

Kongsberg, 11.12.15

## **Kongsberg Automotive's Letter to Shareholders regarding the ISS report**

Dear Shareholder,

Reference is made to the report presented by Institutional Shareholder Services ("ISS") on Tuesday 8 December, which was brought to our attention Wednesday 9 December. The report in question points to several alleged issues related to Kongsberg Automotive ASA ("KA" or "the Company") and to the process leading up to the Extraordinary General Meeting ("EGM") demanded to be held 21 December. Furthermore, the report comments on KA's financial performance, its strategy and position in relevant markets. Comments are made by a group of shareholders consisting of the hedge funds Makuria, Teleios and others holding more than 5% (the "Minority Shareholder Group" or "the MSG") of KA shares and ISS. We find substantial parts of this information to be incorrect and biased to the extent that it misrepresents the actual situation. We therefore find it necessary to address some of these issues.

### **1. Structure of the election of Directors at the Extraordinary General Meeting**

#### **Extract from the ISS report:**

*"[...] based on market and past company practice, it is ISS' conclusion that the all-or-nothing structure of this election is the result of a decision on the part of the board, rather than a request by the proponents.[...] While such poor corporate governance is not in itself a sufficient reason to oppose the current board, the aforementioned conditions can be seen to have a negative effect on shareholder value by insulating the board from dissent both with regard to the concerns outlined herein, as well as concerns that may arise in the future."*

#### **Comment by KA:**

This statement is incorrect. The request for the Extraordinary General Meeting was made by e-mail to the Chairwoman of the Board 24 November 2015. The request was made by the Minority Shareholder Group. The Minority Shareholder Group had not previously communicated these intentions to the Nomination Committee or any other body of the Company.

The ISS report states that the Minority Shareholder Group has been flexible with regards to the composition between current and proposed board members for the upcoming election. This is not correct. The MSG presented in an e-mail to the Nomination Committee and the CEO a complete replacement of the current board with new candidates. The MSG has in all communication with the CEO, the Chairwoman of the Board and the Chair of the Nomination Committee communicated the need for an entire new board, thus leaving no room for compromise, which could have facilitated continuity for the Company by keeping some of the current board members. Such a suggestion would also have secured the interests of other shareholders.

Furthermore, the proposed directors for the Board are unknown to the Nomination Committee. The request for an EGM by the Minority Shareholder Group was received 24 November 2015, giving the Nomination Committee under a week to perform proper interviews and comprehensive background checks for

the proposed board members. The invitation to the upcoming EGM was required by Norwegian law to be sent the week after receiving the letter, in order to hold the EGM before Christmas Eve. Norwegian law dictates, invitations to an EGM must be sent out three weeks in advance of the date of the meeting. The Nomination Committee strongly recommended to postpone the election of a new Board until the Annual General Meeting, in order to ensure proper time for interviews and in-depth background checks of all proposed new board members. This is in-line with good corporate governance. However, to accelerate the process, the Nomination Committee recommended moving the date of the upcoming AGM from May to March 2016.

The “all-or-nothing structure of this election” is therefore not decided by the Board of the Company, nor the Nomination Committee. It is rather a result of the Minority Shareholder Group’ own request and approach.

## **2. Specific comments from the Minority Shareholder Group on strategy and business plan**

### **Extract from the ISS report:**

*“[...] the proponents highlighted the following concerns over the current corporate strategy:*

- *The company is poorly positioned within the electric vehicles market, and poorly positioned to transition to automated manual transmission.”*

### **Comment by KA:**

This is inaccurate; KA has secured customer orders on state-of-the-art onboard chargers for use in both trucks and buses. This is to be launched in 2016, and is a part of the Efficient Powertrain growth platform together with converters and inverters. The second phase of this program is to be launched in China in 2017. Further information is to be found in our CMD presentation.

The company has further secured significant business in the AMT area, to be launched in 2017. KA is increasing its focus on this segment in accordance with AMT moving from being an “European choice” to also being a strong trend globally, also in the US market. The company is further entering the second technology wave for AMT in Europe. Please note that AMT is also part of the company’s Efficient Powertrain growth platform.

Amongst our other growth platforms, you will find Seat Comfort, where major business has been booked in 2015. KA’s third growth platform is Advanced Fluid Handling, where the company has a unique market position within quick connectors. Business for this growth platform is currently being expanded from Europe to both China and the US.

### **Extract from the ISS report:**

- *“The company has not sufficiently participated in the recent growth of the Chinese market”*

### **Comment by KA:**

KA is well positioned to capture market shares in China, with three Chinese plants. Chinese indigenous OEMs are moving in the direction of high quality trucks. This is an excellent opportunity for the company to bring European technology into the Chinese market.

**Extract from the ISS report:**

- *“The board has focused on horizontal, rather than vertical, diversification, despite industry trends in the opposite direction. One effect of this is a potential reluctance on the part of potential buyers, who may only be interested in one particular division*

**Comment by KA:**

First of all, the Management and the Board of Directors have built KA to become a solid and sustainable platform for growth and dividend capacity. Divestment of conventional products is not a sustainable solution to build a R&D intensive platform; Conventional products remain important in terms of scale, customer credibility and cash flow to fund further growth. Customer credibility is key to gain new contracts. Secondly, KA continuously reviews segments and product portfolio to optimize product offering and reduce complexity. At the CMD, KA announced plan to divest Light duty cables business unit in 2016, and in 2Q KA announced phase out Head- and Armrests products.

The proponents have further alleged that KA has not been responsive to proposals ‘from potential buyers of parts of the company. This is not correct. The company has not rejected any indicative offers or substantial proposals to acquire any division or part of the company over the past years. We kindly ask that the allegations are retracted unless ISS or the proponents can substantiate such offers.

**3. Poor performance during the last five years, and low relative valuation**

**Extract from the ISS report:**

- *“For the five years ended Nov. 30, 2015, KOA's TSR of 50.1 percent has significantly underperformed the 116.3 percent of the median of peers. For the last three years, KOA's TSR of 284.2 percent has significantly outperformed the 96.8 percent of the median of peers. However, the three-year data is misleading as it appears to be more of a bounce from a financially distressed situation that true longer term operational improvements*

**Comment by KA:**

To understand the valuation of KA, the history of the company needs to be understood: (1) In the years following the financial crisis, KA found itself in a situation with substantial debt. The company was in financial distress and this was reflected in the share price. The Management and the Board of Directors outlined a successful long-term strategic operational plan to transform KA to a sustainable platform for growth and dividend potential in order to maximize shareholder values. In 2015, five years after the strategic operational plan was proposed, KA has secured record-high values of new contracts. Furthermore, the company is currently investing into R&D at a high pace to maximize growth and value. The company has substantially reduced debt, and communicated a medium-term dividend potential alongside sustaining R&D investments.

Additionally, the ISS report argues that *“for the last three years, KOA's TSR of 284.2 percent has significantly outperformed the 96.8 percent of the median of peers. However, the three-year data is misleading as it appears to be more of a bounce from a financially distressed situation that true longer term operational improvements”*. Contradictory, ISS state that the share price return for a three-year period is misleading as the share price of KA appears bounce from a financially distressed situation in the period, but emphasis the share

price return for a five-year period which contains the same data as in the three-year data period series (!) in the conclusion of the report. The argument of an affected share price by a “*financial distressed situation*” used in the ISS report is true, but the argument is more relevant for why a five-year data period cannot be used for a financial performance review, rather than a three year period review.

Furthermore, a five-year period study of historical share price performance of KA is biased due to two reasons: 1) several companies in the automotive industry filed for Chapter 11 in the years post-financial crisis. Thus, compromising the peer group to only companies in operation today will give a biased result as it exclude the companies which are no longer in operation. 2) The financial distress for KA mentioned above had a negative impact on the share value, but the operational and financial turnaround has led to a significant outperformance for KA compared with peers and the market from 2012 till date. The three-year performance of KA has significantly outperformed the benchmark and all peer companies mentioned in the ISS report (except one: Valeo).

The Management acknowledges that KA is undervalued compared to its Swedish peers. The Management of Kongsberg Automotive ASA is of the strong belief that the long-term strategy and business plan which was communicated on the Capital Markets Day (CMD) on Wednesday 2 December 2015 will bring the valuation of the company up to peer levels. This belief seems to be shared by our shareholders; the market reacted by sending the KA share up 8.7%, in an otherwise flat market on the CMD.

**Extract from the ISS report:**

- “*The company's share price performance has significantly underperformed the MSCI World Auto Components index as measured from the entry of each of the current five shareholder-elected board members, including current chairperson Ulla-Britt Fräjdin-Hellqvist.*”

**Comment by KA:**

The report further includes a statement by the proponents referring to the development of the share price in the respective periods of the board directors and in particular the present chair of the board; Ulla-Britt Fräjdin-Hellqvist who has served at the board from 2007. The proponents here completely disregard the impact of general market conditions on the company's share price hereunder the finance crisis that started in 2007 which hit the company hard. Unfortunately, the company made a large acquisition pre-financial crisis. The financial crisis hit the new group hard, resulting in a financial distressed situation which had a negative effect on the share price. However, the current chair of the board join the board post-acquisition completion, thus comparing the share price performance with the date of joining the board is bizarre.

**4. The Board's claimed lack of automotive experience**

**Extract from the ISS report:**

- “[...] *experience is a particularly salient issue in the case of this election*”

**Comment by KA:**

The report claims that the current Board lacks automotive experience. We cannot agree to this statement. Three of the five board directors elected by the shareholders have long and broad experience from the Automotive Industry covering both passenger cars and commercial vehicles.

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Aligned with the Board of Directors, the Management of Kongsberg Automotive supports the Nomination Committee's recommendation to postpone any changes to the Board of Directors until the 2016 AGM, which is to be accelerated from May to March 2016.

Please do not hesitate to contact myself if you have any questions to this report.

Yours sincerely

On behalf of Kongsberg Automotive ASA

*Hans P. Havdal*

Hans Peter Havdal

President & CEO