

RUAG

Aerospace Defence Technology

Annual Report 2006

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RUAG achieves solid earnings

The RUAG technology group achieved a satisfactory, solid profit in the 2006 financial year, further increasing the value of the company. Every division contributed to this success. Companies and divisions acquired in recent years were integrated, consolidated and made more profitable. Strategic objectives for upcoming years were revised in Strategy 2010.

With production sites in Switzerland, Germany and Sweden, RUAG provides customers with military and civilian products and services in three markets:

- Aviation & Space
- Defence & Security
- Ammunition & Products

The company's eighth year of business since its founding as a registered corporation under private law saw the previous year's already discernible trend toward improved earnings performance confirmed. Whereas an otherwise strong operating income was exceptionally hard hit by one-time occurrences in 2005 – storm damage reduced EBIT by CHF 35 million – EBIT for the year under review showed a strong gain. In general, the key figures show that the Group is proceeding successfully on its chosen course.

Business environment

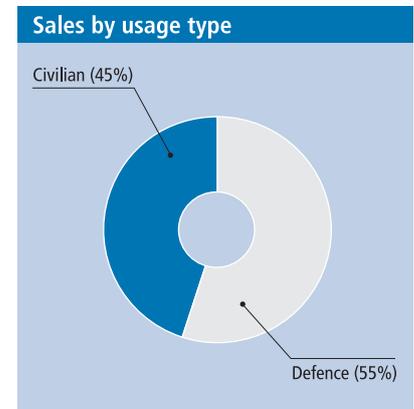
The economic environment was favourable during the year under review. The world economy is in the strongest upturn since the early 1970s. While this upswing was initially driven mainly by the United States and China, the recovery in the euro zone has gained momentum. Moreover, Japan, Latin America and various east European countries

have furnished a broader regional base for growth. Even the shock of a substantial increase in crude oil prices has been absorbed, a fact attributed by experts to the economy's reduced dependency on oil, a stability-focused monetary policy and moderate inflation. Large increases in non-ferrous metal prices, however, have substantially increased pressure on RUAG's margins in the small calibre ammunition business.

The market

In the *aviation industry* optimism has returned with a vengeance. Healthy growth is forecast in the years ahead both for passenger aircraft with a capacity of over 100 seats and for business jets. The opening of additional markets, a good economic outlook and the increasing mobility needs of a growing number of people are seen as the main drivers of this growth. Stable sales of regional aircraft are expected. This overall positive picture for civil aviation was somewhat overshadowed in the public eye during the year under review by the delays in delivery of the Airbus A380 superjumbo, for which RUAG produces wing trailing edges and other structural components, and by continuing turbulence at Airbus parent company EADS.

Since then the Airbus A380 has successfully completed major long-distance test flights. European and American agencies certified the A380 as airworthy on 12 December 2006, a major milestone. While the A380's high profile has pushed the success story of the Airbus A320 family, on the market now for 20 years, into the background, exceptionally strong order intake has repeatedly ratcheted up the pace of deliveries. RUAG supplies various structural com-

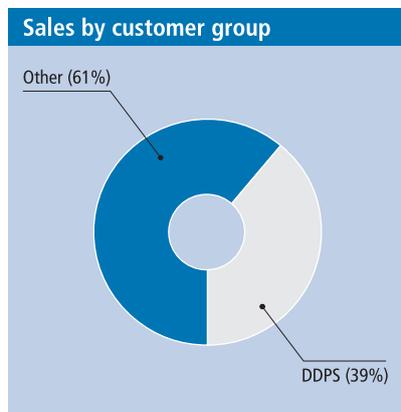


ponents for A320 aircraft, including the rear fuselage section, pressure bulkhead and side fuselage panels.

Following a period of stagnation, the long-awaited recovery in *space activities* is gradually setting in. The European Space Agency ESA has replenished the budgets for some interesting missions. For its part, NASA is planning further missions, some of them spectacular, for the years ahead. It remains to be seen how far RUAG will benefit from this improved outlook as a niche player in the space market. The relevant operations were combined in a single organizational structure and placed under unified management during the 2006 financial year.

Defence technology: Deployed forces are unanimous in affirming the usefulness and necessity of armour protection for vehicles and installations, and especially of network-enabled operation systems. There is growing readiness to invest in these areas. Otherwise, the defence budgets of various European countries, while seeing some upward correction, have not generated any new impetus for the defence technology market as a whole. The industry contin-





ues to work its way through the consequences of the enormous reduction in unit volumes and associated drop in sales during the past fifteen years and remains bogged down in a consolidation process.

Armaments programme: The Federal Parliament's approval of the 2006 armaments programme is encouraging. Based on this decision, RUAG will be able to undertake significant modernization programmes in a number of projects for its single largest customer, the Federal Department of Defence, Civil Protection and Sports (DDPS)/the Swiss Armed Forces. This follows several years in which RUAG's share of the Swiss Armed Forces' capital expenditure was under ten percent.

Reconstruction

The metalworking facility at Altdorf had to be rebuilt at considerable cost after the devastating severe weather of the previous August. At the same time, the operation's strategy was realigned and a forward-looking technology transition was undertaken in production of a key product, high-precision "metroframes" for the semiconductor industry. Thanks to the staff's enormous hard work and

to generally favourable economic conditions for the Swiss machine tool industry, this business was successfully stabilized. Due to the delivery times for certain special processing machines, however, the RUAG metalworking centre will not be producing at full capacity until 2007.

Acquisition

The activities of development company C.O.E.L. in Wedel/Hamburg were acquired as at 1 January 2006. The acquisition makes RUAG the leading European supplier of two-way laser systems for simulation and training equipment for security forces.

Structural issues

Aircraft Service Bern Belp AG, Sun Aircraft Services SA in Lugano, Mecanex S.A. in Nyon, HTS AG in Wallisellen, Derendinger & Cie SA in Geneva and RUAG Aerospace Structures GmbH and RUAG Aerospace Services GmbH, both in Oberpfaffenhofen, Germany, all formerly reporting to RUAG Aerospace, were fully integrated into the Aerospace division. The division in turn restructured its internal organization on a business unit basis. The integration had several aims, including improving earnings, concentrating management responsibility and, thanks to a unified presentation, better visibility on the market.

Divestment

RUAG Ammotec Inc. USA, a trading company, was sold to UMAREX GmbH & Co. KG of Arnsberg, Germany, effective retroactively at 1 January 2006.

Revenue

Sales grew 4.5% from the previous year to reach CHF 1.247 billion (CHF 1.194

billion). The share of civilian business increased to 45% (38%).

By region, Switzerland's share of sales remained at the 2005 level of 47%. 40% of sales were realized in other European countries (42%), 7% with customers in North America and 4% in the Asia-Pacific region.

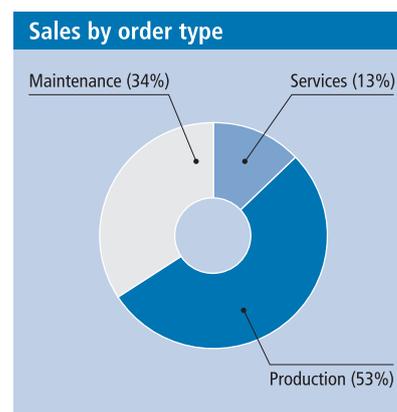
Sales by order type also proved robust, with production accounting for 53%, maintenance for 34% and services for 13%.

Capital expenditure

Capital expenditure for the year under review totalled CHF 100 million (CHF 46 million), of which some 75% was spent on renovating and modernizing operating equipment. Two investments were particularly salient: the reconstruction of the metalworking centre in Altdorf and two modern riveting robots for the manufacture of aircraft structural components at the Oberpfaffenhofen site.

Earnings

Earnings before interest and taxes amounted to CHF 71 million (CHF 19 million). A direct comparison with the



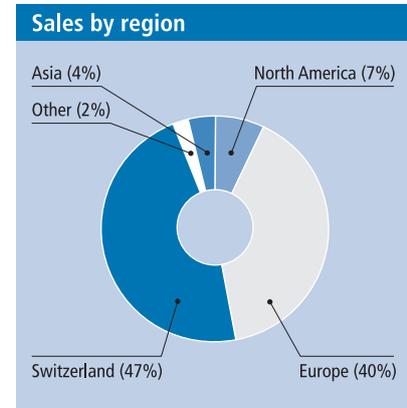
previous year yields a distorted picture if the one-time occurrences that caused the loss are not considered. A comparison with the prior year operating profit of CHF 61 million, however, reveals that the planned improvement in ROE has already been partially achieved and is beginning to bear fruit.

Major projects and orders

For seven years RUAG has been manufacturing sophisticated components for the CF34-10E jet engine of leading producer General Electric (GE). This engine is used in the Brazilian aircraft manufacturer Embraer's short and mid-range planes. Collaboration with GE was expanded during the year under review: RUAG was awarded a contract to produce components for the CF34-10A engine. This engine is used to equip the ARJ21 aircraft built by Chinese manufacturer AVIC (Aviation Industry of China). RUAG also overhauled and modified F-5 engines for the Chilean air force.

In addition to the Swiss Air Force's Cougar fleet, RUAG has also won contracts to equip the Super Puma helicopters of the Spanish and Swedish air forces with self-protection systems. Partnerships have been initiated with SAAB Avionics and EADS for further projects in this area.

RUAG is developing a new armoured vehicle launched bridge (AVLB) for the Finnish army based on the Leopard 2 tank chassis on the behalf of the Finnish armaments group Patria. The new generation of AVLBs makes short work of obstacles with its 20-metre span and is intended for both civilian and military use. The prototype has undergone a wide range of industrial tests in Thun



and has been delivered to the buyer for extensive field testing in Finland.

RUAG modernized M109 self-propelled howitzers for the Chilean army, meeting a fourth-quarter delivery schedule.

RUAG won an order to install a new radio network at Geneva International Airport. The network is based on Tetra technology and is one of the biggest in Switzerland. It is a major element of airport operation and passenger processing and is being implemented in cooperation with systems partner Rhode & Schwarz.

Lead-free small calibre ammunition was delivered for the first time to the Luxembourg army. RUAG developed a special range of cartridges for the Heckler & Koch MP7 short-range weapon, for which it subsequently received an order from the German Bundeswehr.

Work is under way on Joint Architecture Project II for the Swiss Armed Forces. The project is the first technological step on the way to implementation of the C4ISTAR (Command, Control, Communication, Computer, Intelligence, Surveillance, Target Acquisition and Recon-

naissance) integrated system for network-centric warfare.

RUAG was also awarded an integration order for the Swiss Air Force's Command and Information System. The interfaces with the air intelligence system (Lunas), the Military-Civil Airspace Management System (Micams) and Eurocontrol will be automated.

Research and development

RUAG has for many years promoted lively exchange and cooperation with universities. For example, RUAG established the Space Centre with Ecole Polytechnique Fédérale de Lausanne (EPF Lausanne) in 2003. Together with EPF Lausanne students and other partners, RUAG is developing the first Swiss micro-satellite. The project has already achieved major milestones. The test phase is being carried out at RUAG, and the satellite is scheduled to be placed in orbit in 2008.

Real estate

CHF 23 million was invested in property in 2006 (previous year: CHF 12 million). This increase is attributable to two factors: in Altdorf, parts of the building's

utility infrastructure that had been destroyed by storms had to be restored, and in Berne a major construction project was successfully completed and dedicated.

Human resources

Employees are a critical success factor for any successful enterprise. Following the principle of "develop and challenge", RUAG invests continually in ongoing training. For example, RUAG successfully conducted a tailored training programme for young managers called RUAG Top Leadership during the 2006 financial year. In various modules, participants explored the topics of leadership, self-management, corporate culture, strategic management, marketing and sales and entrepreneurship.

Investments are also being made in a company training centre, for which an existing property in Stans is currently being repurposed as the training strategy undergoes refinement. Training courses will commence at the centre in 2008.

In the year under review RUAG employed 0.7% more staff on average than in the previous year. Headcount

rose to 5,677. For the first time in some while, recruitment of engineers has proven quite costly as a consequence of a tightening labour market.

It has been agreed with labour representatives that, for a limited period to the end of 2007, weekly working hours at the Altdorf metalworking plant and the Thun small calibre production unit will be increased from 40 to 42 hours without extra remuneration. This amicable decision to secure jobs is based on the Swissmem collective labour agreement.

Special attention is devoted to the training of young people just starting their careers. The number of apprenticeships remains high at nearly 400, including 355 in Switzerland alone.

Outlook

Most forecasters expect the economy to continue strong in 2007, even though first signs of a certain weakening can be seen. The excellent order intake (up 35%) and new order levels (up 59%) put the Group on a positive trajectory.







Strategy 2010: A road map to further successful development

The Board of Directors adopted the revised corporate strategy, Strategy 2010, during the first quarter of the year under review, redrawing the road map for further successful development of RUAG. The central feature of Strategy 2010 is the operational focus on three markets: Aviation & Space, Defence & Security and Ammunition & Products. Interim goals are set for the end of 2007, strategic goals for 2010.

After the founding of RUAG as a registered corporation under private law, the guiding plan was the 2000 corporate strategy. The initiatives and goals laid out in this strategy have put the Group on a successful path. In just six years of business, RUAG's customer base has been significantly extended, the loss of defence technology sales to the DDPS for the benefit of the Swiss Armed Forces more than offset, civilian activities expanded and the value of the company enhanced.

A solid foundation

Thus while RUAG's initial strategy has been quite successful, market conditions have changed faster and Swiss Armed Forces reforms have proceeded more rapidly than originally expected. For these reasons, the Board of Directors

ordered a review of the 2000 corporate strategy in 2005. First external experts were engaged to analyse the business environment and the market. They then worked with the Executive Board to apply the results as a foundation for drawing systematic conclusions and developing an action plan.

The new Strategy 2010 does not represent a sudden change, but rather a continuous evolutionary development. It can be summed up in three sets of three keywords: in the next few years, RUAG will focus on three markets, three major directions and three success factors (see diagram).

In addition to a tightening of the portfolio, better returns in all divisions are crucial so that sufficient funds can be generated for capital investments, depreciation and amortization and to finance growth. RUAG will not seek to grow across the board in the next few years, but rather with a focus on the following four areas:

- Aircraft structure manufacture
- Space
- Network enabled operations (C4ISTAR)
- Simulation and training

Implementation of Strategy 2010 is already fully under way at the operating level. Work is proceeding to meet targets in three programmes: innovation, optimization and focus. RUAG will remain active in both the defence and civilian businesses since the two fields are closely linked in terms of technology and know-how. Technological expertise in particular is a central pillar for ensuring the Group's long-term survival and for fulfilling orders for the Swiss Armed Forces.

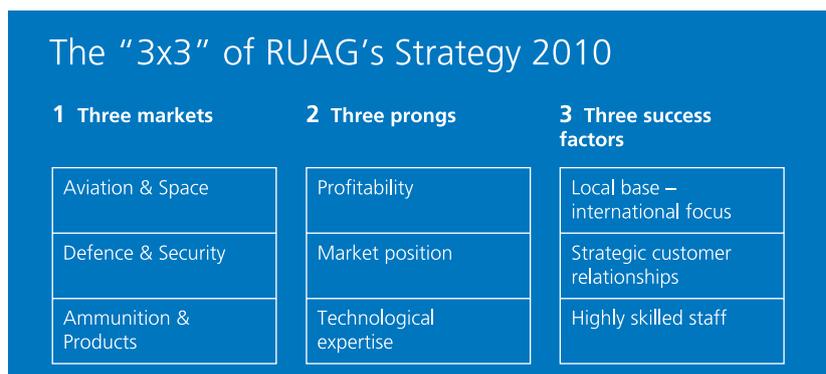
Directors reelected

In May Federal Councillor Samuel Schmid, the head of the DDPS, attended the annual shareholders' meeting in Emmen as the owner's representative. He paid tribute to the positive development of RUAG. The 2005 financial statements were approved, discharge was granted to the governing bodies and the distribution of a reduced dividend was resolved. Due to various special factors, primarily the extraordinary flood damage to facilities and equipment at the Altdorf site, the 2005 income statement reported RUAG's first-ever loss, despite strong net operating income.

In the statutory elections to the Board of Directors, Konrad Peter (Chairman), Hans-Peter Schwald and Dr Peter Saurer were appointed for a further four-year term of office.

New appointments to the Executive Board

At the end of August, Stephan Kocher resigned as a member of the Executive Board and operating head of subsidiary RUAG Land Systems due to his advanced age. The Board of Directors ap-



pointed Urs Breitmeier, head of Marketing and Systems Management at Land Systems since 2001, to succeed Kocher and join the Executive Board.

The Board of Directors also appointed Dr Viktor Haefeli, General Manager of RUAG Components since 2005, to the Executive Board with effect from 1 September.

Peter Scherrer, head of Space Division at RUAG Aerospace, and Claudia Sallay, deputy head of Human Resources at RUAG Electronics, were appointed as the employer representatives on the board of trustees of the RUAG pension fund.

Reimbursement completed

Reserves for socially acceptable measures financed by the Swiss Confederation were included in the starting bal-

ance sheet of 1 January 1999. Intended for planned restructuring measures in the Aerospace division in accordance with the FER accounting standards then in effect, these reserves were never fully utilized, and the Board of Directors approved a reimbursement of CHF 7.1 million to the Confederation in the year under review.

Acknowledgements

The Board of Directors thanks its customers for their trust and for their orders. Thanks are due to the Swiss federal government for its cooperation, and to the Executive Board and the employees for their outstanding performance during the year under review. The Board of Directors and the Executive Board will spare no effort to ensure that RUAG continues to reliably satisfy the needs and expectations of its employees, customers, shareholder and stakeholders.



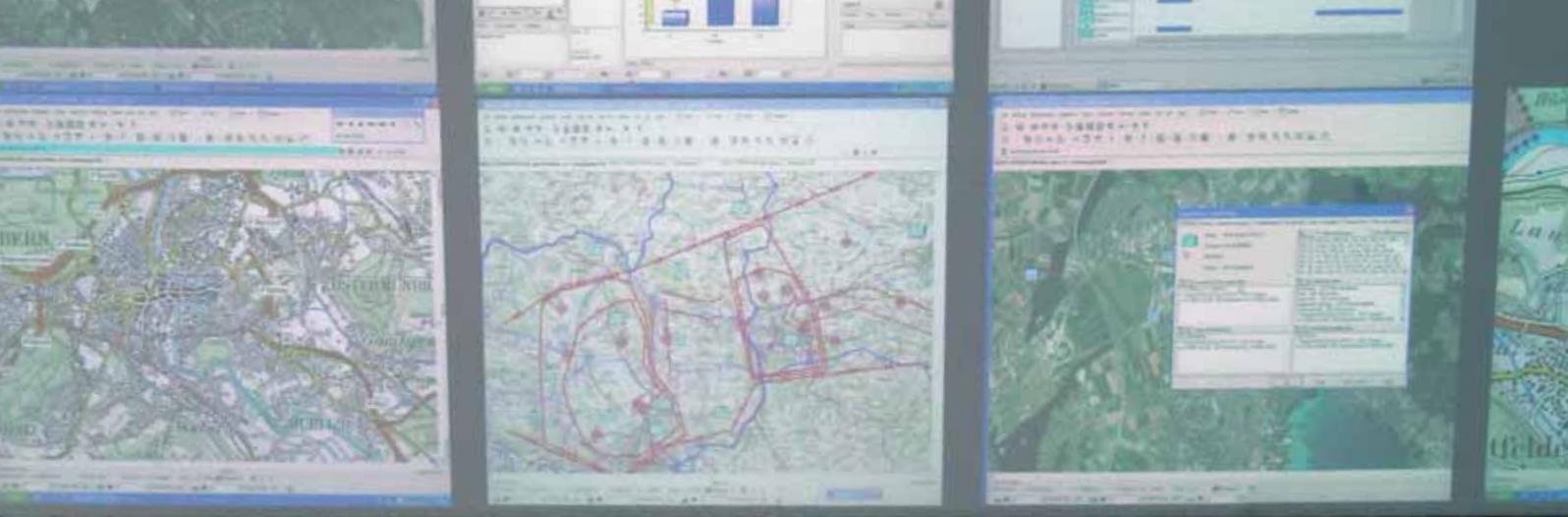
Konrad Peter

Chairman of the Board of Directors



Toni J. Wicki

Chief Executive Officer



Board of Directors

Name	Born	Position	Member since	Elected until
Konrad Peter	1946	Chairman, non-executive	2002	2010
Toni J. Wicki	1944	Chief Executive Officer	1999	2007
Dr Hanspeter Käser	1943	Vice-Chairman as of 5 May 2004, non-executive	1999	2007
Dr Peter Saurer	1945	Non-executive member	2002	2010
Hans-Peter Schwald	1959	Non-executive member	2002	2010
Jakob Baumann	1958	Non-executive member	2003	2007
Paul Häring	1957	Non-executive member	2004	2008

Executive Board

Name	Born	Position	Member since
Toni J. Wicki	1944	Chief Executive Officer	1999
Urs Breitmeier	1963	Member, CEO RUAG Land Systems	2006
Ueli Emch	1945	Member, CEO RUAG Electronics	1999
Dr Viktor Haefeli	1966	Member, CEO RUAG Components	2006
Urs Kiener	1965	Member, Chief Financial Officer	2002
Eduard Knecht	1954	Member, Group Head Human Resources	1999
Cyril Kubelka	1963	Member, CEO RUAG Ammotec	2004
Dr Myriam Meyer Stutz	1962	Member, CEO RUAG Aerospace	2005
Martin Stahel	1946	Member, Head Group Services	2000

The CVs of the members of the Board of Directors and the Executive Board can be found on our website, www.ruag.com.

Corporate management and control principles

This chapter of our Annual Report describes the principles of management and control at the most senior level of the RUAG technology group in accordance with the SWX Swiss Exchange directive regarding information on corporate governance. However, the RUAG Group has made certain adaptations and simplifications to reflect its shareholder structure. Unless otherwise specified, the information is applicable as at 31 December 2006.

Board of Directors

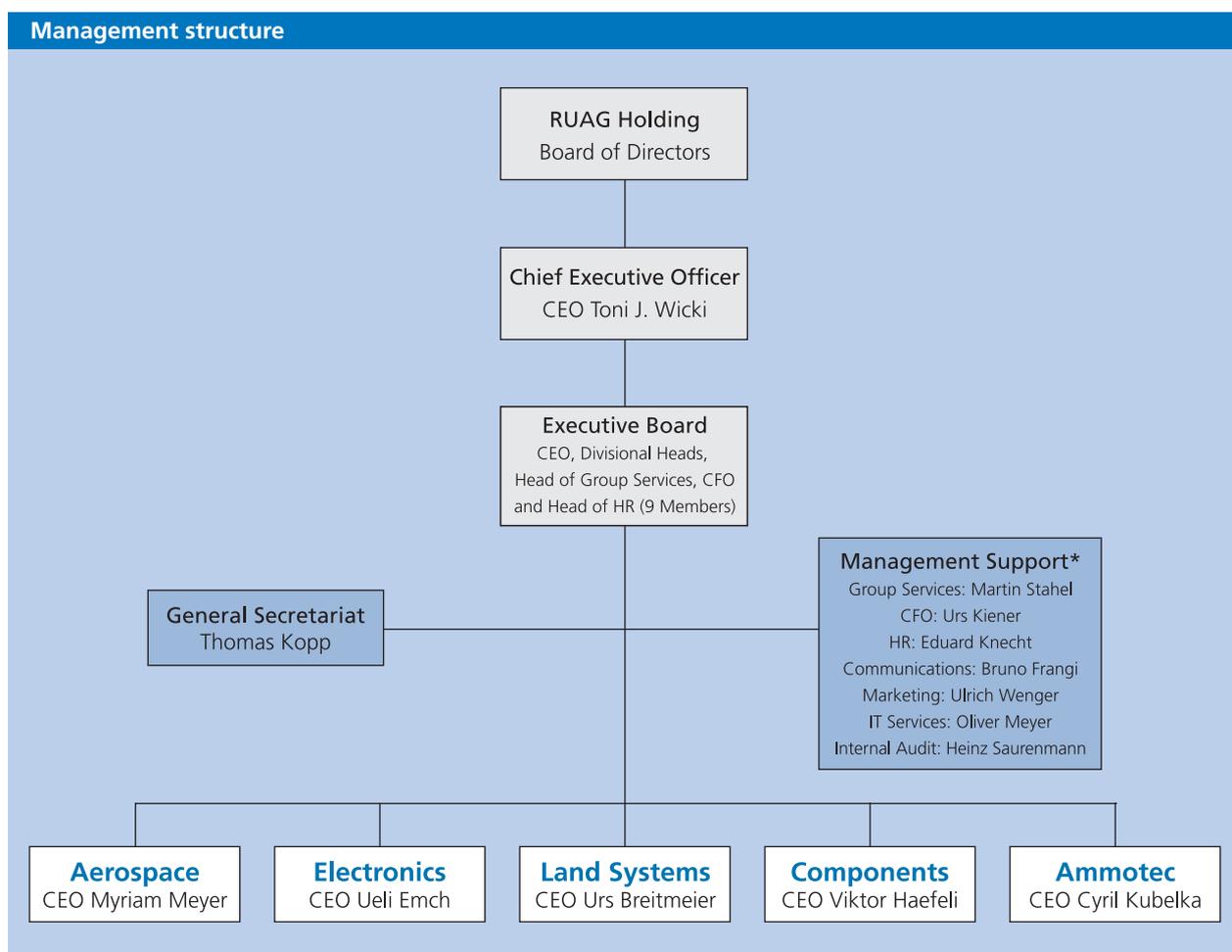
The duties of the Board of Directors of RUAG Holding are governed by the Swiss Code of Obligations, the Federal Council's owner's strategy, the Articles of Association and the Regulations Governing Organization and Operations.

The Board of Directors of RUAG Holding consists of seven individuals. The Chief Executive Officer is currently the sole executive member of the Board. The non-

executive members have no material business relationship with the RUAG Group. The list on page 11 provides information about the name, age, position, date of appointment and remaining term in office of each member of the Board of Directors.

Conflicts of interest

The members of the Board of Directors of RUAG Holding do not sit on the board of any other listed company.



* Finance/Controlling, HR, Communications, Marketing, IT Services, Legal, Internal Audit

Detailed information on the company's legal structure can be found on page 40 of the 2006 Financial Report.

Election and term of office

The Board of Directors of RUAG Holding is elected by the annual shareholders' meeting. In accordance with the Articles of Association, the Board of Directors consists of at least three individuals. A majority of the members of the Board of Directors must be Swiss nationals domiciled in Switzerland. The members of the Board of Directors are elected for a four-year term and may be re-elected. The Board of Directors is responsible for defining the rotation of such elections.

Internal organization

The Board of Directors holds ultimate responsibility for the business strategy and overall management of the RUAG Group. It possesses supreme decision-making powers and determines the guidelines for strategy, organization, finance and accounting to be pursued by the RUAG Group. The Board of Directors has delegated the management of day-to-day business to the Chief Executive Officer (CEO), who is responsible for the overall management of the RUAG Group and for all matters not delegated to another corporate body under the terms of Swiss law, the Articles of Association, the owner's strategy of the Federal Council and the Regulations Governing Organization and Operation.

The main duties of the Board of Directors under the terms of the Swiss Code of Obligations and Articles of Association of RUAG Holding are:

- The strategic orientation and leadership of the RUAG Group in accordance with the owner's strategy of the Federal Council

- The structuring of the accounting system, financial controlling and financial planning
- The appointment and dismissal of members of the Executive Board and other senior executives
- Supreme oversight of business activities
- Production of the Annual Report, preparation of the annual shareholders' meeting and implementation of resolutions passed by the latter.

Decisions are taken by the Board of Directors as a whole. To assist the Board in its role, two committees have been formed: an Audit Committee and a Compensation Committee. In the 2006 financial year the Board of Directors held regular meetings on six occasions. In addition, the committees met on seven occasions. The agenda for meetings of the Board of Directors is set by the Chairman in consultation with the Chief Executive Officer. Any member of the Board of Directors may request that an item be included on the agenda. The members are provided with documentation prior to each meeting to enable them to prepare for the items to be discussed.

The Board of Directors maintains an exchange of views with the senior executives of the company and regularly visits one or more of RUAG's sites.

Committees

The Board of Directors has formed an Audit Committee and a Compensation Committee and elected chairmen. The

committees meet regularly to draw up the minutes of meetings and recommendations for discussion at the regular meetings of the Board of Directors. The agenda of each committee's meetings is set by its chairman. The members of the committees are provided with documentation prior to the meetings to enable them to prepare for the items to be discussed.

Audit Committee

The Audit Committee is composed of the four non-executive members of the Board of Directors: Hanspeter Käser (Chairman), Konrad Peter, Peter Saurer and Paul Häring. The members of the Audit Committee are experienced in financial and accounting matters. The Audit Committee meets regularly, although it may also be convened by the Chairman as and when business requires. The meetings are attended by the Chief Executive Officer, Head of Group Services, Chief Financial Officer, Internal Auditor and representatives of the external auditors.

The main duty of the Audit Committee is to ensure a comprehensive and efficient audit structure for RUAG Holding and the RUAG Group. The duties of the Audit Committee include:

- Assessing processes in the risk and monitoring environment (internal controlling system)
- Monitoring financial reporting
- Assessing the internal and external auditors
- Establishing and approving the main elements of the audit

- Acceptance of the audit report and any recommendations of the auditors prior to submission of the annual financial statements (individual and consolidated) to the full Board of Directors for approval
- Submitting a proposal to the full Board of Directors regarding which external firm should be proposed to the annual shareholders' meeting for election as auditor and group auditor; assessing the service provided, remuneration and independence of the external auditors and examining the compatibility of audit activities with any consultancy mandates

The Audit Committee regulates and monitors internal auditing. It provides the full Board of Directors with a regular report on its activities and immediately informs the Board of any important matters.

Compensation Committee

The Compensation Committee is composed of three non-executive members of the Board of Directors: Konrad Peter (Chairman), Hanspeter Käser and Hans-Peter Schwald.

The Compensation Committee is responsible for personnel planning for the Executive Board and submitting nominations for vacant posts at this level to the full Board of Directors.

The Committee is also charged with proposing the compensation package for the members of the Board of Directors, determining remuneration policy for the members of the Executive Board and approving the emoluments of the members of the Executive Board. The

Compensation Committee meets at least once a year.

Information and controlling tools in relation to the Executive Board

The Management Information System (MIS) of the RUAG Group is structured as follows: The subsidiaries' balance sheet, income statement and cash flow statement are compiled on a monthly, quarterly, semi-annual and annual basis. This information is consolidated for the various divisions and for the group as a whole and compared to the budget. The budget, which represents the first year of a four-year plan for each subsidiary, is examined in the form of a feasibility forecast based on quarterly results.

The Chief Executive Officer provides the Board of Directors with a monthly written report on budget compliance.

Executive Board

Management organization

The Board of Directors has appointed an Executive Board under the chairmanship of the Chief Executive Officer. Its powers and duties are set out in the Regulations Governing Organization and Operations and in the description of the functions of the Chief Executive Officer. The Divisional Heads report to the Chief Executive Officer, who is responsible for overall management and cross-divisional cooperation.

The CEO, Divisional Heads, Head of Group Services, Chief Financial Officer and Head of Human Resources sit on the Executive Board (9 members).

Chief Executive Officer

The Chief Executive Officer manages the RUAG Group. He submits the RUAG Group's strategy, long- and medium-term objectives and management guidelines to the full Board of Directors for their approval.

At the proposal of the Chief Executive Officer, the full Board of Directors decides the four-year corporate plan, annual budget, individual projects, individual and consolidated financial statements and human resources issues. At the request of the Chief Executive Officer, the Compensation Committee reviews the remuneration of the members of the Executive Board as well as insurance issues.

The Chief Executive Officer regularly provides reports to the Board of Directors on business performance, anticipated business matters and risks, and also changes at the more junior management level. The members of the Board of Directors may request and examine additional information. The Chief Executive Officer must inform the Chairman without delay of any significant unexpected developments.

The Chief Executive Officer regularly monitors whether the Articles of Association or the regulations and signatory powers issued by the Board of Directors require amendment and applies for such amendments to be made.

Members of the Executive Board

The list on page 11 provides information on the name, age, position and date of appointment of each member of the Executive Board.



Management contracts

No management contracts have been concluded by RUAG Holding and its subsidiaries with any third parties.

Compensation, profit-sharing and loans

Compensation and compensation policies

The members of the Board of Directors receive remuneration for their services as proposed from time to time by the Compensation Committee, submitted to the full Board of Directors for approval and ratified by the annual shareholders' meeting.

The Chief Executive Officer and Executive Board of the RUAG Group are compensated according to their performance. Their compensation consists of a fixed and a variable component. Employer contributions to pension funds are also taken into account. The variable component comprises between 0 and 50% of the fixed component and is based on the achievement of various measurable, individually agreed goals. Goals are defined annually and in advance. At the request of the Chief Executive Officer, the Compensation Committee approves the remuneration of the members of the Executive Board.

There are no profit-sharing schemes that allow for the purchase of shares or stock options.

Compensation for incumbent company officers

The overall emoluments (excluding employer contributions to statutory retirement and survivors' insurance) paid

to non-executive members of the Board of Directors in the 2006 financial year amounted to CHF 0.45 million (previous year: CHF 0.45 million).

The overall emoluments (including all employer contributions to pension funds, excluding employer contributions to statutory retirement and survivors' insurance or similar state social insurance contributions) paid to the executive member of the Board of Directors and the other members of the Executive Board for the 2006 financial year amounted to CHF 3.87 million (previous year: 3.28 million).

In the 2006 financial year, no severance compensation was paid to non-executive members of the Board of Directors or members of the Executive Board having terminated their function with the company.

Maximum overall compensation

The highest total compensation (including all employer contributions to pension funds, excluding employer contributions to statutory retirement and survivors' insurance) paid to the executive member of the Board of Directors for the 2006 financial year was CHF 0.76 million (previous year: CHF 0.65 million).

Compensation for former company officers

No compensation was paid during the financial year to non-executive members of the Board of Directors or members of the Executive Board having departed during the financial year, the prior-year period or previous to that after the departure of such members.

Additional fees and remuneration

During the 2006 financial year, the members of the Board of Directors and Executive Board and/or related parties received no appreciable fees or other remuneration for additional services provided to RUAG Holding or one of its subsidiaries.

Loans to members of governing bodies

The members of the Board of Directors or Executive Board and/or related parties are not, or were not, involved in transactions outside the normal business activities of RUAG Holding or one of its subsidiaries, or in any other transactions which are in some shape or form unusual yet material for RUAG Holding, during the current or preceding financial year.

As at 31 December 2006, RUAG Holding and its subsidiaries had not provided any securities, loans, advances or credits to the members of the Board of Directors or Executive Board and/or related parties.

Capital structure

The share capital of RUAG Holding amounts to CHF 340,000,000, comprising 340,000 fully paid-up registered shares, each with a par value of CHF 1,000. As at 31.12.06, RUAG Holding did not have any conditional or authorized capital, nor had it issued participation or dividend-right certificates. The registered shares of RUAG Holding are not listed.

Changes to capital in the last three financial years

No changes to capital were decided.

Shares

Each registered share carries one vote at general meetings of shareholders of RUAG Holding. The voting right may only be exercised if the shareholder is registered in the RUAG Holding share register as a shareholder with voting rights. The registered shares carry full dividend entitlement.

Share register

The Board of Directors keeps a register of shareholders.

Shareholder structure

Shareholders

The Swiss Confederation owns 100% of the share capital and all the voting rights in RUAG Holding. The Federal Department of Defence, Civil Protection and Sports represents shareholder interests of the Swiss Confederation pursuant to the Federal Act on State-Owned Armaments Companies, art. 3, section 2.

Owner's strategy of the Federal Council

The owner's strategy of the Federal Council establishes the transparent, binding framework which enables RUAG Holding and its subsidiaries to fulfil their duties on a commercial basis while taking account of broader interests. The owner's strategy is anchored in the Articles of Association of RUAG Holding.

In its owner's strategy the Federal Council lays down strategic objectives in the interest of Swiss national defence, expectations regarding cooperation and joint undertakings as well as human

resources policy and financial objectives.

The Federal Council amended certain points of the owner's strategy and extended its validity to 2006 in November 2002.

Swiss Confederation representation on the Board of Directors

In addition to the representative of the Department of Defence, Civil Protection and Sports (post currently held by Jakob Baumann), a representative of the Federal Finance Administration (post currently held by Peter Saurer) sits on the Board of Directors of RUAG Holding.

Cross-shareholdings

The RUAG Group has not entered into any cross-shareholdings with other companies, either in terms of capital or votes.

Codetermination rights of shareholders

Voting right restrictions and representation

Each registered share carries one vote at general meetings of shareholders of RUAG Holding. A shareholder may be represented by another shareholder only by written proxy.

Statutory quorums

The following resolutions are subject to decision by statutory quorums in accordance with the Swiss Code of Obligations (art. 704):

- Changes to the purpose of the company

- Introduction of voting shares
- Restrictions on the transferability of registered shares
- Approved or conditional capital increase
- Capital increase out of equity in consideration of a contribution in kind or for the purpose of acquisition in kind and the granting of special benefits
- Restriction or abolition of subscription rights
- Relocation of the company's registered office
- Dissolution of the company without liquidation

Convening and setting the agenda of annual shareholders' meetings

The annual shareholders' meeting is convened and its agenda set in accordance with statutory provisions.

Change in control and defensive measures

Obligatory offer for sale

The Articles of Association contain no provisions concerning opting-out and opting-up in accordance with the Federal Act on Stock Exchanges and Securities Trading (SESTA art. 22).

Change in control clauses

Under the terms of the Federal Act on State-Owned Armaments Companies, any disposal of the capital or voting majority of the Swiss Confederation to

third parties requires the approval of the Federal Assembly. Otherwise there are no specific clauses concerning a change in control of RUAG Holding.

Auditors

Duration of mandate and term of office for lead auditor

PricewaterhouseCoopers AG, Berne, have been auditors to RUAG Holding since 1999 and Group auditors to the RUAG Group since 1999.

The lead auditor has been responsible for the audit mandate for both RUAG Holding and the RUAG Group since 2000.

Audit fees and additional expenses

In the 2006 financial year, PricewaterhouseCoopers billed the RUAG Group CHF 0.8 million (previous year: CHF 0.8 million) for its services in connection with the auditing of the annual accounts of RUAG Holding and the Group companies as well as the auditing of the consolidated financial statements of the RUAG Group.

In addition, PricewaterhouseCoopers billed the RUAG Group CHF 0.3 million (previous year: CHF 0.3 million) in respect of audit-related services, management consultancy, tax advisory and due diligence services as well as other auditing services related to internal auditing.

Supervisory and controlling tools in relation to auditing

The Audit Committee of the Board of Directors evaluates the performance,

fees and independence of the auditors and of the Group auditor on an annual basis and submits to the Board of Directors a proposal as to which external auditor should be recommended to the annual shareholders' meeting for appointment. The Audit Committee then monitors on an annual basis the scope of external auditing, the auditing plans and the relevant processes and in each case discusses the audit results with the external auditors.

Information policy

The RUAG Group pursues an open information policy in relation to the public and to the financial markets. The published figures extend beyond the statutory requirements in terms of transparency.



Forward-looking services for business and special-mission aircraft

Worldwide developments in the aviation market show growing demand for business, executive and special-mission aircraft with an integrated package of services that includes fleet management. During the year under review RUAG combined its various service locations in Switzerland and Germany into one business unit. This provides customers with one-stop shopping for a broader range of products and services.

Starting with the acquisition of business components in Oberpfaffenhofen, Germany, supplementing already established RUAG service locations in Berne, Zurich and Lugano, the company has had the aim of creating a civil aviation service group since 2002. The initial major goal was to create a licensed aviation organization and stabilize business based on existing contracts and customers.

A contact point for customers

Integration was initiated in 2006. The process will be completed during the next financial year. In line with the market, all civil aircraft service activities have already been gathered into the Aircraft Services business unit.

The Oberpfaffenhofen location near Munich serves as the main base of the Aircraft Services Network (ASN). From here, in cooperation with the service stations in Switzerland and Germany, customers receive comprehensive service in accordance on the principle of "One face to the customer".

Positioned in the high-quality range

Current market developments show strong demand for business, executive

and special-mission aircraft with an integrated package of services that includes fleet management. RUAG intends to meet this demand and become a "premium quality service provider". The Aircraft Services business unit strategy developed in 2006 pursues this aim. RUAG today services the European market, the Middle East and parts of Asia. Customers mainly include operators of business and executive aircraft, airlines and operators of special-mission aircraft.

Oberpfaffenhofen has traditionally provided services for public-sector clients in Germany. In addition to comprehensive services as a civil and military maintenance provider, the main technologically interesting and innovative focus is on systems integration and development, outfitting and support for mission aircraft.

Three civil aviation projects provide a good example of activities in this area:

HALO (High Altitude and Long Range Research Aircraft): A Gulfstream G550 is being refitted with technology for atmospheric research work in cooperation with the manufacturer. The German Aerospace Centre (DLR) will deploy HALO for research flights around the globe from Oberpfaffenhofen airport starting in 2008.

Dornier 228 Kustwacht: Next year two extensively modified Dornier 228-212s will be deployed as maritime surveillance aircraft for the Netherlands Coastguard. The planes will be outfitted with high-tech mission equipment and a digital cockpit featuring the latest communications technology.

Embraer maintenance: A centre of excellence is being set up in Switzerland to maintain business and regional aircraft produced by Brazilian manufacturer Embraer.

The Oberpfaffenhofen Aircraft Services Network platform will be further expanded in 2007 and grow into the market leadership position. The foundation has been laid and the path forward is clear.

Innovative technology transition in metalworking

Over a period of just a few years, RUAG Components has evolved from a contract manufacturer into a specialized industrial partner. One example is the successful technology transition undertaken for the key “metroframe” product, a precision component used in the semiconductor industry.

RUAG has been producing metroframes – high-precision machine frames – for a manufacturer of lithographic systems used in microchip production since 2000. These systems are successfully marketed worldwide.

From Invar to aluminium

The machine frame was initially made of individual Invar pieces welded together and then machined. Invar is the name given to a group of metal alloys that possess special properties. Invar alloys have a wide range of uses in industry in applications where low thermal expansion is needed.

Developer team seeks new solution

When sales of the lithographic systems declined in 2003 due to the economic slump, a team of developers, designers and materials specialists looked for savings potential with a view to bringing a new, more cost-effective generation of systems to market. Various materials were considered for the metroframe, but it was finally decided to use aluminium. RUAG was able to put the experience it had gained in the working of aluminium components to good use. First a functional model was built for tests, then a prototype. Series production began about one year after the decision to change materials and technologies.

The metroframes are precision-milled from aluminium blocks weighing 3,600 kilograms and measuring a respectable 440x1400x2200 mm. After that, over 1000 precision holes are drilled and each piece is anodized by a specialist.

Benefits of technology change

The benefits of the technology change are clear: 150 individual pieces no longer need to be welded together, a potential source of defects has been eliminated and production time has been reduced. To meet the stringent precision machining requirements for this product, RUAG has invested substantially in its machine base. The production hall and measuring room, with its latest-generation measuring system, are fully air-conditioned to ensure that the strict tolerances are met. Production is highly automated using a transfer system. The willingness to innovate and invest in this technology transition is illustrative of RUAG’s versatility in transforming itself.

One-stop shopping for simulation-supported training

The Swiss Armed Forces plan to commission four complete simulation-supported combat training centres by 2011. During the first stages of implementation, industrial partner RUAG has proven its effectiveness.

The origins of training with live simulators go back to the early 1980s and the introduction of the first laser shooting simulators. Some ten years ago a major step towards combat training using live simulators was taken with the launch of the SIMUG project. RUAG was awarded the contract to develop and manufacture a core system that was delivered and made available to the troops in 2001.

New training options

By realistically portraying factual circumstances and processes using simulation systems, exercises can be made reproducible, more interesting and more diverse. Moreover, these exercises can be carried out in controllable environments. For example, laser-based shooting simulators can replace live ammunition, a key requirement for combat exercises involving live participants on both sides.

Combat training centres with integrated weapon simulators enable all participating units to be trained on all weapons without firing a single real shot. This greatly reduces ammunition costs and minimizes impacts on the natural and human environment. Especially for military operations in urban terrain, realistic and high-quality training is indispensable for combat readiness. Simulators optimized for specific training goals greatly improve the value of the training.

RUAG as industrial partner

For RUAG to be able to develop and supply training solutions that meet the users' expectations, it must not only have a command of the relevant technologies, but also an accurate understanding of the training goals to be achieved. Close cooperation between users and industry make it possible to integrate the technologies in such a way that the high expectations placed on training can be effectively met.

The training systems and solutions produced by RUAG, especially the simulators and simulation platforms developed for and supplied to the Swiss Armed Forces' combat training centres, are the outcome of a fruitful collaboration between military and industry.

Step-by-step development

Since its first step with the core SIMUG system, the Swiss Armed Forces have been systematically expanding their use of live simulations. Further significant steps have included the order for laser firing simulators for the "Schützenpanzer 2000" infantry fighting vehicle and "Radschützenpanzer 93" light armoured vehicle between 2001 and 2006. After two years of development, delivery of the SIM KIUG core system in 2006 was a further milestone. This system complements SIMUG and is used for simulation-supported training in urban combat. RUAG was subsequently engaged to develop the system further in order to equip two complete installations.

While the core SIMUG system was proving its capabilities over several years of active use by the troops, intensive work continued to ready the system for series



production. This work was successfully completed during the year under review. It was followed by an order to supply two standard-production installations for the Bure and Walenstadt/St. Luzisteig sites. These installations, each designed for combat training of two opposing reinforced companies (with up to 600 participating soldiers and 70 combat vehicles), will be delivered and made available to the troops in 2009 and 2010.

Based on RUAG's "traditional" maintenance of the simulators, a model of efficient training support was developed in collaboration with participating partners from the Swiss Armed Forces. As a result, the RUAG Training Support Com-

bat Training Centre (RTS GAZ) will commence operations in early 2007. This pilot project will lay the groundwork for efficient support of the troops involved in the exercises, who will have two training centres for open terrain and two training centres for urban terrain as of 2012. Thanks to its experience in the development and manufacture of laser firing simulators, the integration of simulators in total combat training centres as well as training support for complete facilities, RUAG offers its customers one-stop shopping for end-to-end solutions. Based on the expertise it has acquired, RUAG has also successfully secured several export contracts. The references from Switzerland strengthen RUAG's international competitive position.

Technology leader in environmentally friendly ammunition

RUAG possesses strong technological expertise in the development of environmentally friendly small calibre ammunition, based on profound knowledge and many years of experience in explosives chemistry and lead-free alternative materials.

Over 25 years ago, it became a priority to develop ammunition technology that would reduce heavy metal emissions in closed police firing ranges so that marksmanship instructors would be protected against heavy metal (lead, barium and antimony) dust from shooting. The heavy-metal-free, low-pollutant SINTOX ignition element was brought to market in 1980 and remains the

undisputed market leader today. After observing the police's positive experience with low-pollutant ammunition, the German Bundeswehr, concerned for the health of its soldiers, adopted a directive in 1990 requiring the procurement of low-pollutant versions of all infantry ammunition. Only RUAG Ammotec technology has been approved by the Bundeswehr for all infantry ammunition. The 9 mm and 5.56 mm combat rounds subsequently became the first low-pollutant cartridges qualified by NATO, i.e. this ammunition is interchangeable within NATO.

Completely lead-free

A further major milestone was achieved

in 1990, when the Dutch police deployed fully lead-free ammunition in a police-issue brass projectile together with the low-pollutant ignition element. RUAG has produced a total of two billion low-pollutant cartridges for government agencies and military forces since 1980, underlining the importance of this technology for RUAG's small calibre ammunition division.

Environmental agencies in some European countries today require the use of lead-free projectiles to prevent further contamination on military firing ranges. RUAG Ammotec was a pioneer in launching a development project in this area and now offers Green Power Technology cartridges for the military market.

Lead-free solutions for hunting

Environmentally friendly ammunition for hunting has to satisfy a completely different set of requirements to its military and police counterpart. The aim is to avoid contaminating wetlands with lead shot from the buckshot cartridges used to hunt waterfowl. Thus alternative materials have been developed to replace lead. Soft iron has been available for shot for many years. However, its use entails certain compromises for hunters as its shooting performance is inferior. To overcome this disadvantage in comparison to conventional lead shot, other alternative materials with shooting properties similar to lead are being tested. These new forms of ammunition are already appearing on the market.

Demands for lead-free ammunition are also becoming louder in hunting for hoofed game, such as roe deer, chamois

and red deer, to ensure that human and animal food chains are kept free of heavy metals such as lead, barium and antimony. Shooting hoofed game with lead-core projectiles can lead to excessive lead contamination of the meat. Researchers and the government agencies have not yet defined a safe ceiling for such contamination.

Regardless of whether a final ruling mandating lead-free hunting ammunition is ever adopted, RUAG, as Europe's leading producer of hunting cartridges, has a certain obligation to the market to offer lead-free alternatives. Thus development of lead-free hunting cartridges has been a high priority. After extensive testing with different kinds of game at various hunting grounds, two lead-free projectile options have been brought to market.

A broad offering

RUAG offers a broad range of high-quality, environmentally friendly ammunition with low-pollutant ignition and lead-free projectiles for its various target markets. It continues to monitor this special market segment, where demands for environmentally friendly ammunition for sport shooting are bound to start appearing soon as well.







Expertise in effective protection

For many years RUAG has been successfully carrying out research and development in the field of modular protection systems. These systems are used to protect vehicles and installations from current threats. RUAG's capabilities are underscored by international sales successes.

Experience from crisis areas shows that the easy availability of weapons makes combat vehicles and fixed security installations – and with them soldiers in action – especially vulnerable to attack in built-up areas. Ambush attacks in urban areas frequently target vehicles' weak points and installations. The threat is not limited to lightweight systems such as armoured all-wheel-drive vehicles, but extends to heavy tracked vehicles such as armoured personnel carriers and main battle tanks. High-performance protection systems are needed to prevent devastating effects on systems and personnel. Countries that send troops on international missions are no longer willing to accept losses among their own forces, so there is growing investment in effective force protection.

From concept to product

RUAG Land Systems designs and produces protective equipment that meets the high standards required. Since conventional passive armour made of layers of metal or composite materials rapidly runs into weight limitations, today's solution lies with reactive or active protective measures used by themselves or in combination.

Whereas reactive armour drastically reduces the impact effects of incoming fire by energy counteraction, active pro-

tection counters incoming projectiles by disabling their guidance systems or payloads.

RUAG also offers solutions that protect against electromagnetic interference from within and without. Installations that have been enhanced with these systems can continue to function flawlessly even after NEMP incidents and focused high-power microwave attacks.

International cooperation in R&D

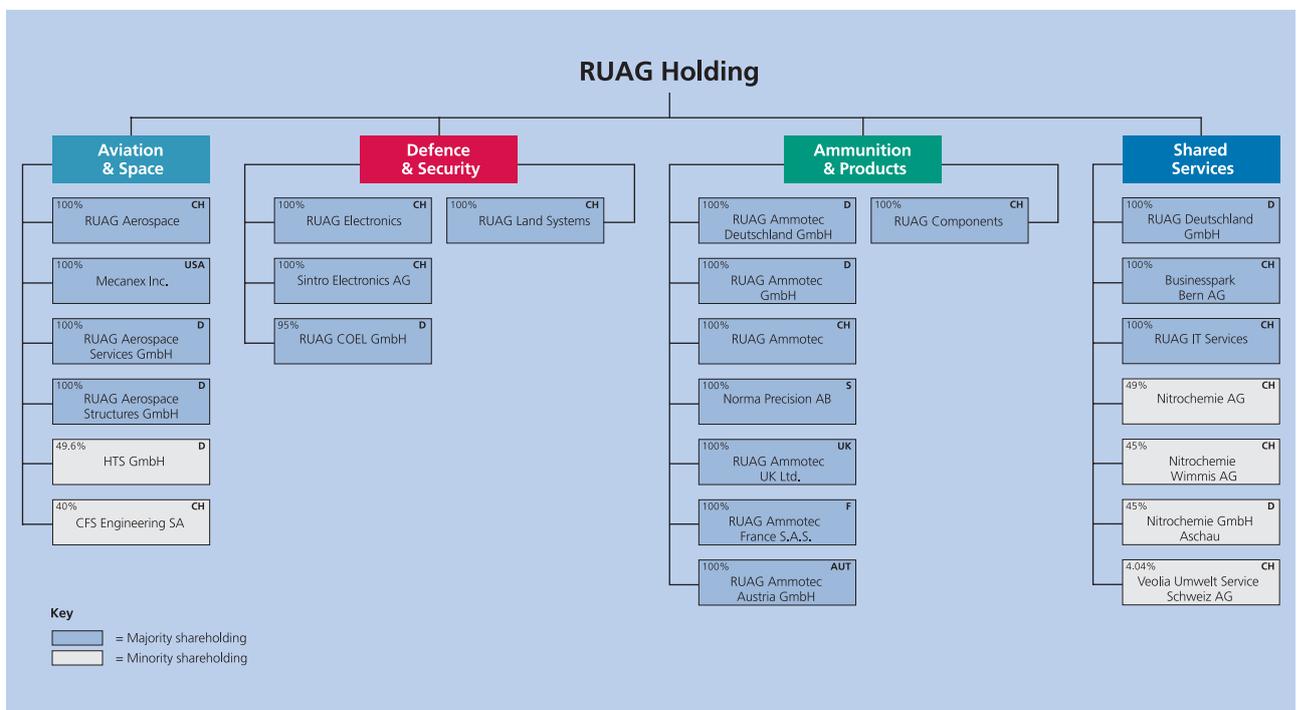
Given the need for interdisciplinary refinement of technical systems optimized for the market, RUAG relies on international cooperation in research and development (R&D) for efficient implementation of new protection technologies. Its existing broad technological expertise serves as a catalyst for this sort of cooperation. By continually expanding our knowledge and deploying new technologies, we keep pace with developments – to the benefit of our customers.

Financial year-end:	31.12.2006
Announcement of annual results:	23.03.2007
Publication of Annual Report:	23.03.2007
Annual shareholders' meeting:	02.05.2007

The Annual Report containing the annual financial statements for the year ended 31 December 2006 is sent to shareholders together with an invitation to the annual shareholders' meeting.

Current Annual Reports and press releases can be found at www.ruag.com. Media conferences are held at least once a year.

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