aap Implantate AG

Management Board Report to the General Meeting of Shareholders of *aap* Implantate AG on July 19, 2004 on Agenda Items 4 and 5

Management Board report to the General Meeting on Agenda Item 4

The proposal put forward under Agenda Item 4 of the General Meeting of *aap* Implantate AG held on July 19, 2004 recommends increasing capital stock by an increase in cash capital. The issue amount and subscription price is EUR 1.00. Shareholder subscription rights are not ruled out, so the interests of existing shareholders are fully protected.

The background to this recommendation is the serious liquidity crisis that the Company currently faces. Unless new liquidity is brought into the Company within the next few months, insolvency cannot be ruled out.

Because of this the Company has entered into an agreement with a group of investors on a financing package. This guarantees an inflow of funds of at least EUR 8 million into the Company on condition that (i) creditor banks waive a substantial part of their debt claims, (ii) BAFin, the German Financial Supervisory Authority, grants exemption from a mandatory offer and (iii) this General Meeting adopts a resolution to this effect and this is recorded in the Commercial Register. The waiver by creditor banks of a substantial part of their debt claims has already been arranged in binding agreements. BAFin exemption has been applied for. Once exemption is granted, the financing package will be subject only to a resolution by the General Meeting, recording of this resolution in the Commercial Register and implementation of the capital increase.

The Company and the group of investors consider the sum of EUR 8 million to be the minimum required to ensure lasting financial cover for the Company's reorganization, to equip the Company with sufficient liquid resources and to finance investment in new products and activities aimed at further developing markets.

After an intensive search the Management Board succeeded in finding investors to ensure the Company's continued financing. No other possibilities of bringing in liquid funds were found. Moreover, given the present restrictive lending practices of banks the Management Board sees no adequate way of financing the Company's future business activities enduringly by taking up more conventional loans. Recent talks with our bankers have confirmed this assessment.

The above-mentioned agreement with the group of investors was entered into against this background. Among other things, the agreement stipulates:

a. The investors will guarantee a capital increase of EUR 8,000,000.00, i. e. they will subscribe the amount remaining from EUR 8,000,000.00 after free shareholders have exercised their options.

b. Capital will be increased by a maximum of EUR 9,739,058.00, i. e. twice the present capital stock (subscription right 1:2).

c. The present major shareholder, Mr. Uwe Ahrens, and other existing shareholders of the Company will transfer their subscription rights to the investors, with the result that the group of investors will have approximately 43% of subscription rights.

d. Immediately after the agreement has been signed, a bridging loan of EUR 800,000.00 will be granted (this has already been done).

e. The Company will grant the group of investors the right to subscribe for shares that are not subscribed for by shareholders, at the price of EUR 1.00.

f. After implementation of the capital increase, the Company will use the proceeds of the capital increase to pay off a large part of the remaining loan liabilities to banks after the waiver.

g. Mr. Oliver Bielenstein, a former partner of Ernst & Young, Zürich, will be appointed as the new CFO (this has already been done).

h. Discussion and agreement on refilling Supervisory Board posts (the Management Board's proposal that one member should remain and that there should be two new members, is based on this agreement).

Management Board report on Agenda Item 5 under § 203 sub-sections 1 and 2 clause 2 in conjunction with § 186 sub-section 4 clause 2, § 186 sub-section 3 clause 4 of the German Stock Corporation Act (AktG)

Under Agenda Item 5 of the General Meeting of *aap* Implantate AG to be held on July 19, 2004, the Management Board and the Supervisory Board propose an amendment to existing approved capital to the effect that an exclusion from subscription rights also be possible for the purpose of issuing shares for reorganization purposes. In that case new shares can be issued speedily to investors wishing to contribute toward the Company's reorganization. In putting forward this proposal the Management Board is reacting to the Company's tight situation, in which it may prove necessary to recruit investors willing to aid recovery. This applies particularly in the event that the recovery strategy outlined under Agenda Item 4 cannot be implemented successfully, for whatsoever reasons. In that case, discussions with further investors could not be completed with the necessary speed if another General Meeting had to be held before they were allowed to participate.

The dilution of existing stockholders' participations associated with a possible increase from approved capital would be unavoidable given that the overriding priority is to ensure the Company's survival. The Management Board undertakes to make use of this option to rule out subscription rights only after prior examination of all financing instruments that can be considered in the context of reorganization. Naturally, the Management Board will only exercise this power if the share issue is clearly in the Company's interest and the Management Board's decision will be subjected to critical and thorough examination by the Supervisory Board.

The Management Board will report each utilization of approved capital to the General Meeting.