutting machines for production materials and sheet metal to be loaded automatically. The additional space will enable us to reorganise and refurbish our existing production halls and integrate them in the logistics system.

The commissioning of two CNC turning centres and a roller-grinding machine has upgraded the roller machining centre and streamlined manufacture at our Frankenthal facility.

New CNC machining centres for prismatic small components and cylinder manufacture were also commissioned at our sheetfed offset plant in Radebeul. Following nine years of dynamic growth, and the integration of Karat Digital Press in our sheetfed offset operations in 2002, work also started on a new administration building for assembly and service management, complete with a demonstration centre for digital presses. The building will be inaugurated in September.

RESOURCE MANAGEMENT AND LOGISTICS



"The superior quality of our sheetfed offset presses has become an industry benchmark, and our customers reap the reliability and performance benefits."

Dr Frank Junker, executive vice president, sheetfed offset production and service

Streamlining the Procurement and Flow of Materials

Resource management focused on optimising cost prices and securing the supply of parts. Additional savings were achieved by negotiating umbrella agreements for all our production facilities. We are making increasing use of electronic order handling via e-mail as a means of rationalising and accelerating procurement procedures. In addition we are collaborating with the School of Business Information Technology at Würzburg-Schweinfurt University to develop systems supporting the use of e-commerce, and with strategic suppliers to create a managed supply chain. Long-term alliances with systems providers, and the formation of supplier groups, are also expected to bring appreciable benefits.

Integrating New Logistics Centres

In the course of the 2002 business year the new logistics centres in Würzburg and Radebeul were embedded in the goods and materials flow, bringing a huge improvement in parts supply to the production and assembly islands. This enabled us to eliminate buffer stores, significantly increase production turnover and reduce the capital-intensive storage of subassemblies and assemblies. Optimising logistics within our after-sales service department promoted a faster response to customer orders for spare parts.

Adjacent to the logistics centre at our Würzburg facility we are building a new 10,000m² production hall for cylinder machining, pre-assembly and panel beating. Once it is up and running later this year it will streamline the materials flow still further.

OUTLOOK FOR 2003



"Extending the frontiers of press technology has been a tradition at Koenig & Bauer for more than 185 years. Our enduring aim is to provide printers throughout the world with the most advanced systems and processes on the market."

Albrecht Bolza-Schünemann, deputy president

Subdued Prospects for the Print Trade

After seeing their hopes dashed in 2002, market watchers doubt that 2003 will witness a rapid rebound in the global economy to the previous high rates of growth. The outlook for the advertising, graphic arts and press manufacturing industries is correspondingly subdued. Investors' shattered faith in the markets is being tested still further by the war in Iraq and political developments in North Korea. The knock-on effects on energy prices, the economy and international trading are difficult to calculate and represent a psychological hurdle to further investment and higher consumption.

Capital investment by members of the printing industry in major markets such as Western Europe, North America and Japan is unlikely to budge above last year's glacial level in the months to come. However, sales prospects are good in China, where strong growth combines with a huge pent-up demand for print, and also in Eastern Europe, where many countries are gearing up ready for admission to the EU.

In view of the troubled economic and political climate, and the volume of orders scheduled for shipping this year, we anticipate a slight decline in annual Group turnover compared to 2002.

Although demand was softer overall, sales of sheetfed and special presses are on course to match last year's level. However, on current calculations, turnover in newspaper and commercial web presses – the mainstay of our Würzburg and Frankenthal operations and their branch factories – will fall approximately 10% as the backlog of orders from previous years diminishes and industry players continue to fight shy of making capital commitments.

To absorb this reduction in plant utilisation at our web press facilities, short-time work, which was initially introduced for a period of six months to 28 February, has been extended to the end of September. Staff cuts in the web and special press division were made last year by terminating temporary labour contracts, introducing a voluntary redundancy scheme, extending the use of phased retirement and exploiting natural wastage by leaving vacant posts unfilled. These measures are being continued in 2003. If the market situation does not materially improve in the next few months we cannot exclude the possibility of more radical measures for downsizing capacity.

Incoming orders for sheetfed presses remained steady in the first quarter of the current year. The web press division, however, despite winning contracts from China and South Korea for newspaper press lines, and from a German publishing house for the first installations of our new TR 12B rotogravure press for a web width of 4.32m, was unable to secure the volume of smaller orders needed to fill plant capacity in the short term. The total turnover generated by our web and special press division in 2003 will depend on the number of additional orders we can book by mid-year for batch-produced single-width newspaper and commercial presses.

A reliable forecast of our performance in 2003 at this early date is made all the more difficult by the fact that it will not become clear until much later in the year whether investors are adopting a "wait and see" approach prior to the Drupa trade fair in May 2004.



Our ultra-compact Genius 52 is a revolutionary new system for delivering small-format prints even faster and more economically

Against this backdrop of political tension, economic stagnation and market malaise a concrete prediction of Group results for the current year would not be in keeping with our corporate policy of issuing credible, reliable communications – particularly when the going gets tough.

Nonetheless, in conjunction with the cost-cutting measures we have initiated, our objective is to post an operating profit for the year as a whole. We shall publish a more precise prognosis at the end of the quarter, based on developments in the economy and print industry.

Financial Statements for the KBA Group

46 Balance Sheet

47 Income Statement

48 Statement of Changes in Shareholders' Equity

49 Cash Flow Statement

50-80 Notes to the Financial Statements

50 (A) Preliminary Remarks

50 (B) Accounting Policies

53 (C) Consolidated Companies and
Consolidation Principles

54 (D) Foreign Currency Translation

54 (E) Notes to the Adoption of IFRS

58 (F) Non-current Asset Movement Schedule

60 (G) Explanatory Notes to the Balance Sheet

60 (1) Non-current Assets

62 (2) Inventories

62 (3) Receivables and Other Assets

63 (4) Securities

63 (5) Cash and Cash Equivalents

64 (6) Deferred Taxes

65 (7) Equity

65 (8) Pension Provisions

67 (9) Other Provisions

68 (10) Liabilities

69 (11) Derivatives

70 (12) Other Financial Commitments and
Contingent Liabilities

71 (H) Explanatory Notes to the Income Statement

71 (13) Revenue

71 (14) Expenses by Function

72 (15) Expenses by Nature

72 (16) Other Operating Income and Expenses

73 (17) Financial Result

74 (18) Income Taxes

74 (19) Earnings per Share

74 (I) Explanatory Notes to the Cash Flow Statement

75 (J) Segment Information

76 (K) Related Party Relationships

77 (L) Management and Supervisory Boards

78 (M) Proposal for the Utilisation of Net Profit

79 (N) Auditors' Report

80 Key Financial Dates / Contacts

Group Balance Sheet to 31 December 2002

Assets			
in T€	Note	31.12.2002	31.12.2001
Non-current assets	(1)		
Intangible assets		35,397	23,906
Property, plant and equipment		247,618	233,633
Financial assets		15,433	14,611
		<u>298,448</u>	<u>272,150</u>
Current assets			
Inventories	(2)	388,634	498,457
Trade receivables	(3)	384,391	345,080
Other receivables and assets	(3)	72,543	62,461
Securities	(4)	13,103	31,381
Cash and cash equivalents	(5)	44,045	70,491
		<u>902,716</u>	<u>1,007,870</u>
Deferred tax assets	(6)	39,399	54,086
		<u>1,240,563</u>	<u>1,334,106</u>
Equity and liabilities			
in T€	Note	31.12.2002	31.12.2001
Equity	(7)		
Issued capital		41,786	41,600
Capital reserve		81,505	79,948
Revenue reserves		324,199	291,430
Net profit		28,113	39,973
		<u>475,603</u>	<u>452,951</u>
Minority interest		0	189
Provisions			
Pension provisions	(8)	82,509	79,066
Tax provisions	(9)	3,496	2,136
Other provisions	(9)	180,398	183,828
		<u>266,403</u>	<u>265,030</u>
Liabilities	(10)		
Bank borrowings		132,876	109,504
Payments received on account of orders		197,463	301,292
Trade payables		65,288	88,662
Other liabilities		54,255	58,045
		<u>449,882</u>	<u>557,503</u>
Deferred tax liabilities	(6)	48,675	58,433
		<u>1,240,563</u>	<u>1,334,106</u>

Group Income Statement for 2002

in T€	Note	2002	2001
Revenue	(13)	1,353,755	1,304,024
Costs of conversion	(14)	– 1,051,888	– 1,022,962
Gross profit		301,867	281,062
Distribution costs	(14)	– 124,490	– 103,439
Administrative expenses	(14)	– 91,766	– 78,549
Other operating income and expenses	(16)	– 39,038	– 40,436
Profit from operations		46,573	58,638
Financial result	(17)	– 3,373	3,615
Profit from ordinary activities		43,200	62,253
Income taxes	(18)	– 15,087	– 22,282
Net profit for the period		28,113	39,971
Profit applicable to minority interest		0	2
Profit net of minority interest		28,113	39,973
Earnings per share (in €)	(19)	1.75	2.49

Statement of Changes in Shareholders' Equity

in T€	Share capital	Capital reserve	Revenue reserves			Other	Net profit	Total
			Original financial instruments	Derivatives	Currency translation			
1 January 2001	41,600	79,948	6,131	0	4,750	274,954	22,557	429,940
Prior year dividend	0	0	0	0	0	0	– 12,400	– 12,400
Net profit	0	0	0	0	0	10,157	29,816	39,973
Translation differences	0	0	0	0	284	0	0	284
Changes in value of financial instruments	0	0	– 4,846	0	0	0	0	– 4,846
31 December 2001	41,600	79,948	1,285	0	5,034	285,111	39,973	452,951
1 January 2002	41,600	79,948	1,285	0	5,034	285,111	39,973	452,951
Prior year dividend	0	0	0	0	0	0	– 16,000	– 16,000
Net profit	0	0	0	0	0	23,973	4,140	28,113
Capital increase from approved capital	186	1,557	0	0	0	0	0	1,743
Translation differences	0	0	0	37	3,228	0	0	3,265
Changes in value of financial instruments	0	0	– 1,187	6,718	0	0	0	5,531
31 December 2002	41,786	81,505	98	6,755	8,262	309,084	28,113	475,603

Cash Flow Statement

in T€	2002	2001
Profit from ordinary activities	43,200	62,253
Depreciation on non-current assets	45,046	38,467
Foreign exchange gain/loss	- 391	9,235
Interest income/expense	- 1,675	- 1,207
Loss on disposal of non-current assets	255	89
Gross cash flow	86,435	108,837
Changes in inventories	110,955	- 86,515
Changes in receivables and other assets	- 12,572	18,002
Changes in provisions	- 6,115	11,366
Changes in liabilities	- 155,463	- 89,312
Interest expense	- 5,524	2,118
Tax expense	- 11,441	- 4,246
Cash flows from operating activities	6,275	- 39,750
Proceeds from disposal of intangible assets, property, plant and equipment	2,509	2,518
Payments for investment in intangible assets, property, plant and equipment	- 51,698	- 81,433
Proceeds from disposal of financial assets	286	925
Payments for investment in financial assets	- 1,049	- 1,299
Payments for acquisition of consolidated companies	0	- 15,774
Investment subsidies received	2,500	2,675
Dividends received	68	58
Cash flows from investing activities	- 47,384	- 92,330
Proceeds from capital contributions	1,743	0
Proceeds from borrowings	36,656	65,862
Repayment of debt	- 35,325	- 2,163
Change in minority interest	- 189	8
Proceeds from repayment of loans to associates	0	3,538
Other changes in equity	5,567	- 4,846
Dividends paid (previous year)	- 16,000	- 12,400
Cash flows from financing activities	- 7,548	49,999
Change in funds	- 48,657	- 82,081
Effect of changes in exchange rates	3,933	- 694
Funds at beginning of period	101,872	184,647
Funds at end of period	57,148	101,872

For further information see explanatory Note (I).

Notes to the Financial Statements

(A) Preliminary Remarks

The consolidated financial statements for the year to 31 December 2002 were prepared for the first time in accordance with the International Financial Reporting Standards (IFRS) valid on that date, as issued by the International Accounting Standards Board (IASB), London, and interpreted by the International Financial Reporting Interpretation Committee (IFRIC).

The conditions laid down in the German Commercial Code (HGB), paragraph 292a, for exemption from the preparation of consolidated financial statements in accordance with German accounting and reporting law, were fulfilled as stipulated with additional explanatory notes. The consolidated financial statements and management report, which must be filed with the

Commercial Register and published in the *Bundesanzeiger (Federal Gazette)*, also comply with the European Union Directive on Consolidated Financial Statements (83/349/EEC) as interpreted by German Accounting Standard No. 1, "Exempting Consolidated Financial Statements in Accordance with §292a of the German Commercial Code", issued by the German Accounting Standards Committee.

Individual items in the balance sheet and the income statement were aggregated to clarify presentation. These items are disclosed and explained separately in the notes below. For the first time we used the cost of sales method for the income statement. The Group currency is the euro. All amounts disclosed in the financial statements represent thousand euros (T€), unless otherwise indicated.

(B) Accounting Policies

The financial statements for Koenig & Bauer AG and its domestic and foreign subsidiaries were prepared in compliance with IAS 27 (revised 2000) using uniform accounting policies. Discrepancies in the accounting policies of associates were not adjusted where the amount involved was insignificant.

Intangible Assets

Purchased intangible assets were disclosed at their purchase price as per IAS 38 if it was likely that economic benefits attributable to the use of the assets would flow to the enterprise and their cost could be measured reliably. Each asset was amortised on a straight-line basis over its estimated useful life.

Development costs for new or significantly improved products were capitalised at cost if, as stipulated in IAS 38, the technical feasibility, an intention to sell and the existence of a market could be demonstrated, the attributed expenditure measured reliably, adequate development and marketing resources were available and future economic benefits probable. Prior to 2002 development costs were recognised as an expense under IAS 38.41. The straight-line method was used to allocate the

depreciable amount of such products over their projected useful life. Adequate provision was made for uncertainties associated with future market trends. Annual impairment tests will be carried out for development projects recognised as assets but not yet completed.

Property, Plant and Equipment

Items of property, plant and equipment were measured at cost less depreciation based on the straight-line method and the use to which they are put. Manufacturing costs for self-constructed plant and equipment included an appropriate proportion of production overheads, material and labour costs. Under IAS 23 (revised 1993) borrowing costs were carried as an expense, not as part of the cost of an asset. Costs for maintenance and repairs were also recognised as an expense. No land or buildings were held as financial investments as defined in IAS 40.

Grants

Since government grants are classified by IAS as a reduction in the cost of assets, they were recognised as a reduced depreciation charge over the asset life.

Leases

Leases for which the KBA Group, as the lessee, assumed the basic risks and rewards incident to ownership were capitalised as finance leases under non-current assets. Leased property was measured at fair value or the lower present value of the minimum lease payments. Depreciation was calculated using the straight-line method for the shorter period (the term of the contract or the useful life of the leased property). Payment obligations arising from future lease payments were disclosed in other liabilities. Where the risks and rewards incident to ownership were not assumed, the lease was classified as an operating lease and payments carried as expenses.

Depreciation

The systematic depreciation of intangible Group assets, property, plant and equipment was based on the following useful lives:

	Years
Industrial property rights and similar rights	3 to 7
Goodwill	3 to 10
Negative goodwill	10
Product development costs	4 to 6
Buildings	5 to 40
Plant and machinery	3 to 15
Other facilities, factory and office equipment	2 to 12

In addition intangible assets, property, plant and equipment were, where applicable, tested for impairment loss on the balance sheet date as per IAS 36 and the recoverable amount defined as the higher of an asset's net selling price and its value in use. Where the recoverable amount was lower than the carrying amount the difference was disclosed as an impairment loss. If the reason for a write-down no longer applied, an adjustment in the allowance account was made, up to the amortised cost of acquisition or manufacture.

Financial Assets

These were measured at cost upon initial disclosure and subsequently classified in four categories under IAS 39 (68) (revised 2000): loans and receivables originated by the enterprise and not held for trading; investments held to maturity; financial assets available for sale; and financial assets held for trading. Loans originated by the enterprise and investments held to maturity were measured at their amortised cost or lower net recoverable amount. Available-for-sale financial assets were measured at fair value, with unrealised gains and losses recognised directly in equity, net of deferred taxes. No financial assets were held for trading.

Investments in unconsolidated affiliates (see Note (C)) were measured at their amortised cost. Investments in associates were measured using the equity method, based on the Parent's share of company equity.

Inventories

Inventories were carried at the cost of purchase or conversion, with the latter including individual items, their proportionate share of total overheads and depreciation based on a normal level of plant utilisation. Borrowing costs under IAS 23 (revised 1993) were not included. The cost of inventories that could not be measured on an item-by-item basis was calculated using the weighted average cost formula.

Inventories whose net realisable value on the balance sheet date was lower than cost, for example due to prolonged storage, damage or impaired marketability, were written down to the lower value. The net realisable value is the estimated sales revenue realisable in normal business minus the estimated cost of completion and the estimated costs that would be incurred to make the sale.

Receivables and Other Assets

Receivables and other assets relate to loans and receivables originated by the enterprise, with the exception of derivatives. Under IAS 39 (revised 2000) they were stated at their amortised cost or the lower recoverable amount. Value adjustments were made for all recognisable risks, based on item-by-item risk assessments and past experience. Bill holdings, non-interest-bearing debts and low-interest debts with maturities of more than one year were discounted.

Contract Revenue and Expenses

Contract revenue and expenses were disclosed using the percentage of completion method, as per IAS 11 (revised 1993). Under this method, contract revenue is matched with the contract costs incurred in reaching the stage of completion, resulting in the reporting of revenue, expenses and profit which can be attributed to the proportion of work completed. Contract revenue was carried under trade receivables after deducting payments received.

Marketable Securities, Cash and Cash Equivalents

These refer to available-for-sale financial instruments carried at market value on the balance sheet date, as specified in IAS 39 (revised 2000). This classification was also used for fixed-interest securities and shares, since we have no plans to hold these until final maturity. Unrealised gains or losses were recognised in equity, net of deferred taxes.

Pension Provisions

Pension provisions were measured using the projected unit credit method described in IAS 19 (revised 2000), an actuarial means of valuation that recognises the present and potential benefits known on the balance sheet date and includes a prudent estimate of anticipated increases in salaries and pensions. Actuarial gains and losses were recognised only where they exceeded a 'corridor' of plus or minus 10% of the accrued benefits, divided by employees' average remaining years of service.

As a rule, in accordance with national and regional regulations, we offer our employees defined-benefit pension plans.

Other Provisions

These included all other corporate risks and contingent liabilities to third parties, insofar as an outflow of resources was probable and could be reliably assessed. The amounts disclosed in other provisions represent the best estimate of the expenditure needed to settle current obligations on the balance sheet date. Long-term provisions were disclosed at their present value where the interest effect was substantial.

Liabilities

Financial liabilities, with the exception of liabilities arising from finance leases, were initially disclosed at cost of purchase. In future years all liabilities, with the exception of derivatives, will be measured at the amortised cost.

Derivatives

In accordance with IAS 39 (revised 2000) all instruments such as swaps and future currency contracts were carried at market value. Changes in market value were reported in net profit or loss where no hedge accounting was used.

Where **hedge accounting** was used, changes in market value were reported either in equity or in the income statement. With a **fair value hedge**, changes in the market value of a hedging instrument and the underlying transaction were reported as a profit or loss. With a **cash flow hedge**, the portion of the gain or loss in the hedging relationship that was determined to be an effective hedge was recognised directly in equity and the ineffective portion reported immediately in the income statement. Gains and losses were reported in the income statement as soon as the hedged transaction itself was recognised.

Derivatives in the form of marketable futures, currency and interest swaps were used to hedge against Group currency and interest risks. From 1 January 2002 onwards, where the conditions defined in IAS 39 (revised 2000) for an effective hedging relationship and its documentation were fulfilled, hedge accounting was used, more specifically cash-flow hedges. Futures contracts were the prime hedging instrument against foreign currency risks for projected or existing transactions. Changes in the market value of derivatives prior to 2002 were disclosed in the income statement because IAS 39 (revised 2000) states that the hedging relationship must be formally documented at inception. It cannot be documented retrospectively.

Deferred Taxes

Deferred tax assets and liabilities were recognised on temporary differences between IFRS and tax bases for Group enterprises, and in consolidation measures. Differences were calculated using the liability method specified in IAS 12 (revised 2000), and only tax-relevant temporary differences were taken into account. Deferred tax assets also included claims to future tax reductions arising from the anticipated use of existing tax loss

carryforwards, where this use was probable. Adequate provision was made against the likelihood that insufficient taxable income would be generated against which a deferred tax asset could be offset. The tax rates used to calculate deferred taxes were the national rates applicable or anticipated at the time of recovery. The effect of changes in tax rates on deferred taxes was reported when such changes came into force.

(C) Consolidated Companies and Consolidation Principles

Consolidated Companies

In addition to Koenig & Bauer AG, Würzburg, the consolidated financial statements include ten (previous year: 9) subsidiaries and 1 (2) associated enterprise. On 1 January 2002 Karat Digital Press GmbH, Radebeul, which had previously been consolidated using the equity method, was merged with the parent company following the acquisition of shares to make it a full subsidiary. Since Koenig & Bauer had already taken over all sales activities for Karat digital presses the increase in Group turnover was of minor significance. The effect of the acquisition on the Group's financial position at the balance sheet date could not be quantified because the company had been merged.

The financial statements for the consolidated companies were prepared using uniform accounting policies.

Seven (previous year: 6) subsidiaries were not included in the consolidated financial statements since they were of minor significance to the Group's financial position and performance. Of these, two companies were established during the business year.

A special fund, classified under IAS 27 (revised 2000) and SIC 12 as a special-purpose entity, was not included in the consolidated financial statements since it was also of minor significance to the Group's financial position and performance. Available-for-sale financial instruments were carried at market value as per IAS 39 (revised 2000).

A list of Koenig & Bauer's investment holdings was filed in the Commercial Register at the Municipal Court in Würzburg under number HBR 109.

Consolidation Principles

The capital consolidation of affiliates and the disclosure of business combinations were reported using the book-value method, offsetting the cost of acquiring shares in subsidiaries against the Parent's share of equity at the date of initial consolidation. The difference between purchase cost and the Parent's share of equity was allocated to the subsidiary's assets and liabilities where the difference resulted from undisclosed reserves or liabilities. Any excess of cost over the amounts allocated was recognised as goodwill and amortised over the estimated useful life on a straight-line basis. Negative goodwill was deducted as a separate item in intangible assets and written back over the useful life, which was calculated from the weighted average depreciation period of the intangible assets, property, plant and equipment of the consolidated company. Goodwill generated prior to 1 January 1995 remained netted against reserves as permitted by IAS 22 (revised 1998).

Associates were consolidated using the equity method, following the consolidation principles stated above.

Receivables, liabilities, income and expenses relating to transactions among consolidated companies were eliminated, as were the profits from such transactions. With the exception of goodwill, temporary tax deferrals arising from the consolidation were recognised as deferred taxes under IAS 12 (revised 2000).

(D) Foreign Currency Translation

The financial statements of consolidated companies prepared in a foreign currency were translated using their functional currency and the foreign entity method specified in IAS 21 (revised 1993).

Since foreign subsidiaries are financially, economically and organisationally autonomous their functional currency is the same as their local currency. Their assets and liabilities were therefore translated in the consolidated financial statements at the closing rate, equity items at the historic rate and income and expenses at the average

exchange rate for the year. The resulting exchange differences were disclosed in equity.

Goodwill arising from the acquisition of subsidiaries, and adjustments in the carrying amounts of assets and liabilities to fair value, were translated at the closing rate on the date of acquisition.

Monetary items in foreign currency were also translated at the closing rate in the financial statements for the individual companies. The ensuing currency gains and losses were recognised directly as income or expense.

(E) Notes to the Adoption of IFRS

The KBA Group financial statements were prepared as though IFRS and the SIC interpretations had always applied. The adjustments resulting from the conversion to

IFRS from German accounting regulations (HGB) were carried in equity. The basic effects on the Group balance sheet are shown on the right.

Assets			
	31.12.2001		Change
in T€	IFRS	HGB	
Intangible assets	23,906	24,846	– 940
Property, plant and equipment	233,633	199,632	34,001
Financial assets	14,611	14,619	– 8
Non-current assets	272,150	239,097	33,053
Inventories	498,457	166,353	332,104
Trade receivables	345,080	362,951	– 17,871
Other receivables and assets	62,461	60,653	1,808
Securities	31,381	28,627	2,754
Cash and cash equivalents	70,491	70,478	13
Current assets	1,007,870	689,062	318,808
Deferred tax assets	54,086	3,790	50,296
	1,334,106	931,949	402,157
Equity and liabilities			
	31.12.2001		Change
in T€	IFRS	HGB	
Issued capital/capital reserve	121,548	121,548	0
Revenue reserves	291,430	202,772	88,658
Net profit	39,973	74,900	– 34,927
Equity	452,951	399,220	53,731
Minority interest	189	163	26
Special items with equity portion	0	9,166	– 9,166
Pension provisions	79,066	58,975	20,091
Tax provisions and other provisions	185,964	216,939	– 30,975
Provisions	265,030	275,914	– 10,884
Bank borrowings	109,504	109,504	0
Payments received on account	301,292	0	301,292
Trade payables	88,662	88,892	– 230
Other liabilities	58,045	49,090	8,955
Liabilities	557,503	247,486	310,017
Deferred tax liabilities	58,433	0	58,433
	1,334,106	931,949	402,157

Non-current Assets

Under IFRS, the systematic depreciation of non-current assets is calculated over their useful economic lives on a straight-line, pro-rata basis, whereas German regulations favour the declining-balance method and simplification rules, with the useful life determined by tax regulations.

The application of IAS 17 (revised 1997) led in some cases to a reclassification of operating leases as finance leases and thus to the recognition of their current market value in property, plant and equipment.

According to German accounting regulations, investment subsidies must be disclosed as special items in equity and liabilities. Under IFRS they reduce the cost price.

IFRS stipulates that, under certain conditions, internally generated intangible assets, and more specifically development costs, must be capitalised. This form of disclosure was not adopted for the KBA Group until 2002.

Inventories

IFRS writes down inventories to the lower net selling price. The prudence principle advocated by German accounting regulations, however, recognises a higher volume of provisions.

IFRS favours the percentage of completion method for measuring contract revenue and expenses. This is not permitted under German accounting laws.

IFRS does not allow payments received to be deducted from inventories.

Other Marketable Securities and Liabilities

German accounting law states that financial instruments (securities, receivables and liabilities, derivatives) are to be carried at cost (historical cost method) and at the most prudent value (impairment method in conjunction with the

highest and lowest value method). Unrealised gains must not be collected, but provision must be made for anticipated losses related to incomplete contracts. IFRS, on the other hand, stipulates that financial instruments, depending on how they are classified, must be carried at market value, at amortised cost or at the recoverable amount, and derivatives marked to market. Unrealised gains and losses must be disclosed in accordance with IAS 39 (revised 2000). The conditions for hedge accounting were not fulfilled (see Note (B)) until 1 January 2002, so prior changes in the market value of derivatives were recognised as income or expense.

Provisions

Pension provisions were reported using the projected unit credit method as per IFRS. This differs from measurement under German accounting regulations in that it factors in projected salary, career and pension trends.

In contrast to German accounting regulations no provisions could be made for expenses.

With IFRS, provisions are measured at the current best estimate, whereas German accounting regulations specify the prudence principle, which leads to higher provisions.

Deferred Taxes

According to IFRS all deferred tax assets and liabilities must be disclosed and deferred tax assets created for tax loss carryforwards. In the KBA Group, deferred tax liabilities were recognised in accordance with German accounting regulations and deferred tax assets only created on consolidated entries. IFRS allows deferred tax liabilities to be offset against deferred tax assets only if the conditions stipulated in IAS 12 (revised 2000) are fulfilled.

Equity

The impact of the differences between German and IFRS valuation methods on equity at 31 December 2001, and on the financial statements for 2001, is shown below.

in T€	Equity 31.12.2001	Net income 2001
HGB	399,220	74,900
Depreciation on non-current assets	41,394	4,677
Finance leases	– 121	– 44
Inventory valuation	16,894	3,089
Profit recognition by percentage of completion method	12,402	– 7,287
Measurement of monetary items on balance sheet date	4,617	– 587
Market value measurement of financial instruments	– 1,618	– 5,017
Elimination of 6b reserve	101	– 329
Reclassification of pension provisions	– 13,538	– 6,634
Derecognition of expense provisions	764	– 1,571
Creation of deferred taxes	– 5,991	– 21,434
Consolidation/other	– 1,173	210
IFRS	452,951	39,973

(F) Non-current Asset Movement Schedule

							Cost
in T€	01.01.2002	Group additions	Additions	Translation differences	Reclassifications	Disposals	31.12.2002
Intangible assets							
Industrial property rights and similar rights	22,145	7,541	3,914	176	34	425	33,385
Goodwill	11,883	10,100	364	0	0	0	22,347
Negative goodwill from capital consolidation	- 328	0	0	0	0	0	- 328
Product development costs	0	10,770	1,612	0	0	0	12,382
	<u>33,700</u>	<u>28,411</u>	<u>5,890</u>	<u>176</u>	<u>34</u>	<u>425</u>	<u>67,786</u>
Property, plant and equipment							
Land and buildings	163,448	5,695	4,067	- 1,083	1,933	963	173,097
Plant and machinery	194,139	2,579	14,763	- 1,917	2,138	3,714	207,988
Other facilities, factory and office equipment	85,689	2,037	13,316	- 458	196	9,977	90,803
Advanced payments made and assets under construction	3,841	0	11,161	- 21	- 4,301	74	10,606
	<u>447,117</u>	<u>10,311</u>	<u>43,307</u>	<u>- 3,479</u>	<u>- 34</u>	<u>14,728</u>	<u>482,494</u>
Financial assets							
Investments in affiliates	3,270	0	431	- 38	0	0	3,663
Investments in associates	1,038	0	78	19	0	148	987
Investments in other companies	4,328	0	0	- 2	0	4,288	38
Investment securities	2,535	0	0	0	0	12	2,523
Other loans	372	0	34	0	0	27	379
Claims from life insurance	8,144	0	429	0	0	0	8,573
	<u>19,687</u>	<u>0</u>	<u>972</u>	<u>- 21</u>	<u>0</u>	<u>4,475</u>	<u>16,163</u>
	<u>500,504</u>	<u>38,722</u>	<u>50,169</u>	<u>- 3,324</u>	<u>0</u>	<u>19,628</u>	<u>566,443</u>

						Depreciation	Residual value	
01.01.2002	Group additions	Annual depreciation	Write-ups	Translation differences	Disposals	31.12.2002	01.01.2002	31.12.2002
9,139	4,329	5,800	0	25	424	18,869	13,006	14,516
693	0	4,553	0	0	0	5,246	11,190	17,101
- 38	0	- 33	0	0	0	- 71	- 290	- 257
0	7,675	670	0	0	0	8,345	0	4,037
9,794	12,004	10,990	0	25	424	32,389	23,906	35,397
46,566	373	4,433	0	- 495	683	50,194	116,882	122,903
119,504	256	15,645	0	- 1,410	3,082	130,913	74,635	77,075
47,414	926	13,958	0	- 330	8,199	53,769	38,275	37,034
0	0	0	0	0	0	0	3,841	10,606
213,484	1,555	34,036	0	- 2,235	11,964	234,876	233,633	247,618
382	0	0	0	0	0	382	2,888	3,281
53	0	0	65	- 52	24	42	985	945
4,290	0	0	0	- 2	4,288	0	38	38
320	0	0	- 45	0	0	275	2,215	2,248
31	0	0	0	0	0	31	341	348
0	0	0	0	0	0	0	8,144	8,573
5,076	0	0	20	- 54	4,312	730	14,611	15,433
228,354	13,559	45,026	20	- 2,264	16,700	267,995	272,150	298,448

(G) Explanatory Notes to the Balance Sheet

(1) Non-current Assets

Depreciation on intangible assets and on property, plant and equipment was carried in costs of conversion, selling costs, general administrative costs and other operating expenses, the amortisation of goodwill and income from the reversal of negative goodwill were stated in the income statement as administrative costs. There were no write-ups or write-downs as per IAS 36.

Changes in individual items of non-current assets were disclosed in the non-current asset movement schedule on pages 58 and 59.

Non-current assets include T€358 (previous year: T€0) for rights arising from finance leases, T€5,463 (T€103) for plant and machinery and T€699 (T€1,070) for other facilities, factory and office equipment. Further details of finance leases are given in Note (10) under sundry other liabilities.

No intangible assets or items of property, plant or equipment were pledged against liabilities and there were no other restrictions on the right of free disposal.

Government grants for promoting investment reduced the carrying amounts for intangible assets by T€559 and for property, plant and equipment by T€11,583 (2001: T€156 and T€8,644 respectively).

Intangible Assets

Additions to industrial rights and similar rights related to purchased software and licences.

Goodwill at 1 January 2002 arising from the acquisition of KBA-GIORI S.A., Lausanne, and Holland Graphic Occasions B.V., Wieringerwerf, in 2001 was amortised over 10 years. Goodwill to the value of T€10,100 arising from the acquisition of Karat Digital Press GmbH, Radebeul, by Koenig & Bauer AG was amortised over three years on the straight-line basis.

Negative goodwill resulting from the purchase of shares in KBA-Mödling AG, Mödling, in previous years was carried as income over a period of 10 years as specified in IAS 22 (revised 1998).

Development costs for new digital and web offset products were capitalised for the first time in 2002. Product development costs generated in previous years were recognised in full as an expense (*see Note (B)*).

Property, Plant and Equipment

Additions to property, plant and equipment predominantly related to new and replacement plant and machinery as well as other plant.

Financial Assets

Major interests held by Koenig & Bauer AG are shown in the table below.

Company / Seat	Capital share in %	Equity in T€	Net profit/loss in T€
Consolidated affiliates			
KBA-Mödling AG, Mödling, Austria	>99.9	20,823	530
KBA North America Inc., Wilmington, Delaware, USA	100.0	31,513	273
KBA-Berlin GmbH, Berlin, Germany	100.0	3,100	2,851 ¹⁾
KBA-Le Mont-sur-Lausanne SA, Lausanne, Switzerland ⁵⁾	100.0	9,716	5,387
KBA-GIORI S.A., Lausanne, Switzerland	100.0	27,900	17,167
Holland Graphic Occasions B.V., Wieringerwerf, Netherlands	100.0	- 360 ²⁾	- 980
Non-consolidated affiliates			
KBA (UK) Ltd., Watford, UK	100.0	1,488	0
KBA-France SAS, Tremblay-en-France, France	100.0	707	1
KBA-Italia S.p.A., Milan, Italy	100.0	1,277 ³⁾	80 ³⁾
KBA Koenig & Bauer (Asia Pacific) Sdn. Bhd., Kuala Lumpur, Malaysia	70.0	- 102 ²⁾	- 251
KBA (HK) Company Ltd., Hong Kong, China	51.0	911	327
KBA Australasia Pty. Ltd., Lane Cove, Australia	100.0	46	- 224
KBA NORDIC A/S, Herlev, Denmark	50.2	219	- 32
Associates (equity method)			
Print Assist AG, Hori, Switzerland ⁵⁾	33.3	2,550	179
Interests			
KBA Leasing GmbH, Bad Homburg, Germany	24.9	- 511 ²⁾	- 492 ⁴⁾

1) A profit and loss transfer agreement with KBA-Berlin exists since 8.4./9.11.1971

2) Deficit not covered by equity

3) Figures for 2001

4) Preliminary figures

5) Indirect holding via KBA-Le Mont-sur-Lausanne SA

Unless otherwise indicated, the figures for equity and net profit or loss are those disclosed in the single-entity statements audited under the pertinent national accounting laws. Statements in foreign currencies show equity and profit or loss translated at the balance sheet date.

Two new sales subsidiaries were established in 2002: KBA Australasia Pty. Ltd. in Sydney, Australia, and KBA NORDIC A/S, in Herlev, Denmark, which has branches in Finland and Sweden. Our two US subsidiaries, KBA North America Inc., Sheetfed Division in Williston, Vermont, and KBA North America, Inc., Web Press Division in York, Pennsylvania, were combined in a holding, KBA North

America Inc., in Wilmington, Delaware. The liquidation of Publishers Equipment Corp. (PEC), Dallas, Texas, resulted in a T€4,288 disposal in other interests.

In 2002 the 50:50 joint-venture agreement between Koenig & Bauer AG and Scitex Corp. Ltd., Israel, for the purpose of developing a digital offset press, was terminated. Following the acquisition by Koenig & Bauer AG of the remaining 76.1% interest in the former joint-venture enterprise, Karat Digital Press GmbH, Radebeul, for T€78 the company was absorbed by the Parent with effect from 1 January 2002. Karat Digital Press GmbH had previously been consolidated as an associate under IAS 28 (revised 2000), using the equity method.

(2) Inventories

By improving inventory management we substantially reduced our stocks of raw materials, consumable and supplies. The T€71,809 reduction in work in progress was the result of preparatory work carried out the year before for contracts shipped in the first half of 2002.

The carrying amount of inventories balanced at net realisable value was T€118,129 (2001: T€64,707).

in T€	31.12.2002	31.12.2001
Raw materials, consumables and supplies	52,465	68,626
Work in progress	312,119	383,928
Finished goods and products	1,717	3,886
Payments on account	22,333	42,017
- to associates	(0)	(5,546)
	<u>388,634</u>	<u>498,457</u>

(3) Receivables and Other Assets

in T€	31.12.2002				31.12.2001			
		up to 1 year	Term to maturity 1 to 5 years	more than 5 years		up to 1 year	Term to maturity 1 to 5 years	more than 5 years
Trade receivables	384,391	315,336	67,940	1,115	345,080	270,818	73,669	593
Other receivables								
- from affiliates	25,865	25,865	0	0	26,248	26,248	0	0
- from associates	138	138	0	0	2,990	2,990	0	0
- from companies in which interests are held	2,850	2,850	0	0	4,522	4,522	0	0
Other assets								
- tax receivables	4,380	4,380	0	0	10,859	10,859	0	0
- receivables from employees	4,636	4,615	21	0	3,159	3,130	24	5
- sundry other assets	34,674	25,978	7,871	825	14,683	11,015	3,256	412
	72,543	63,826	7,892	825	62,461	58,764	3,280	417
	<u>456,934</u>	<u>379,162</u>	<u>75,832</u>	<u>1,940</u>	<u>407,541</u>	<u>329,582</u>	<u>76,949</u>	<u>1,010</u>

Receivables and other assets were measured at their amortised cost. The amounts recoverable in the normal course of business were the carrying amounts.

Adopting the percentage of completion method resulted in T€54,165 (2001: T€79,205) being carried in **trade receivables**. The T€39,311 increase partly reflects a mounting demand for customer financing.

Sundry other assets contain prepayments of T€1,720 (2001: T€1,902), other advance payments of T€3,190 (T€2,552) and a no-claims bonus of T€2,812 for accident

insurance from the previous year. Assets from derivatives are detailed in Note (11).

Interest, exchange and credit risks at the balance sheet date related to customer financing and loans to employees and agents. Interest risks are summarised in the table on the next page. Currency risks related to the conclusion of delivery contracts in foreign currencies, usually US dollars. These were hedged using derivatives (*see Note (11)*). Credit risks were contained by creating adequate provisions. Provisions made in 2002 totalled T€6,890 (2001: T€5,740).

in T€	31.12.2002			31.12.2001		
	Carrying amount	Interest rate	Term to maturity in years	Carrying amount	Interest rate	Term to maturity in years
Trade receivables	384,391	up to 9.4%	up to 9	345,080	up to 9.9%	up to 10
Receivables from affiliates	25,865	up to 5.1%	up to 1	26,248	up to 4.5%	up to 1
Receivables from employees	4,636	up to 6%	up to 6	3,159	up to 6%	up to 7
Other loans and assets	34,674	up to 6%	up to 11	14,683	up to 6%	up to 12
	<u>449,566</u>			<u>389,170</u>		

(4) Securities

These mainly refer to fixed-interest securities owned by the Parent and shares in a special fund combining stocks and bonds classified under IAS 39 (revised 2000) as available for sale financial instruments. T€5,228 (previous year: T€3,979) of this special fund was pledged to employees in order to hedge phased retirement credits in accordance with the law on flexitime.

Fixed-interest securities were valued at T€6,836 (2001: T€7,083).

The sale of shares in the **special fund** resulted in a profit of T€1,936 (2001: T€4,758) being carried in the income statement as other operating income. Previously this had been disclosed in equity. The balanced market value was T€6,267 (T€24,298).

(5) Cash and Cash Equivalents

in T€	31.12.2002	31.12.2001
Cheques, cash in hand,		
balance at Bundesbank	3,689	684
Balances with banks	<u>40,356</u>	<u>69,807</u>
	<u>44,045</u>	<u>70,491</u>

(6) Deferred Taxes

Deferred tax assets and liabilities comprised the following:

in T€	Deferred tax assets		Deferred tax liabilities	
	31.12.2002	31.12.2001	31.12.2002	31.12.2001
Assets				
Non-current assets	1,383	1,014	21,904	18,322
Inventories	4,952	13,130	1,874	7,396
Receivables and other assets	6,287	7,490	6,811	1,512
Securities, cash and cash equivalents	0	0	141	1,050
	<u>12,622</u>	<u>21,634</u>	<u>30,730</u>	<u>28,280</u>
Equity and liabilities				
Equity	0	0	2,062	4,091
Provisions	19,820	15,049	7,773	7,554
Liabilities	3,345	7,433	8,514	18,572
	<u>23,165</u>	<u>22,482</u>	<u>18,349</u>	<u>30,217</u>
Tax loss carryforwards	4,133	10,084	0	0
Other	- 521	- 114	- 404	- 64
	<u>39,399</u>	<u>54,086</u>	<u>48,675</u>	<u>58,433</u>

Deferred taxes on equity refer to deferred taxes on the translation differences arising from consolidation procedures.

Other deferred tax assets and liabilities include offsetting as per IAS 12 (revised 2000) and provisions.

Tax loss carryforwards relating to Karat Digital Press GmbH resulted in an increase in deferred tax assets of T€8,012, which was almost completely consumed in the course of the year.

(7) Equity

Changes in shareholders' equity are described in a separate schedule on page 48.

Issued Capital

At 31 December 2002 Koenig & Bauer AG had a total share issue of 16,071,396 (2001: 16,000,000) no-par shares with a par value of €2.60. The 71,396 increase over the previous year represents the first issue of employee shares, using part of the T€15,600 capital approved by the AGM on 22 November 2001. The remaining T€15,414 was approved until 22 November 2006. Until 26 December 2003 the company is authorised to buy back shares up to a maximum of one tenth of the issued capital of T€41,600.

All bearer shares issued were paid up in full.

Capital Reserve

This included the extra charge from the issue of shares. Our capital reserve rose by T€1,557 compared to the previous year, due to the issue of employee shares.

Revenue Reserves

These encompassed the accumulated net profits posted in previous years by consolidated companies (unless dividends were paid) and adjustments arising from the adoption of IFRS. Goodwill and negative goodwill acquired from capital consolidation prior to 1 January 1995 increased revenue reserves by T€429.

Revenue reserves also included translation differences relating to the financial statements of foreign entities and to changes in the market value of financial instruments

after taxes, where these were not recognised as income or expense. The disclosure of original financial instruments reduced revenue reserves by T€17 (T€352), realised gains reduced them by a further T€1,936 (T€4,758). The use of hedge accounting increased revenue reserves by T€11,087. During completion of the underlying transactions T€3,828 was recognised as income.

Deferred taxes were carried in equity, reducing revenue reserves by T€3,566 (2001: T€264 increase).

(8) Pension Provisions

Pension provisions related to obligations to active and retired employees of Koenig & Bauer AG, and their survivors, from accrued and current benefits. Company pensions are based on a **defined-benefit plan**, with the company meeting all commitments to active and retired employees. Pensions are largely financed through additions to provisions and through a funded benefit system. If fund assets exceed obligations from pension commitments, the excess is capitalised in other assets as per IAS 19 (revised 2000). If fund assets do not cover obligations, net liabilities are carried in pensions provisions.

The extent of the pension obligation (defined-benefit obligation) was calculated using actuarial methods which necessarily entailed making estimates.

Calculations were based on a discount rate of 5.8% (2001: 6%), or 6.5% (7%) in the USA, a salary increase of 3.5% (2.9%) and a median fluctuation rate of 3.7% (3.7%). Pension adjustments were calculated at 2% (1.8%).

Pension provisions constituted the following:

in T€	31.12.2002	31.12.2001
Present value of non-funded obligations	83,453	80,529
Present value of funded obligations	13,634	11,282
Current market value of plan assets	- 11,662	- 14,118
Current market value of obligations (offset)	85,425	77,693
Unrecognised actuarial gains/losses	- 1,043	2,688
Unrecognised changes due to implementation/change of plan	- 1,743	- 1,988
Currency gains/losses	- 625	- 150
Balance sheet amount at 31.12.	82,014	78,243
- pension provisions	82,509	79,066
- assets	495	823

Net liability recognised in the balance sheet changed as follows:

in T€		31.12.2002		31.12.2001
Net liability recognised in the balance sheet at 01.01.		78,243		63,015
Annual expense		7,492		18,879
- current service cost	(2,750)		(1,903)	
- interest cost	(5,544)		(4,844)	
- expected return on assets	(- 1,002)		(- 1,228)	
- recognised actuarial gain/loss	(- 71)		(4,189)	
- change due to implementation/change of plan	(271)		(9,171)	
Benefits paid		- 3,809		- 3,688
Changes in consolidated companies		0		86
Translation changes		88		- 49
Net liability recognised in the balance sheet at 31.12.		82,014		78,243

The inclusion of our Radebeul facility in the Koenig & Bauer company pension plan resulted in a substantial expense in 2001 (change due to implementation of plan).

The actual return on plan assets was -T€1,153 (previous year -T€181).

All pension components were disclosed in the income statement according to their function, with the exception of the interest portion, which was included in interest expense.

Expenses for **defined contribution plans** totalled T€3,047 (2001 T€1,392).

(9) Other provisions

in T€	Status on 01.01.2002	Group addition	Consump- tion	Reversal of provisions	Allocation	Translation difference	Status on 31.12.2002
Tax provisions	2,136	0	398	660	2,458	- 40	3,496
Other provisions							
- for employees	34,262	82	16,256	109	19,982	- 149	37,812
- for sales	65,166	2,457	14,669	10,671	19,913	- 938	61,258
- for sundry other purposes	84,400	6,319	74,737	1,894	67,454	- 214	81,328
	183,828	8,858	105,662	12,674	107,349	- 1,301	180,398
	185,964	8,858	106,060	13,334	109,807	- 1,341	183,894

Tax provisions primarily related to income taxes for the business year.

Provisions for employees included holiday and flexitime credits, long-service expenses, credits for pre-retirement part-time plans and performance bonuses. Sales expenses

covered provisions for process risks, warranty and commission obligations. Provisions for sundry other purposes primarily related to outstanding invoices.

The maturity schedule for provisions is given below.

in T€	31.12.2002				31.12.2001			
		up to 1 year	Term to maturity 1 to 5 years	more than 5 years		up to 1 year	Term to maturity 1 to 5 years	more than 5 years
Tax provisions	3,496	3,496	0	0	2,136	1,823	313	0
Other provisions								
- for employees	37,812	18,814	14,588	4,410	34,262	20,043	11,667	2,552
- for sales	61,258	48,299	12,959	0	65,166	48,369	16,797	0
- for sundry other purposes	81,328	69,330	11,998	0	84,400	73,341	11,059	0
	180,398	136,443	39,545	4,410	183,828	141,753	39,523	2,552
	183,894	139,939	39,545	4,410	185,964	143,576	39,836	2,552

(10) Liabilities

in T€	31.12.2002				31.12.2001			
		up to 1 year	Term to maturity 1 to 5 years	more than 5 years		up to 1 year	Term to maturity 1 to 5 years	more than 5 years
Bank borrowings	132,876	89,506	26,188	17,182	109,504	53,837	36,083	19,584
Payments received								
on account	197,463	197,463	0	0	301,292	277,595	23,697	0
Trade payables	65,288	61,620	3,668	0	88,662	88,078	584	0
Other liabilities								
- from the issue of promissory notes	0	0	0	0	794	794	0	0
- to affiliates	1,492	1,492	0	0	235	235	0	0
- from taxes	6,674	6,674	0	0	11,623	11,623	0	0
- from social security and similar obligations	7,514	7,514	0	0	7,985	7,985	0	0
- from sundry other obligations	38,575	27,652	10,604	319	37,408	30,841	6,567	0
	54,255	43,332	10,604	319	58,045	51,478	6,567	0
	449,882	391,921	40,460	17,501	557,503	470,988	66,931	19,584

The carrying amounts of liabilities largely corresponded to their market value.

Lines of credit not drawn down by the KBA Group totalled T€179,918 (2001: T€145,833). Details of **bank borrowings** relating to existing interest risks are summarised below.

in T€	Term to maturity in years	31.12.2002		31.12.2001	
		Carrying amount	Interest rate	Carrying amount	Interest rate
Loans	up to 1	72,095	up to 5.9%	40,573	up to 6.8%
	up to 5	26,188	up to 6.2%	36,083	up to 6.2%
	up to 10	9,513	up to 5.7%	11,915	up to 5.7%
	up to 12	7,669	up to 4.9%	7,669	up to 4.9%
Rolling loans	up to 1	9,545	up to 6.8%	11,338	up to 7.2%
Bank overdrafts	up to 1	7,866	up to 4.5%	1,926	up to 6.5%
		132,876		109,504	

Bank borrowings were secured by mortgages and other rights of lien to the value of T€11,231 (2001: T€13,055), and by the assignment of trade receivables totalling T€4,860 (T€4,869).

Payments received included contract revenues of T€108,677 (2001: T€119,579).

Sundry other liabilities included liabilities from finance leases to the sum of T€6,585 (2001: T€1,263). Sale and leaseback transactions based on customer finance models were concluded for the first time, with liabilities offset

against accounts receivable to the same amount. Turnover was carried upon delivery of the machinery. The present value of future payments for finance leases was broken down as follows:

in T€	31.12.2002				31.12.2001			
		up to 1 year	Term to maturity 1 to 5 years	more than 5 years		up to 1 year	Term to maturity 1 to 5 years	more than 5 years
Minimum lease payments	7,830	1,796	5,789	245	1,435	495	940	0
Interest portion	- 1,245	- 431	- 806	- 8	- 172	- 84	- 88	0
Present value of finance lease	6,585	1,365	4,983	237	1,263	411	852	0

The derivative items included in liabilities for sundry other purposes are explained more fully in Note (11).

(11) Derivatives

The KBA Group is exposed to numerous risks arising from its global activities.

Currency risk is the risk that the value of business transactions conducted in other currencies, particularly US dollars, will fluctuate due to changes in foreign exchange rates.

Interest rate risk is the risk that the value of variable-interest monetary investments or borrowings will fluctuate due to changes in market interest rates.

Credit risk is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss.

These risks are contained by a risk management system at group level. The principles laid down for the KBA Group ensure that risk is assessed and documented in accordance with systematic and uniform procedures. A regular

reporting schedule promotes the efficacy of the risk management system. Further information can be found on pages 22 to 24.

Risks were hedged using standard market instruments such as future exchange transactions in tandem with interest and currency swaps.

In 2001 a currency swap with a maturity of 5 years was concluded to hedge current, fixed-term business transactions concluded in US dollars. The nominal volume at the balance sheet date 2002 was T€45,815 (2001: T€68,027). In addition forward contracts with a maturity of up to 3 years (2001: 3 years) were used to hedge the calculation rate of additional foreign currency trade contracts. The currencies hedged were primarily US dollars, Swiss francs and British pounds.

The nominal volumes underlying derivatives, and their market values, are listed below.

in T€	Nominal volume		Market value	Nominal volume		Market value
	Total	Term to maturity more than 1 year		Total	Term to maturity more than 1 year	
	31.12.2002	31.12.2002		31.12.2001	31.12.2001	
Forward contracts	153,493	31,475	8,522	178,213	41,083	- 1,563
Currency swaps	51,488	40,034	2,953	73,593	59,988	- 4,434
Interest swaps	30,686	30,686	- 1,695	30,678	30,678	- 1,852
	235,667	102,195	9,780	282,484	131,749	- 7,849

The **nominal volume** of derivatives signifies a calculated reference amount from which payments are deducted. The risk therefore lies not in the nominal volume but in changes in the related exchange and interest rates.

Market value corresponds to the gains and losses derived from a fictitious offsetting of derivatives on the balance sheet date calculated using standardised measurement procedures.

In the balance sheet the market values were carried as T€17,740 (2001: T€901) in other assets and T€7,960 (T€8,750) in other liabilities. After 1 January 2002 the effective portion of a cash flow hedging relationship was offset against equity as per IAS 39 (revised 2002) and only carried in the income statement when the underlying transaction was completed.

(12) Other Financial Commitments and Contingent Liabilities

Other financial commitments								
in T€	31.12.2002				31.12.2001			
		up to 1 year	Term to maturity 1 to 5 years	more than 5 years		up to 1 year	Term to maturity 1 to 5 years	more than 5 years
Commitments from:								
operating leases	8,060	3,445	4,615	0	7,794	3,430	4,364	0
leasing and service contracts	5,646	1,642	4,004	0	8,627	3,879	4,748	0
delivery agreements	10,271	10,271	0	0	28,510	28,510	0	0
investment plans	8,674	8,396	278	0	11,112	11,112	0	0
sundry other activities	971	156	243	572	3,366	507	2,275	584
	33,622	23,910	9,140	572	59,409	47,438	11,387	584

Operating leases were mainly negotiated for IT equipment and our vehicle fleet. Leasing payments of T€4,086 (2001: T€3,579) were carried in the income statement. Commitments from operating leases were stated at the minimum lease payments.

Investment plans included commitments to invest in intangible assets to the value of T€209 (previous year:

T€898) and in property, plant and equipment to the value of T€8,465 (T€10,214).

Sundry other commitments were carried at their nominal amount and included outstanding ground rent and deposits.

Contingent Liabilities

These comprised contingencies totalling T€139,643 (2001: T€142,452) from warranty agreements, and a bill commitment of T€9,043 (T€6,025).

Contingencies from warranty agreements primarily related to repurchase guarantees to lessors and banks. The

guaranteed repurchase price decreased over the term of the repurchase obligation.

No provisions were created for the contingent liabilities stated. Where existing risks were not classified as minor they were recognised in the balance sheet.

(H) Explanatory Notes to the Income Statement

(13) Revenue

Revenue was recognised in accordance with IAS 18 (revised 1993) and comprised revenue from sales and from the rendering of services relating to web presses, special presses and sheetfed offset presses. Price reductions, rebates, bonuses and bulk discounts granted to customers were deducted from revenue.

Contract revenue and expenses for big newspaper press lines were calculated using the percentage of completion method specified in IAS 11 (revised 1993). Contract revenue totalled T€254,670 (previous year: T€343,690), accumulated revenue for contracts not completed by the balance sheet date came to T€427,312 (T€546,076).

Further details can be found in Segment Information, Note (J).

(14) Expenses by Function

Costs of Conversion

Costs of conversion included the purchase and manufacturing costs of products sold. In addition to directly attributable material and prime costs these incorporated overheads, depreciation on production plant and inventory adjustments.

Costs of conversion also contained T€49 in subsidies (2001: T€223) for apprentice training, job promotion and project advancement.

Selling and Administrative Expenses

The increase in selling and administrative expenses was largely due to a change in the number of consolidated companies in 2001. The new additions did not feature in the income statement until after their acquisition in mid-year. The figures for 2002, however, include income and expenses for the entire 12 months. As a result, goodwill amortisation carried in administrative expenses rose from T€693 to T€4,553.

Higher costs for winning and processing smaller contracts in more remote regions, and higher personnel expenses due to negotiated pay rises, could not be passed on to customers.

(15) Expenses by Nature

In order to maintain transparency in key items during conversion to the classification of expenses by function, basic expenses are summarised below according to their nature.

Material costs		
in T€	2002	2001
Cost of raw materials, consumables, supplies and purchased goods	589,083	584,367
Cost of purchased services	121,345	136,834
	<u>710,428</u>	<u>721,201</u>

The lower level of plant utilisation at our web press facilities reduced the volume of purchased services by T€15,489.

Personnel costs (classified by nature)

in T€	2002	2001
Wages and salaries	312,411	306,856
Social security and other benefits	60,635	59,135
Pensions	5,693	14,860
	<u>378,739</u>	<u>380,851</u>
Average payroll		
	2002	2001
Wage-earning industrial staff	4,309	4,315
Salaried office staff	2,766	2,663
Apprentices/students	464	446
	<u>7,539</u>	<u>7,424</u>

The inclusion of our Radebeul facility in the Koenig & Bauer pension plan generated a one-off pension expense in 2001 of T€8,826.

(16) Other Operating Income and Expenses

in T€	2002	2001
Other operating income		
Gains from the disposal of non-current assets	544	464
Foreign currency gains	1,626	1,355
Currency measurement	9,718	0
Reversal of write-downs and provisions	17,288	12,693
Income from the disposal of marketable securities	1,378	4,791
Sundry other operating income	10,640	4,116
	<u>41,194</u>	<u>23,419</u>
Other operating expenses		
Research and development costs	47,796	36,714
Losses from the disposal of non-current assets	799	553
Currency losses	451	519
Currency measurement	9,327	9,235
Creation of write-downs and provisions	6,890	8,112
Sundry other operating expenses	14,969	8,722
	<u>80,232</u>	<u>63,855</u>
Other operating income and expenses	<u>- 39,038</u>	<u>- 40,436</u>

Other operating income included insurance and compensation claims and other refunds. Government subsidies provided under the German Investment Subsidy Law of 1999 amounted to T€2,055 (2001: T€1,417) and subsidies for job promotion T€1,498 (T€1,308).

Research and development costs encompassed costs for original and planned investigation undertaken with the prospect of gaining new scientific or technical knowledge and understanding, and these were recognised in full in the income statement together with development costs not recognised by IAS 38. In addition the amortisation and disposal of capitalised development projects were recognised in the research and development costs.

Government research grants for expenses already incurred were recognised at the time of approval, reducing research and development costs by T€668 (2001: T€780). One condition for the disbursement of funds is that a complete record must be kept of all the costs incurred, and this record was submitted upon completion of the relevant project.

Sundry other operating expenses included the loss of receivables outstanding and the payment of compensation and warranty claims.

(17) Financial Result

in T€	2002	2001
Investment income		
Income from investments in affiliates	0	58
Income from investments in associates	3	56
	<u>3</u>	<u>114</u>
Interest income/expense		
Write-downs on marketable securities	- 275	0
Income from other securities and non-current loans	748	176
Other interest and similar income	12,755	14,172
- from affiliated companies	(150)	(97)
Other interest and similar expense	- 16,604	- 10,847
	<u>- 3,376</u>	<u>3,501</u>
Financial result	<u>- 3,373</u>	<u>3,615</u>

(18) Income Taxes

Tax expense mainly comprised the following:

in T€	2002	2001
Actual tax expense	4,763	1,192
Deferred tax expense from use of tax loss carryforwards	5,951	26,606
Deferred tax income/expense from temporary differences	4,373	– 5,516
	<u>15,087</u>	<u>22,282</u>

Deferred taxes were calculated at the relevant national tax rates, which in 2002 were between 10.4% and 40%. Changes in tax rates on the balance sheet date were included. The corporation tax rate of 26.5% levied in, and limited to, 2003 to finance compensation for victims of the floods which occurred in 2002 was disregarded, since the expense of calculating it would have been disproportionately high. The Group tax rate was the same

in T€	2002	2001
Pre-tax profit	<u>43,200</u>	<u>62,253</u>
Group tax rate	39.0%	39.0%
Expected tax expense	<u>16,848</u>	<u>24,279</u>
Tax effects from		
- variances due to different tax rates	– 5,655	– 552
- tax-free income	– 3,219	– 1,739
- reversal of write-downs	0	– 1,308
- amortisation of goodwill	1,740	258
- tax decreases and increases	5,649	454
- other	– 276	890
Taxes on income	<u>15,087</u>	<u>22,282</u>
Overall tax ratio in %	34.9%	35.8%

as the domestic tax rate, since more than 80% of Group pre-tax profit was generated in the domestic market.

Other tax effects included prior period income tax refunds and the cumulative effects from the disclosure of hidden reserves upon initial consolidation.

(19) Earnings per Share

The total number of ordinary shares issued was 71,396 higher than in the previous year due to the introduction of an employee share-ownership plan (ESOP) in the second quarter. There was no dilution of earnings per share. In accordance with IAS 33 (revised 1997) earnings per share for the previous year were adjusted retrospectively.

	2002	2001
Net profit for the year in T€ after minority interest	28,113	39,973
Weighted average of ordinary shares issued	<u>16,045,380</u>	<u>16,045,380</u>
Earnings per share	<u>1.75</u>	<u>2.49</u>

(I) Explanatory Notes to the Cash Flow Statement

The cash flow statement as per IAS 7 (revised 1992) shows how Group financial resources changed as a result of cash inflows and outflows from operating, investing and financing activities.

Cash flows from operating activities were adjusted for currency translation effects and changes in the number of consolidated companies. Financial resources comprised cash and cash equivalents and securities.

At T€148, the cost of acquiring other companies was much lower than in 2001 (T€44,801). Both amounts were paid in full in the relevant business year. They were set against cash and cash equivalents worth T€148 (2001: T€29,027). Following the merger of Karat Digital Press

GmbH, non-current assets worth T€15,063 and current assets worth T€27,735 were included in the consolidated financial statements. The borrowed capital acquired totalled T€52,943.

Interest expense comprised T€5,676 (previous year: T€9,144) in interest received and T€11,200 (T€7,026) in interest paid. Tax expense embraced tax refunds of T€31 (2001: T€589) and payments of T€11,472 (T€4,835).

(J) Segment Information

In accordance with the rules contained in IAS 14 (revised 1997), segment information for the KBA Group was broken down into business segments (web and special presses, sheetfed offset presses) as the primary reporting format and geographical segments as the secondary format. The distinction reflects internal reporting structures.

The business segment **web and special presses** encompasses newspaper, commercial, gravure, directory and security presses.

The business segment **sheetfed offset presses** constitutes commercial, book, packaging and digital presses.

Segment information was based on the same accounting and consolidation policies as the consolidated financial statements. Intragroup transactions contained in

the segment result (operating profit) were priced to market.

There were no inter-segment sales. Non-cash expenses included changes in provisions and the impairment of current assets. Segment assets and liabilities included all assets and liabilities that had contributed to the operating profit generated in the business segment concerned. Segment assets primarily related to intangible assets, property, plant and equipment, inventories, trade receivables, receivables from affiliates and other assets. Segment liabilities basically included other provisions, payments received, trade payables and other liabilities.

Reconciliation covered assets, debts and consolidation between segments.

Business segments								
in T€	Web and special presses		Sheetfed offset presses		Consolidation/ reconciliation		Group	
	2002	2001	2002	2001	2002	2001	2002	2001
External turnover	734,796	752,534	618,959	551,490	0	0	1,353,755	1,304,024
Operating profit	29,183	31,726	17,390	26,912	0	0	46,573	58,638
Depreciation	26,484	27,832	18,542	10,910	0	0	45,026	38,742
Significant non-cash expenses	73,621	94,271	38,392	41,837	0	0	112,013	136,108
Net profits of associates	3	56	0	0	0	0	3	56
Capital expenditure	30,977	50,109	18,220	28,980	0	0	49,197	79,089
Assets	532,982	618,047	591,222	534,631	116,359	181,428	1,240,563	1,334,106
Liabilities (with payments received)	344,371	492,167	143,751	126,774	276,838	262,025	764,960	880,966

The geographical areas were defined according to their significance for Group income. Other regions encompass Asia, central and south America, Africa and Australia.

Geographical segments						
in T€	External turnover		Capital expenditure		Assets	
	2002	2001	2002	2001	2002	2001
Germany	255,785	255,789	43,416	59,857	871,681	884,622
Rest of Europe	589,248	675,717	3,292	18,633	163,407	178,262
North America	207,095	183,433	2,489	599	89,116	89,794
Other regions	301,627	189,085	0	0	0	0
Consolidation/reconciliation	0	0	0	0	116,359	181,428
Group	1,353,755	1,304,024	49,197	79,089	1,240,563	1,334,106

(K) Related Party Relationships

Related party relationships as defined by IAS 24 (reformatted 1994) exist between the members of the management board and supervisory board.

Remuneration for active members of the management board fell to T€3,630 from T€5,521 in 2001, with T€1,409 (T€1,349) representing fixed remuneration and T€2,221 (T€4,172) variable remuneration. Remuneration for retired members and their survivors stood at T€824 (T€797). Supervisory board remuneration totalled T€426 (T€862).

T€13,713 (2001: T€13,592) was set aside for pension claims by active and retired members of the management board, and their survivors.

At 31 December 2002 members of the management board held 3.6% and members of the supervisory board 6.2% of Koenig & Bauer share capital, giving a total of 9.8%. No options or derivatives were issued.

There were no other transactions with related parties.

(L) Management and Supervisory Boards

A declaration of compliance was issued in accordance with §161 of German Company Law and made permanently

accessible under www.kba-print.de/en/investor/corporate_governance.html

Supervisory Board

Peter Reimpell

Chairman
Banker
Munich

Dr Hans-Bernhard Bolza-Schünemann

Deputy chairman
Engineer and physicist
Würzburg

Gottfried Weippert*

Deputy chairman
Technician
Eibelstadt

Josef M. Barth

Tax consultant
Stuttgart

Peter Hanzelka*

Milling machine operator
Coswig

Rupert Hatschek

Investment manager
Vienna, Austria

Alfred Kuffler*

Representative of IG Metall
Frankenthal

Philipp Pöhlert*

Machinist
Bensheim

Dieter Rampl

Spokesman for the management board
Bayerische Hypo- und Vereinsbank AG
Munich

Werner Ring*

Representative of IG Metall
Würzburg

Klaus Schmidt*

Director
Hettstadt

Prof Horst Peter Wölfel

Professor of engineering dynamics
Technical University Darmstadt
Höchberg

* elected by the workforce

Committees

Mediation committee as per § 27 (3) of the Law on Codetermination

Peter Reimpell
Rupert Hatschek
Klaus Schmidt
Gottfried Weippert

Human Resources Committee

Peter Reimpell
Rupert Hatschek
Dr Hans-Bernhard Bolza-Schünemann
Gottfried Weippert

Financial Audit Committee

Dr Hans-Bernhard Bolza-Schünemann
Peter Reimpell
Peter Hanzelka
Philipp Pöhlert

Management Board

Reinhart Siewert

President
Würzburg

Albrecht Bolza-Schünemann

Deputy president
Radebeul

Claus Bolza-Schünemann

Würzburg

Dr Frank Junker

Radebeul

Peter Marr

Waldbüttelbrunn

Andreas Mössner

Radebeul

Walter Schumacher

Gerbrunn

Other positions held by members of the Koenig & Bauer AG supervisory board

	Member of the supervisory board at:
Dr Hans-Bernhard Bolza-Schünemann	Körber AG, Hamburg
Deputy chairman	E.ON Bayern AG, Würzburg
Rupert Hatschek	Wienerberger AG, Vienna
	KBA-Mödling AG, Mödling
Dieter Rampl	Brau und Brunnen AG, Dortmund
	Vereins- und Westbank AG, Hamburg
	Bode Grabner Beye AG & Co. KG, Grünwald
	Odeon Film AG, Munich
	Bavaria Film GmbH, Munich
	Bavaria Filmkunst GmbH, Munich
	MAHAG - Münchener Automobil-Handel Haberl GmbH & Co. KG, Munich
	Bank Austria AG, Vienna
	HVB Asset Management GmbH, Munich
	HVB Consult GmbH, Munich
	Pension Consult GmbH, Munich

(M) Proposal for the Utilisation of Net Profit

The single-entity statements for Koenig & Bauer AG were prepared under German accounting and reporting law. In accordance with §58 (2) of German Company Law half the net profit of T€17,940 was transferred to revenue reserves. The net profit shown in the balance sheet was T€8,970.

The dividend payable to shareholders was based on the net profit disclosed in the financial statements for Koenig & Bauer AG, in compliance with German Company Law. With the approval of the supervisory board a proposal will be submitted to the AGM to utilise net profit totalling T€8,970 as follows:

Payment of a dividend of 50 cents per ordinary share on 16,071,396 no-par shares	€8,035,698
Balance carried forward	€934,302

The proposed dividend payment does not give rise to a tax reduction for either shareholders or the company.

Würzburg, 21 March 2003

Management Board



Reinhart Siewert
President



Albrecht Bolza-Schünemann
Deputy president



Claus Bolza-Schünemann



Dr Frank Junker



Peter Marr



Andreas Mössner



Walter Schumacher

(N) Auditors' Report

We have audited the consolidated financial statements, comprising the balance sheet, the income statement and the statements of changes in shareholders' equity and cash flows as well as the notes to the financial statements prepared by Koenig & Bauer Aktiengesellschaft, Würzburg, for the business year from 1 January to 31 December 2002. The preparation and the content of the consolidated financial statements in accordance with International Financial Reporting Standards (IFRS) are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

We conducted our audit of the consolidated financial statements in accordance with German auditing regulations and German generally accepted standards for the audit of financial statements promulgated by the Institut der Wirtschaftsprüfer (IDW). Those standards require that we plan and perform the audit such that it can be assessed with reasonable assurance whether the consolidated financial statements are free of material misstatements. Knowledge of the business activities and the economic and legal environment of the Group and evaluations of possible misstatements are taken into account in the determination of audit procedures. The evidence supporting the amounts and disclosures in the consolidated financial statements are examined on a test basis within the framework of the audit. The audit includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements give a true and fair view of the net assets, financial position,

results of operations and cash flows of the Group for the business year in accordance with International Financial Reporting Standards.

Our audit, which also extends to the Group management report prepared by the Company's management for the business year from 1 January to 31 December 2002, has not led to any reservations. In our opinion, on the whole the Group management report provides a suitable understanding of the Group's position and suitably presents the risks of future development. In addition, we confirm that the consolidated financial statements and the Group management report for the business year from 1 January to 31 December 2002 satisfy the conditions required for the Company's exemption from its duty to prepare consolidated financial statements and the Group management report in accordance with German law.

Munich, 21 March 2003

Bayerische Treuhandgesellschaft
Aktiengesellschaft
Wirtschaftsprüfungsgesellschaft
Steuerberatungsgesellschaft
Auditors and Tax Consultants



Wiegand
Auditor



Dr Grottel
Auditor

Key Financial Dates

Interim report on 1st quarter 2003
15 May 2003

Koenig & Bauer Annual General Meeting
26 June 2003
Congress Centrum Würzburg

Payment of dividends:
27 June 2003

Interim report on 2nd quarter 2003
14 August 2003

Interim report on 3rd quarter 2003
14 November 2003

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