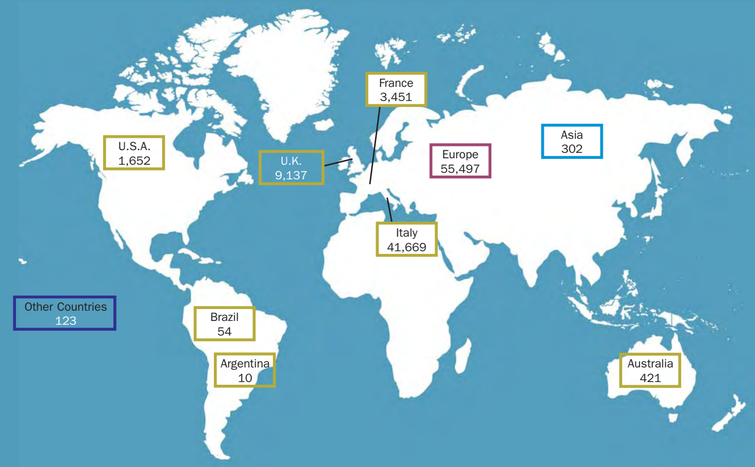
CONTENTS

2006 CONSOLIDATED FINANCIAL STATEMENTS






	HELICOPTERS	AERONAUTICS	SPACE	DEFENCE ELECTRONICS AND SECURITY	DEFENCE SYSTEMS	ENERGY AND TRANSPORT
Companies Owned Companies Joint venture	AgustaWestland BAAC	Alenia Aeronautica Alenia Aermacchi Alenia Aeronavali ATR Global Military Aircraft Systems Global Aeronautica	Telespazio Thales Alenia Space	Selex Communications Selex Sensors and Airborne Systems Galileo Avionica Selex Sistemi Integrati Selex Service Management Elsag Datamat Seicos Orizzonte Reles	Oto Melara WASS MBDA	Ansaldo Energia AnsaldoBreda Ansaldo STS
Activities	Finmeccanica is a world leader in the helicopter industry, with the design and development of helicopters and tiltrotors for civil and military use. Finmeccanica operates in this field through its subsidiary company AgustaWestland. AgustaWestland boasts the technology required to undertake every phase of a helicopter, from the preliminary analysis and definition of operational requirements to the design, development and production of transmissions, rotors, metal and composite structures and avionics systems, as well as their integration into a complete "helicopter system"	Finmeccanica is a cutting-edge manufacturer of tactical transport and combat aircraft, occupies a leading position among the independent suppliers of aerostructures, produces unmanned aircraft for civil and military use and also carries out aircraft conversion and refurbishment for the world's major producers. Thanks to the acquisition of Alenia Aermacchi, Finmeccanica has expanded its product range to include trainer aircraft and ground support services. The global excellence achieved in this sector enables the Company to meet the most stringent requirements of the international armed forces.	Via its agreements with the French company, Alcatel, Finmeccanica has created Europe's leading operator in the space sector in the form of two joint ventures operating in satellite construction and satellite services management. In April 2007, the European Commission approved the transfer to the French company Thales of Alcatel-Lucent's interests in the joint ventures Alcatel Alenia Space and Telespazio. The new space alliance with Thales marked the achievement of a milestone in the European space sector. Finmeccanica has a long tradition of excellence in the space arena and has achieved a world-leading position in the design, development and manufacture of satellites for any civil and military use.	An integrated business was created following agreements with BAE Systems, comprising three companies: Selex Sensors and Airborne Systems, Selex Communications and Selex Sistemi Integrati operating in avionics, military and secure communications, and command and control systems respectively. In March 2007, Finmeccanica acquired 25% of Selex Sensors and Airborne Systems from BAE Systems, thereby gaining 100% control of the company. To this must be added Elsag, which focuses on security, and the recently acquired Datamat. The two companies have been merged into one company named Elsag Datamat. As a result of this new structure, Finmeccanica has become the second-largest European operator and the sixth in the world.	Finmeccanica is a recognised technology leader in the design, development and production of missile systems, torpedoes, naval artillery and armoured vehicles. Finmeccanica is active in the field both through the MBDA joint venture, the major European missile systems company, and its wholly owned subsidiaries Oto Melara and WASS, each of which is a leader in its field.	**Energy:** Finmeccanica has strong competences and a sound market position in the energy sector. In this business, Finmeccanica designs, develops and manufactures parts and systems for energy generation, as well as providing services. **Transport:** Finmeccanica also has strong expertise in the rail transport business, which in the last two years has achieved significant market success and a major improvement in results. The Company operates in the design, development and manufacture of rolling stock, rail signalling systems and complete urban transport systems. 2006 saw the creation of Ansaldo STS as a result of the merger of Ansaldo Signal and Ansaldo Trasporti e Sistemi Ferroviari. The new company was listed on the stock market at the end of March.
Orders	4,088	2,634	851	4,197	1,111	**Energy:** 1,050 **Transport:** 2,127
Order backlog	8,572	7,538	1,264	7,676	4,252	**Energy:** 2,468 **Transport:** 4,703
Revenues 2006	22%	15%	6%	29%	9%	Energy: 8% Transport: 11% 19%



Finmeccanica Group staff in the world

DEFENCE ELECTRONICS AND SECURITY	DEFENCE SYSTEMS	ENERGY AND TRANSPORT
Selex Communications Selex Sensors and Airborne Systems Galileo Avionica Selex Sistemi Integrati Selex Service Management Elsag Datamat Seicos Orizzonte Reles	Oto Melara WASS MBDA	Ansaldo Energia AnsaldoBreda Ansaldo STS
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7,676	4,252	**Energy:** 2,468 **Transport:** 4,703
29%	9%	**Energy:** 8% **Transport:** 11% 19%

Dear Shareholders,

In 2006, Finmeccanica met its business objectives, obtaining results that were better than both those forecast and those achieved the previous year.
Finmeccanica's performance was in line with its established strategic objectives: thanks to organic growth, revenues rose from €10.9 billion in 2005 to €12.5 billion in 2006, and the Company placed a greater focus on its core businesses of aerospace, defence and security, which alone now represent around 80% of revenues and over 90% of the Group's EBIT.

The size of the proposed dividend and its increase over past dividends is based on the growth in EBIT achieved in recent years, and is compatible with the cash flow generated in 2006 from normal operations.
An additional allocation was made to reserves for the purposes of consolidating the Company's assets and to support a dividend policy that aims to provide continuity in dividends paid to Shareholders.
Over the last year, Finmeccanica has consolidated its position on the international market, increased investment in R&D (14% of revenues) and created value for the Company and its Shareholders.
As part of its strategic positioning, it acquired the avionics segment of BAE Systems and consolidated 100% of Datamat, which was merged into Elsag Datamat.
Furthermore, in the space sector, Thales replaced Alcatel in the joint ventures Thales Alenia Space and Telespazio, to form the nucleus of the new Space Alliance with the French group.
The gradual reduction of the national defence budget makes it imperative that Finmeccanica strengthens its international presence: after consolidating our position on the domestic markets (Italy and the UK), we

therefore pursued a strategy to penetrate the important US market, based on alliances with American partners and direct approaches. In addition, we intensified our commercial operations on the large international markets (Russia, India and China) through co-operation agreements with local partners, as well as on rising markets (Greece, Malaysia, Turkey and Eastern Europe), leveraging the success we have already achieved, and finally on markets with high growth potential (UAE, Japan, South Korea, Saudi Arabia, Singapore and Algeria).

Our success stems from an awareness of the excellence of our products and recognition of their qualities on foreign markets. Our accomplishments in the helicopters, aeronautics, space, avionics, large systems, energy and transport businesses bear witness to our technological expertise and are just reward for our decision to invest in technological innovation and staff training. This is also borne out by Finmeccanica's involvement in big international aeronautics programmes, including Airbus, and partnerships with the biggest US companies, notable among which is our participation with Boeing in the B787 programme, the biggest success in the history of commercial aviation.

From now until 2008 we expect to receive many high-quality orders, and diversify our international portfolio even further. Another of the management's objectives is to increase our critical mass.

The tools for growth must be based on skills and competence in: 1) managing large contracts using appropriate operational mechanisms that can control delivery times, costs and quality; 2) continually reducing production costs; 3) providing integrated solutions that leverage the Group's synergies; 4) entering new markets via local industrial initiatives and partnerships with domestic operators; 5) applying innovative product technologies and managing innovation risks.

Going forward, our objectives are to continue along our path of organic growth both in terms of revenues and profitability; to pursue external growth by means of selective asset acquisitions and to extract further value from our activities.

Finmeccanica's strength is in the men and women who contribute to our success on a daily basis in Italy, Europe and the rest of the world. The efforts of these 60,000 people, working together, are our greatest resource and inspire us to continually strive for synergies and crossovers between our companies within a framework of unity and the value of belonging to a large international organisation.

The challenges we will face in the future are extraordinarily complex. Our optimism, however, is based on firm foundations: our expertise and capabilities, as well as our Group culture and international vision. These will enable us together to meet our clients' and Shareholders' expectations, and satisfy the ambitions of Finmeccanica's companies and employees.

FOR THE BOARD OF DIRECTORS
The Chairman and Chief Executive Officer
Pier Francesco Guarguaglini

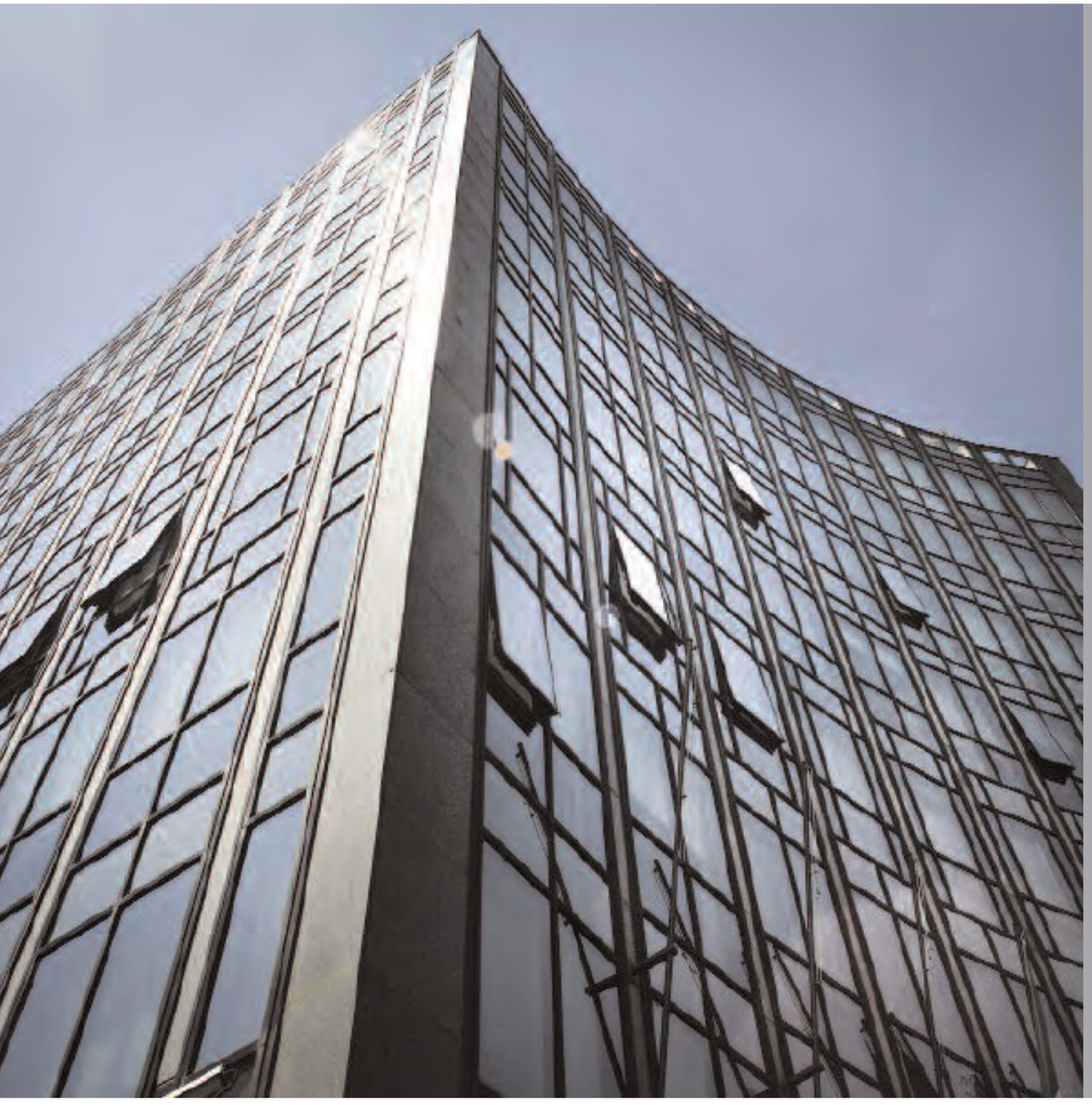
(1) Member of the Strategy Committee

(2) Member of the Internal Auditing Committee

(3) Member of the Remuneration Committee

(*) Appointed by the Board of Directors' Meeting of 27 March 2007 in accordance with Art. 2386 of the Civ. Code and by the Shareholders' Meeting of 30 May 2007

(**) Director without voting rights appointed with Ministerial Decree pursuant to Decree Law 332/94 ratified with amendments by Law 474/94



BOARD OF DIRECTORS
(for the 2005-2007 term)
appointed by the Shareholders' Meeting
of 12 July 2005

PIER FRANCESCO GUARGUAGLINI (1)
Chairman/Chief Executive Officer

PIERGIORGIO ALBERTI (2) (3)
Director

FILIPPO ANDREATTA (1)
Director (*)

FRANCO BONFERRONI (2) (3)
Director

GIOVANNI CASTELLANETA (1)
Director (since 22 July 2005) (**)

MAURIZIO DE TILLA (2)
Director

GIAN LUIGI LOMBARDI CERRI (2)
Director

ROBERTO PETRI (1)
Director

DARIO SCANNAPIECO (1) (3)
Director

RICCARDO VARALDO (3)
Director

GUIDO VENTURONI (1)
Director

PAOLO VIGEVANO (1)
Director

ERNESTO MONTI (2) (3)
Director
(suspended by Board resolution of 19 January 2007;
resigned as of 28 February 2007)

BOARD OF AUDITORS
(through 23 May 2006)

DOMENICO PIACENZA
Chairman

GIORGIO CUMIN, FRANCESCO FORCHIELLI, LUIGI GASPARI, ANTONIO TAMBORRINO
Auditors

GAETANO DE GREGORIO, PIERO SANTONI
Alternate Auditors

BOARD OF AUDITORS
(for the 2006-2008 term)
appointed by the Shareholders' Meeting
of 23 May 2006

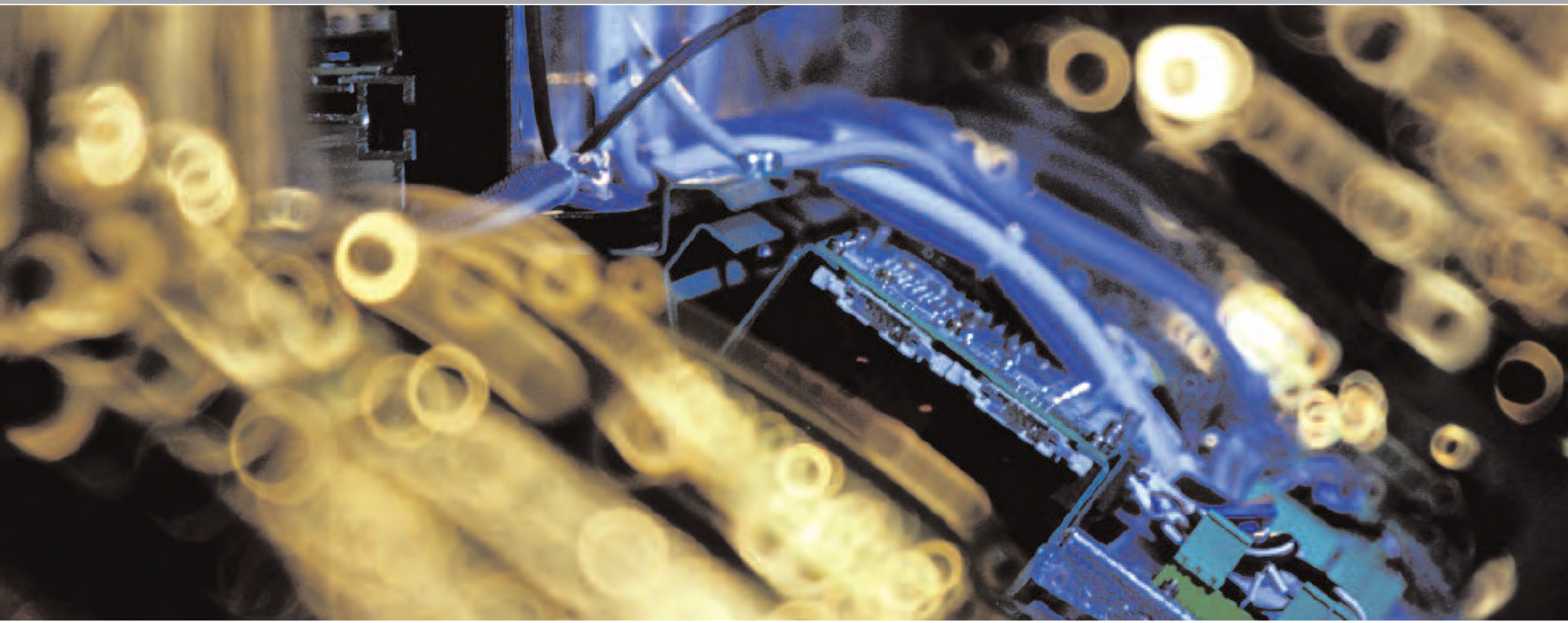
LUIGI GASPARI
Chairman

GIORGIO CUMIN, FRANCESCO FORCHIELLI, SILVANO MONTALDO, ANTONIO TAMBORRINO
Auditors

MAURIZIO DATTILO, PIERO SANTONI
Alternate Auditors

LUCIANO ACCIARI
Secretary of the Board of Directors

INDEPENDENT AUDITORS
(for the 2006-2011 term)
PRICEWATERHOUSECOOPERS S.p.A.



Report on Operations at 31 December 2006

The 2006 consolidated financial statements closed with a net profit of €mil. 1,020 (€mil. 396 in 2005), an EBIT of €mil. 878 (€mil. 735 in 2005), revenues of €mil. 12,472 (€mil. 10,952 in 2005), shareholders' equity of €mil. 5,357 (€mil. 4,598 in 2005) and net financial debt of €mil. 858 (€mil. 1,100 in 2005).
These significant results were achieved thanks to increasing focus on sales activities, contract management, development costs and several important extraordinary transactions:
following a review of the primary industrial and financial operations conducted by the Group during the year, this report will analyse the consolidated results achieved. The consolidated results will be broken down by the individual divisions in which the Group operates, ending with a review of the strategic, commercial, manufacturing and financial variables that characterised the business areas in 2006.
After describing research and development projects, human resource management initiatives undertaken and the Group's corporate governance principles, the focus of this report will shift to the outlook for the future.
Finally, the analysis of the accounting standards and notes to the financial statements provide indispensable aid in scrutinizing the Group's performance in 2006.

1. Significant events in 2006 and events subsequent to closure of the accounts for the period

Industrial transactions

Helicopters. Agusta Westland signed an agreement on 28 February 2006 with the British company Sloane Helicopters Ltd to distribute civilian helicopters on the UK and Republic of Ireland markets. The agreement with Sloane Helicopters will further consolidate Agusta Westland's position in the UK light, bi-turbine helicopter market for VIP and Corporate use. It will also pave the way for further growth in the emergency medical services and law enforcement markets.

Defence Electronics. The early months of 2006 saw the completion of the acquisition of 100% of Datamat S.p.A., an Italian company that develops and designs air and naval mission systems and integrated solutions in the defence, space, government, healthcare, banking, finance and telecommunications sectors.
In the previous year, Finmeccanica S.p.A. had initially acquired 52.7% of Datamat S.p.A.for around €mil. 151. An obligatory public offering was subsequently launched for the remaining Datamat shares available, at a price of €9.65 per share, which was completed for a total value of about €mil. 89. After the offering, completed in the first few days of 2006, Finmeccanica held around 89% of the share capital of Datamat S.p.A., including treasury shares already held by the Company. On 1 March 2006, the Finmeccanica Board of Directors decided to begin the process of delisting Datamat shares by launching a residual public tender in accordance with Article 108 of Legislative Decree 58/1998 once the statutory percentage holding had been reached. On 12 June 2006, Finmeccanica completed a series of additional acquisitions of a total of 272,000 ordinary Datamat shares, equal to 0.959% of Datamat's share capital, thus exceeding the 90% necessary to launch the residual offering, at a price per share set by CONSOB (the Italian Securities Regulator) pursuant to Article 108 of the Finance Act.
The price of €9.911 per share was set by CONSOB on 25 October 2006. On 22 November 2006, CONSOB issued approval for the publication of the Offer Document. The residual public offer, completed on 8 January 2007 (the final day for payment), resulted in the purchase of Datamat ordinary shares representing around 7.983% of the share capital, to which are added the ordinary Datamat shares (0.57% of the share capital) purchased for €9.911 per share after the residual public offer. Adding these to the shares already held by Finmeccanica brings the Group's total stake in Datamat to over 98%. In accordance with Article 2.5.1(6) of its Rules of the Market, Borsa Italiana S.p.A. (the Italian Stock Exchange) revoked the listing of ordinary Datamat shares on the MTAX market starting as of 9 January 2007.
Having exceeded the 98% threshold, Finmeccanica will exercise the right to purchase the remaining Datamat shares in a squeeze-out operation pursuant to Article 111 of the Finance Act. The squeeze-out process should be settled within the first ten days of May 2007. For this purpose, on 9 February 2007, at the request of Finmeccanica, the presiding judge of the Court of Rome appointed an expert to determine the price for these remaining shares.
Meanwhile, as indicated in the informational documents related to the obligatory and residual public offerings, the process of merging Elsag and Datamat began, with the aim of ensuring that the two companies are managed on a unitary basis.

With regard to the security segment, the decree of the Minister for the Economy and Finance setting the price for the **Electronic ID Card** was published in Gazzetta Ufficiale no. 61 on 14 March 2007. This marked the start of a nation-wide project to develop a tool for reliability recognising citizens, permitting them to prove their identities unambiguously and with certainty in order to access high added-value services. Finmeccanica, through its subsidiary Selex Service Management S.p.A., together with the Istituto Poligrafico e Zecca dello Stato S.p.A. (70%) and Poste Italiane S.p.A (15%), holds a 15% stake in the Innovazione e Progetti consortium that will be responsible for developing the programme, acting as the consortium's technological and industrial expert, especially with regard to security-related matters.

Aeronautics. On 19 January 2006, Aermacchi S.p.A. (now Alenia Aermacchi S.p.A.) and Hellenic Aerospace Industry (HAI) signed a Memorandum of Understanding governing the terms and conditions of their cooperation on a programme to develop the next generation M346 advanced training aircraft. Under the Memorandum, HAI becomes the prime Greek contractor of the programme and will be responsible for a series of activities, such as the design, manufacture and assembly of major aircraft parts, such as the rear fuselage. In addition, HAI will manage the work of other Greek companies participating in the programme as sub-contractors.

On 27 April 2006, **Alenia Aeronautica** and L-3 Communications signed a Memorandum of Understanding with Boeing Integrated Defense Systems. Under the agreement, Boeing Integrated Defense Systems will participate in the Global Military Aircraft Systems (GMAS) joint venture for C27J aircraft, set up in 2005 to take part in the Joint Cargo Aircraft (JCA) programme for the US Army and Air Force. Boeing will be fully involved in GMAS, including the development of a specific version of the aircraft requested by the US armed forces and, in the event of selection, in manufacturing the C27J in the United States. Boeing's arrival boosts the C27J team, which, in addition to the companies already mentioned, includes leading components and system suppliers such as Dowty, Honeywell, Lockheed Martin and Rolls-Royce.
Furthermore, Boeing Integrated Defense Systems' participation in GMAS could contribute to the development of special versions of the aircraft that satisfy any additional, future requirements of the US armed forces.

Following the preliminary agreement signed in June 2006, **Finmeccanica** and **Sukhoi Aviation Holding** and their respective subsidiaries Alenia Aeronautica and Sukhoi Civil Aircraft Company (SCAC) signed a strategic partnership agreement on 28 November 2006 for the manufacture, marketing and technical support for the SuperJet 100 family of regional jets with capacities of between 75 and 100 seats. Under the agreement, Alenia Aeronautica will purchase a 25% plus one share stake in SCAC which will be responsible for sales activities within the Russian Federation and will form a joint venture with Sukhoi (51% Alenia Aeronautica, 49% Sukhoi) which will be responsible for marketing, sales and delivery in the West, as well as worldwide technical support for the SuperJet 100.

Space. On 19 January 2006 in Berlin, Galileo Industries (now European Satellite Navigation Industries, a company that includes Finmeccanica, EADS Astrium, Thales S.A. and Galileo Sistemas y Servicios) and the European Space Agency (ESA) signed a contract worth around €bil. 1 to develop and build the first four satellites for the European Galileo satellite navigation system and the related earth infrastructure. The Galileo project – the response of the European Union and the ESA to the US Global Positioning System (GPS) – also includes Telespazio S.p.A., a Finmeccanica and Alcatel company, which will supply all services related to satellite launching and orbit placement

and the management of subsequent operations.
In addition to the development of the infrastructure for the building of the Galileo Constellation, Finmeccanica is part of the joint venture created by the merger of two consortiums, Eurely (Finmeccanica S.p.A., Alcatel S.A., AENA and Hispasat) and iNavSat (EADS, Thales and Inmarsat), to negotiate the contract to operate the system. The joint venture is in the process of being incorporated through the formation of a dedicated company that will sign the contract. Finmeccanica's participation in the dedicated company is a golden opportunity for its satellite services business, since it allows the Group to operate as a leading actor in a project of global scope and is particularly strategic for new value-added applications (PRS - public regulated services, infomobility, security, etc.).
A major landmark in the project was reached when Italy was awarded one of the two Constellation and Mission Control Centres and the Performance Evaluation Centre for the new satellite navigation system. In conjunction, Telespazio S.p.A. and the Region of Abruzzo signed an agreement for the construction of the infrastructure to house the Control Centre at the Fucino Space Centre by 2008.
Work is also continuing on the building of the Galileo Test Range (GTR), an advanced technology centre for satellite navigation featuring a technical infrastructure equipped with an environmental control that mimics the primary navigation signals, services and operations characteristics of the Galileo system. In 2005, the Region of Lazio, through Filas S.p.A., awarded the initial construction phase of the GTR to the joint venture in which Telespazio S.p.A (as representative), Alcatel Alenia Space Italia S.p.A. and Finmeccanica S.p.A. (as principals) participate.

Again in the Space segment, in September 2006, **Telespazio**, Telecom Italia, Hughes and Intelsat announced the creation of a new satellite platform called **"Marco Polo"** which will provide value-added broadband services to the business and institutional markets of Eastern Europe and North Africa.
The platform, based on the capacities of the Intelsat IS-901 satellite, will be operated by Telespazio from the Fucino Space Centre. Thanks to this platform, Telecom will be able to complete its range of broadband land and satellite services to users such as institutions, companies, public and private entities.

Defence Systems. In January 2006, MBDA completed its acquisition of LFK GmbH, Germany's leading missile system manufacturer. Announced last year, the acquisition was formalised following approval by the European Commission and the German government. With this operation, MBDA (of which Finmeccanica holds 25%; the other shareholders are BAE Systems and EADS) has further consolidated its global leadership in guided missiles and has taken another step forward in rationalising the European offer in this sector. The merger of the two companies will also increase MBDA's international collaborative relationships in Europe and in transatlantic programmes, as well as boost its overall system and product capacities.

As part of its efforts to leverage its civil activities, the plan to list **Ansaldo STS S.p.A.** (head of a group that comprises Ansaldo Trasporti - Sistemi Ferroviari S.p.A. (ATSF) and Ansaldo Signal N.V.) on the Italian Stock Exchange was completed. On 8 March 2006, CONSOB gave its approval, after Borsa Italiana had agreed to list the company. On 24 March 2006, 52.17% (52,174,000 shares) of the company with institutional and retail investors was placed on the market at a price of €7.80 per share. The first day of trading in the company's shares was 29 March 2006. In the days that followed, the banks that led the placement consortium exercised their greenshoe option to acquire an additional 7,826,000 shares (7.83% of share capital), at a price of €7.80 per share, raising the amount placed to 60%. The stock is listed on the STAR section of Borsa Italiana's electronic stock exchange. The new industrial company will benefit fully from the highly complementary skills of the two companies: ATSF will enjoy greater opportunities to penetrate foreign markets, thanks to the commercial network and international profile of Ansaldo Signal, a global leader in the railway signalling sector, while Ansaldo Signal will increase its ability to compete with integrated systems, thanks to ATSF's design and system specialisations.

In July 2006 **Ansaldo Energia**, a company of the Group operating in the supply of components and services for **Energy Generation**, acquired full control of Swiss company **Energy Service Group Ltd (ESG),** which provides on-site plant maintenance and repair services. In September 2006 Ansaldo Energia also acquired from the US company Calpine European Finance 100% of the shares in **Thomassen Turbine Systems B.V.,** a Dutch company specialising in the gas and turbines service sector. These two transactions, closely related with one another, are part of the process to strengthen Ansaldo Energia's competitiveness, both in achieving technological autonomy in gas turbines and in its service activities for power generation plants. Thomassen, which posted revenues of €mil. 45 million in 2005, specialises in heavy duty gas turbines service operations using General Electric (GE) technology. With this transaction Ansaldo Energia S.p.A. may expand its service operations from Siemens to GE technology, in place in most of the turbines installed worldwide. For Ansaldo Energia, these transactions open up new and important possibilities for commercial synergies both in Italy and abroad and help boost the company's value and visibility internationally.

On 6 August 2006 Finmeccanica signed agreements to resize its stake in **AvioGroup S.p.A** (formerly Aero Invest 1 S.p.A.), which is the holding company of the Avio Group including Avio S.p.A., a company operating in the development and production of large engines and important aeronautics and space components).
Under the agreements, signed on 14 December 2006, Finmeccanica sold, together with Carlyle (which held about 70% of the company), its around 30% stake in AvioGroup to Cinven investment funds for a gross sum of around €mil. 432.
Telespazio Luxembourg S.A. (name later changed to Aeromeccanica S.A.), a subsidiary of Finmeccanica, simultaneously bought back a 15% stake in the Avio Group for about €mil. 130. The difference between the purchase price received and the amount reinvested in the Avio Group contributed to the improvement of the Group's net financial position excluding operating costs. The new shareholders' agreements between Telespazio Luxembourg and Cinven regarding the management of the Avio group provide for the same corporate governance rights and shareholder relations as before between Finmeccanica and Carlyle. In addition, Finmeccanica paid about €mil. 6 to Avio S.p.A. for an option to purchase its Space division.

On 18 October 2006, **Finmeccanica** signed a Memorandum of Understanding with the **Russian railways** to co-operate in the production, sale and technical assistance of rolling stock and rail infrastructure. This agreement is part of the Group's co-operation with Russian companies, and lays the foundations for a series of industrial partnerships. Given growing demand of rolling stock and high-speed facilities in Russia and in other CIS markets, the companies of the Finmeccanica Group specifically operating in the railway sector will be able to enhance their industry and product expertise. This might potentially affect the priority development programmes of the Italian railways.
Within this context, on 9 February 2007, the **Russian railways, the Ferrovie dello Stato Group and Finmeccanica** signed an agreement to develop opportunities for commercial co-operation in carrying out shared international projects, especially in the high-speed rail area, which could also involve the Moscow–St.Petersburg line. The first act of cooperation will involve the high-speed Jeddah–Mecca–Medina line in Saudi Arabia, worth an estimated $bil. 6.
During the most recent Italo-Russian summit held in Bari in March, Finmeccanica also signed a new industrial cooperation agreement with the Russian railways establishing the implementation methods and timetables for priority projects such as: the development of a new regional train, the application of Selex Sistemi Integrati S.p.A.'s existing technologies and expertise in the creation of Safety & Security systems, the development by Telespazio S.p.A. of a satellite observation system for monitoring land subject to landside adjacent to the Tuapse–Adler line.

Finally, please note that a number of Group companies changed their names during 2006 and early 2007: Aermacchi S.p.A. became Alenia Aermacchi S.p.A, Officine Aeronavali Venezia S.p.A. became Alenia Aeronavali S.p.A., S.I.A.-

Società Italiana Avionica S.p.A. became Alenia SIA S.p.A., Selex Composite S.p.A. became Alenia Composite S.p.A., Mecfin S.p.A. became Finmeccanica Group Services S.p.A., GA Immobiliare S.p.A. became Finmeccanica Group Real Estate S.p.A. and Telespazio Luxembourg S.A. became Aeromeccanica S.A..

Financial transactions

In 2006, Finmeccanica did not carry out any new transactions on the capital market. As a result, bond term debt did not undergo any significant variations, recording an overall sum of around €mil. 1,748 at accounts closure (according to IAS/IFRS) and an average debt life of around 9 years.
The following table summarises the outstanding bond issues at 31 December 2006, including the issues placed on the market by the subsidiary Finmeccanica Finance S.A.:

Outstanding bond							
Issuer		Year of issue	Maturity date	Countervalue amount (€mil./000)	Annual coupon	Type of offering	IAS values recognised (€mil./000)(5)
Finmeccanica Finance S.A.		1997	16 Jan 2007	6	3.30%	Japanese institutional	6
Finmeccanica Finance S.A.	(1)	2002	30 Dec 2008	297	Variable	Italian retail	299
Finmeccanica Finance S.A.	(2)	2003	8 Aug 2010	501	0.375%	European institutional	432
Finmeccanica Finance S.A.	(3)	2003	12 Dec 2018	500	5.75%	European institutional	497
Finmeccanica S.p.A.	(4)	2005	24 Mar 2025	500	4.875%	European institutional	514

(1) Bonds offered solely to the general public in Italy and listed on the TLX market operated by Trading Lab Banca S.p.A. – Unicredito Italiano Group. Although they were issued within the framework of a Euro Medium Term Notes programme (EMTN) with a maximum of €bil. 2, the bonds are governed by specific regulations under Italian law. Transaction authorised pursuant to Article 129 of Legislative Decree no. 385/93. Prospectus filed with CONSOB on 4 December 2002 (authorisation notified with note No. 2079342 of 3 December 2002).

(2) Bonds exchangeable for a maximum number of 20,000,000 shares in STMicroelectronics N.V. (STM) at a conversion price of €25.07 per share. Beginning three years after issue, Finmeccanica Finance may require that the bond be exchanged if the average price recorded for the 30 business days prior to the date bondholders were notified is more than 125% of the conversion price. At maturity, Finmeccanica Finance may redeem the bonds in cash or, upon receipt of prior notice of no less than 15 business days, with a combination of STM shares valued at the average price recorded over the 5 previous business days, and with cash for the difference. Transaction authorised pursuant to Article 129 of Legislative Decree no. 385/93. The bonds are listed on the Luxembourg Stock Exchange.

(3) The bonds have been issued under the EMTN programme with a maximum of €bil. 2. The entire issue was converted from fixed rate to variable rate for the first two years of the bond term. Transaction authorised pursuant to Article 129 of Legislative Decree no. 385/93. The bonds are listed on the Luxembourg Stock Exchange.
A number of interest rate transactions involving these bonds were carried out to enable the Company to benefit from low variable rates throughout 2005, with an effective rate of around 3.25%. In 2006, the effective interest rate reverted back to an average of about 5.92%.

(4) The bonds have been issued under the EMTN programme with a maximum of €bil. 2. Transaction authorised pursuant to Article 129 of Legislative Decree no. 385/93. The bonds are listed on the Luxembourg Stock Exchange. A number of interest rate transactions were carried out to optimise funding costs.

(5) The differential between the face value of the bond and the value posted in the financial statements is due to the classification of accrued interest as an increase in the value of the debt, and the recognition of issue discounts as a reduction in that value. Furthermore, with regard to the issue of the exchangeable bond referred to in note (2), IAS 39 requires the separation of the debt component from the call option embedded in the instrument. The debt component is measured using the market interest rate at the issue date rather than the nominal rate, while the option component is subject to periodic measurement at fair value. At 31 December 2006, as a result of the application of this methodology the debt recognised was €mil. 69 less than the face value of the bond; this difference will gradually narrow as the maturity date approaches.

All Finmeccanica Finance S.A. bond issues are irrevocably and unconditionally backed by Finmeccanica S.p.A.

All of the above bond issues are governed by rules containing standard legal clauses for these kinds of transactions carried out by corporations. The terms and conditions of the Finmeccanica issues do not require any commitment regarding specific financial covenants, but they do include so-called negative pledge and cross default clauses.
Under the negative pledge clauses, the issuers Finmeccanica Finance S.A., Finmeccanica S.p.A. and their material subsidiaries (companies in which the issuer or guarantor holds more than 50% of capital or which represent at least 10% of its overall revenues) are specifically and exclusively prohibited from providing guarantees for financial transactions that partially benefit one or more creditors, excluding the rest of the latter. Securitisation transactions and, as of July 2006, the establishment of segregated assets pursuant to articles 2447 bis et seq. of the Italian Civil Code, are exempt from this prohibition.

With regard to the cross-default clauses, these give the holders of each bond the right to demand early repayment of the bond (default) if, as to any bond or, more generally, as to the financial commitments of the Group, the Group fails to make payments in excess of fixed limits or any other default event occurs.

All bonds issued by Finmeccanica S.p.A. and Finmeccanica Finance S.A. have been assigned a medium-term credit rating by the three international rating agencies, Moody's Investors Service, Fitch and Standard and Poor's. Specifically, at the date of this Report, these credit ratings were A3 (Moody's) and BBB (Fitch and Standard and Poor's), all with a stable outlook. The Moody's credit rating in the previous financial year improved two levels, advancing from Baa2 to A3, after a methodological revision by the Agency.

As indicated in the table, the bond issued on the Japanese institutional investors market came to maturity and was entirely repaid on 16 January 2007.

Furthermore, as part of its centralisation of finance activities, Finmeccanica S.p.A has obtained credit lines and guarantees sufficient to meet Group needs. Specifically, it holds a medium-term revolving credit line of €mil. 1,200 agreed in 2004 with a pool of national and foreign banks, whose interest rate terms and duration (current maturity 2012) improved during the previous financial year thanks in part to the improved credit rating. This transaction is also governed by negative pledge clauses whose content has been illustrated earlier. At 31 December 2006, the credit line had not been used. Finmeccanica also has additional short-term credit lines amounting to around €mil. 1,200 (of which around €mil. 275 is guaranteed) entirely undrawn at 31 December 2006. There are also unconfirmed guarantees available amounting to around €mil. 1,900.

Finally, on 21 July 2006 the EMTN bond-issue programme was extended for an additional 12 months, for a maximum of €bil. 2, under which the issues described above in notes (1), (3) and (4) were carried out.

The financial impact of the industrial operations mentioned above are described in the paragraph "Financial Position".

2. Finmeccanica Group results

Highlights

€millions	2006	2005	change
Orders	15,725	15,383	2%
Order backlog	35,810	32,114	
Revenues	12,472	10,952	14%
EBIT	878	735	19%
Net profit	1,020	396	158%
Net invested capital	6,188	5,670	
Net financial debt	858	1,100	
FOCF	506	501	1%
ROI	17.7%	17.5%	0.2 p.p.
ROE	20.5%	9.6%	10.9 p.p.
EVA®	257	217	18%
R&D expenditure	1,783	1,742	2%
Employees (no.)	58,059	56,603	

p.p.: percentage points

Before looking at the results for 31 December 2006, it is important to underscore the fact that the Finmeccanica Group has undergone a number of changes during the periods in question. Certain of these changes were a consequence of changing the accounting policies for certain items, while other substantial changes were due to changes in the Group due, primarily, to transactions to supplement and strengthen the Aerospace and Defence segment, including:

- Defence Electronics: in 2005, the BAE Systems Plc (BAE) agreement and the acquisition of Datamat S.p.A.;
- Space: in 2005, the Alcatel S.A. (Alcatel) agreement;
- Defence Systems: in 2006, MBDA's acquisition of LFK GmbH.

The different times when these transactions took place, particularly those in 2005, the varying contributions to consolidated results of these new enterprises and, in certain cases, a lack of data regarding the prior period performance of the incoming entities means that it has not always been possible to provide a like-for-like comparison of the figures above, particularly earnings figures. In an effort to provide accurate figures for internal Group growth, comments have been provided on discrepancies between the two periods being compared. Approximations of values have been limited as far as possible, implicitly incorporating the effects of the changes to the scope of consolidation as noted above.

Finally, as regards the changes in accounting policies, the most important of these regards development costs, which is a result of the changing regulatory framework. All of these changes are described in more detail in the "Notes to the Consolidated Financial Statements". As such, for the purposes of comparison, we have preferred to comment on "revenues" and no longer on "value of production".
In order to provide more complete information on the Group's financial standing and performance, the following reclassified statements have been prepared.

Income statement		For the 12 months ended 31 December	
€millions	Notes	2006	2005
Revenues	(*)	12,472	10.952
Change in work in progress, semi-finished goods and finished products		(24)	517
Costs for goods and personnel	(**)	(11,121)	(10,330)
Depreciation and amortisation	36	(482)	(347)
Writedowns	36	(23)	(18)
Restructuring costs	(***)	(10)	(32)
Other net operating income (costs)	(****)	66	(7)
EBIT		**878**	**735**
Net financial income (charges)	(*****)	394	(149)
Income taxes	40	(243)	(200)
NET PROFIT (LOSS) BEFORE DISCONTINUED OPERATIONS		**1,029**	**386**
Result of discontinued operations	41	(9)	10
NET PROFIT (LOSS)		**1,020**	**396**

Notes on the income statement reclassification:
(*) Includes "revenues" and "revenue from related parties"
(**) Includes "costs from related parties", "costs for goods", "costs for services", and "personnel costs" (net of restructuring costs), net of "capitalized costs for internal production".
(***) Includes the restructuring costs classified as "personnel costs" and "other operating costs".
(****) Includes the net amount of "other operating revenues", "other operating revenue from related parties", and "other operating costs" (net of restructuring costs).
(*****) Includes financial income and charges from related parties.

As at 31 December 2006, the Finmeccanica Group posted improved financial performance both as compared with the previous year and with the forecasts that had been defined.
Compared with 31 December 2005, revenues have increased by 14% and EBIT by 19%; in terms of internal growth, these figures have increased by 8% and 17%, respectively. Return on sales (ROS) reached 7.0% for an increase over the previous financial year (6.7%) as well, while orders increased by 2% over 31 December 2005. As for the Group's profitability ratios compared with the previous financial year (with last year's figures in brackets), Return On Investments (ROI) amounted to 17.7% (17.5%), Group EVA® [1] was a positive €mil. 257 (positive €mil. 217), and return on equity (ROE) amounted to 20.5% (9.6%).

Consolidated net income as at 31 December 2006 totalled €mil. 1,020, as compared with the €mil. 396 as at 31 December 2005.

Contributing to consolidated net income as at 31 December 2006 were a series of non-recurring transactions, the most significant of which include the following:

- the gain realized on the public tender for the 60.0% stake in Ansaldo STS S.p.A. – roughly €mil. 404 – net of the effect of consolidated tax procedures;
- the gain – roughly €mil. 291 – on the sale to the company specifically established by the British Cinven investment funds, i.e. BCV Investment S.A., of Finmeccanica S.p.A.'s entire equity interest (approximately 30%) in AvioGroup S.p.A., the holding company of the Avio group. As described in greater detail among the industrial transactions, Aeromeccanica S.A., a wholly-owned subsidiary of Finmeccanica S.p.A., then repurchased a 15% stake in the aforementioned company.

[1] Eva® is a registered trademark of Stern Stewart & Co.

New orders acquired as at 31 December 2006 amounted to €mil. 15,725, compared with €mil. 15,383 for the same period of the previous financial year. Approximately 56% of overall new orders acquired can be attributed to the military market, with an increase in percent terms over the previous year (52%).

25% Helicopters
27% Defence Electronics
16% Aeronautics
5% Space
7% Defence Systems
7% Energy
13% Transportation

New orders

€millions	2006	2005	change
Helicopters	4,088	3,712	10%
Defence Electronics	4,197	4,627	-9%
Aeronautics	2,634	3,230	-18%
Space	851	599	42%
Defence Systems	1,111	763	46%
Energy	1,050	1,032	2%
Transportation	2,127	1,615	32%
Cancellations and Other	(333)	(195)	
	15,725	**15,383**	

The main new orders acquired refer to:

- Helicopters:
  - the first lot for the provision of 70 Future Lynx helicopters to the British Armed Forces for a total of roughly €mil. 550 (Q2);
  - the first lot for the first 5 years, out of a total of 25, for the IMOS contract for logistics support to the entire EH101 fleet in service with the British RAF and Royal Navy for a total of €mil. 640 (Q1);
  - the MCSP contract for the upgrading of 30 EH101 Merlin MK1 helicopters in use by the Royal Navy for a total of €mil. 550 (Q1);
  - orders for 42 helicopters for a total value of some €mil. 280 (Q3), including the agreements with Aerolineas Ejecutivas (Mexico) and Synergy Aerospace (Brazil) with initial agreements for 5 helicopters (plus options for 37 more over the next 5 years) and 6 helicopters (plus options for 56 more over the coming years), respectively;
  - the contract for the provision of 34 NH90 helicopters to the Australian Armed Forces for €mil. 150 and two EH101 helicopters to the Italian Navy for a total of €mil. 63 (Q4);

- Defence Electronics:
  - in command and control and communication systems, FREMM orders for some €mil. 200 (Q1, Q2, Q3), the signing of the agreement by the Ministry of the Interior for the start of programme to build the Tetra network for secure digital interforce communications for €mil. 216 (Q4), and the FALCON primary strategic communications programme for the British Ministry of Defence for €mil. 87 (Q2);
  - in avionics, orders related to the second lot of the EFA IRST for €mil. 114 (Q2) and the Tornado upgrading for Saudi Arabia and the British Ministry of Defence for €mil. 320 (Q4);
  - in air-traffic control, the SMART contract in Turkey for €mil. 44 (Q3);
  - in security and information technology, the Telecom order for the Italian postal service's secure network for €mil. 31 (Q2) and the "hybrid mail" order in Russia for €mil. 22 (Q3);
  - and finally, in the Defence Electronics segment, the first nine months of 2005 benefited significantly (by some €mil. 1,200) from the order to produce the Defensive Aids Sub System (DASS) for all of the Typhoon Eurofighters for the second lot in the production of these craft;

- Aeronautics:
  - in the civil segment, concerning aerostructures, the Boeing order for the B787 for roughly €mil. 570 (Q4, while in 2005 it totalled roughly €mil. 1,200);
  - in the military segment, the provision of ten ATR72 ASW craft to the Turkish navy for some €mil. 180 (Q2), orders for five C27J craft to Bulgaria for roughly €mil. 90 (Q2) and for three craft to Lithuania for approximately €mil. 70 (Q4), and orders for eight MB339 training craft to Malaysia for €mil. 90 (Q4);
  - the GIE-ATR consortium, which received orders for 7 (Q3), 29 (Q2), and 18 (Q1) aircraft, with a total value of roughly €mil. 350, plus customer service activities for some €mil. 90;

- Space:
  - in telecommunications, the Turksat 3A and Ciel 2 satellites (Q1) and Eutelsat orders related to the W2A (Q3) and W7 (Q4) satellites and the first lot for the provision of 48 low-earth orbit (LEO) satellites for the second-generation Globalstar Constellation (Q4); orders for the Arabsat 4AR and AMC1 payloads (both Q2);
  - in the civil segment, further orders related to the Galileo and Egnos navigation programmes (Q2) and contracts related to the Cosmo programme to launch the first three satellites, and the first lot for the creation of the fourth satellite (Q4);
  - in the military segment, orders related to the BW Satcom programme for the provision of two satellites to the German Ministry of Defence (Q3), the further lot related to the Sicral 1B satellite to the Italian Ministry of Defence (Q4), and orders for the provision of security and defence networks and services;

- Defence Systems:
  - in the missiles segment, the provision of Trigat long-range anti-tank systems (Q2), Exocet SM39 and Sea Wolf anti-ship systems to Chile (Q1), and SCALP Naval surface-to-surface systems to outfit the French FREMMs and Barracuda submarines (Q4);
  - in the land and sea weapons segment, the order for the provision of armoured combat vehicles to the Italian Army (Q4) and FREMMs for the Italian and French Navies (Q2);
  - in the underwater segment, the Black Shark order by the Singapore Navy (Q4);

- Energy:
  - the Rizziconi combined-cycle plant, including scheduled maintenance, for some €mil. 500 (Q1);
  - three V94.2 gas turbines for the Barka plant in Oman for €mil. 58 and two gas turbine assemblies for the Amman East plant in Jordan for €mil. 41 (Q4);
  - and finally, the strong growth in service orders, which went from €mil. 390 as at 31 December 2005 to €mil. 462 as at 31 December 2006;

- Transportation:
  - in signalling, the order for automated train control systems (SCMT), both wayside and on-board, for Italy, worth some €mil. 70, the order for the Ghaziabad-Kampur stretch in India for roughly €mil. 60 (Q1), the order related to the high-speed Perpignan–Figueras line in France and Spain (Q2), and the Trenitalia order for the fifth contract for the SCMT on-board devices for roughly €mil. 100 (Q3);
  - in systems, the extension, to 2010, of the operation and maintenance of Copenhagen's driverless metro, worth €mil. 127 (Q1), the driverless metros in Thessaloniki, worth around €mil. 280, and Milan Line 5, worth around €mil. 153, which also affected the vehicles segment (Q2), and the order for the Piscinola–Capodichino regional metro line in Campania, Italy, for some €mil. 80 (Q3);
  - in vehicles, the order for Sirio trams in Turkey, worth around €mil. 50 (Q1), the supply contract for Line 2 of the Milan metro, worth around €mil. 40 (Q2), the maintenance contract for the Madrid metro vehicles for some €mil. 240 (Q3), and the order for the provision of regional trains for Ferrovie Nord Milano for €mil. 180 (Q4).

At 31 December 2006, the **order backlog** totalled €mil. 35,810, compared with €mil. 32,114 at 31 December 2005, guaranteeing the Group coverage equal to three years of production. The increase of €mil. 3,696 is due essentially to ordinary acquisition and order volumes and client billing.

23% Helicopters
21% Defence Electronics
21% Aeronautics
3% Space
12% Defence Systems
7% Energy
13% Transportation

Order backlog

€millions	2006	2005	change
Helicopters	8,572	7,397	16%
Defence Electronics	7,676	6,946	11%
Aeronautics	7,538	6,865	10%
Space	1,264	1,154	10%
Defence Systems	4,252	3,869	10%
Energy	2,468	2,329	6%
Transportation	4,703	3,956	19%
Cancellations and Other	(663)	(402)	
	35,810	**32,114**	

In line with the Group's development targets, **revenues** as at 31 December 2006 reached €mil. 12,472, as compared with the €mil. 10,952 as at 31 December 2005, pointing to a net increase of €mil. 1,520 (+14%), of which some €mil. 824 (8%) is attributable to internal growth, with the remaining €mil. 696 being the result of changes in the scope of consolidation.

22% Helicopters
29% Defence Electronics
15% Aeronautics
6% Space
9% Defence Systems
8% Energy
11% Transportation

Revenues

€millions	2006	2005	change
Helicopters	2,727	2,413	13%
Defence Electronics	3,747	3,164	18%
Aeronautics	1,908	1,789	7%
Space	764	735	4%
Defence Systems	1,127	1,143	-1%
Energy	978	764	28%
Transportation	1,368	1,226	12%
Cancellations and Other	(147)	(282)	
	12,472	**10,952**	

Organic growth in revenues was recorded in Helicopters (13%), thanks to the start of work on the VH 71 order for the President of the United States of America, as well as the increased production rate for the AW 139 line and a greater volume of product support, mainly in the United Kingdom. The Defence Electronics, Defence Systems, and Space segments were essentially in line. Growth in Aeronautics was driven by civil business, particularly for the ATR, A380, and B777. The increase in the Energy sector (28%) was due to the systems nature of production for the year and development of the LTSA and Flow businesses. Finally, growth in the Transportation segment may be attributed to the increase in signalling business and an improvement in vehicles as compared with the particularly poor performance of 2005.

At 31 December 2006, **EBIT** was €mil. 878, compared with €mil. 735 at 31 December 2005 – a net increase of €mil. 143 or 19% – of which roughly €mil. 126 (17%) was organic growth, while the remaining share, some €mil. 17, was attributable to changes in the scope of consolidation.
At 7.0%, return on sales (ROS) increased by 0.3 percentage points over 31 December 2005 (6.7%).

30% Helicopters
31% Defence Electronics
20% Aeronautics
4% Space
9% Defence Systems
6% Energy

EBIT

€millions	2006	2005	change
Helicopters	290	272	7%
Defence Electronics	300	269	12%
Aeronautics	203	166	22%
Space	44	26	69%
Defence Systems	91	112	-19%
Energy	63	39	62%
Transportation	15	(48)	
Other	(128)	(101)	
	878	**735**	

Organic growth of EBIT includes:
- a 7% increase in Helicopters due in part to increased production and the effect of efficiency drives implemented last year under the integration of Italian and UK activities;
- an increase in the Defence Electronics sector due essentially to improvements in command and control systems and in information technology, which benefited from the increase in industrial profitability;
- growth in Aeronautics attributable to lower risks due to positive sales trends and the commercial prospects of the ATR programme, which permitted release of excess provisions. This was partly offset by a deterioration at Alenia Aeronavali, due mainly to provisions for charges on orders and write-offs of development costs;
- an improvement in Space due essentially to greater production efficiency, combined with a reduced impact of restructuring costs;
- a worsening in Defence Systems due to a decline in production volumes and lower profitability in the underwater systems segment, which was partially offset by the missiles segment with the newly acquired German firm;
- growth in Energy due to increased production volumes and increased margins on individual contracts;
- an improvement in Transportation due in part to vehicles segment, which, despite posting an operating loss, performed better than the figures as at 31 December 2005. Signalling and systems also posted improvements, benefiting from a substantial improvement in industrial profitability.

Balance sheet			
€millions	*Notes*	31 December 2006	31 December 2005
Non-current assets		9,897	7,671
Non-current liabilities	(*)	(3,275)	(2,018)
		6,622	5,653
Inventories	16	3,095	5,511
Work in progress	17	2,823	2,538
Trade receivables	18	3,856	3,600
Trade payables	28	(3,561)	(3,431)
Advances from customers	17	(5,529)	(4,389)
Provisions for short-term risks and charges	25	(571)	(523)
Other net current assets (liabilities)	(**)	(547)	(3,289)
Net working capital		**(434)**	**17**
Net invested capital		**6,188**	**5,670**
Group shareholders' equity		5,276	4,444
Minority interests		81	154
Shareholders' equity	23	**5,357**	**4,598**
Net financial debt (cash)		**858**	**1,100**
Net (assets) liabilities held for sale	(***)	**(27)**	**(28)**

Notes on the reclassified balance sheet:
(*) Includes all non-current liabilities except "financial liabilities to related parties" (which are included among "non-current liabilities to related parties" and "non-current financial debt".
(**) Includes "tax receivables", other current receivables from related parties (included among "current receivables from related parties") and "other current assets", net of "tax payables", other payables to related parties (included among "current liabilities to related parties"), and "other current liabilities".
(***) Includes the net of "non-current assets held for sale" and "liabilities directly related to assets held for sale".

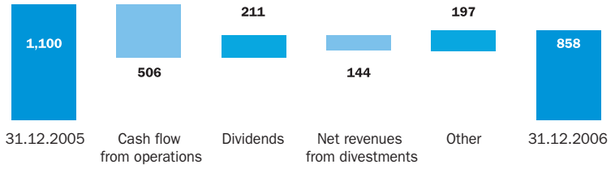
The Group's **net financial debt** (financial payables in excess of financial receivables and cash and cash equivalents) at 31 December 2006 stood at €mil. 858, compared with €mil. 1,100 at 31 December 2005, a net increase of €mil. 242. This level of debt, equal to 16% of consolidated shareholders' equity (24% as at 31 December 2005) is within the limits compatible with sound and prudent financial management and the thresholds indicated by leading credit rating companies.
The Group's debt structure as at 31 December 2006 remains particularly solid, with an average remaining duration that is still high (at 9 years as compared with the 10 years of 31 December 2005) and minimized cost of debt given that the average interest rate as of 31 December 2005 had already reached 3.7% (4.8% for IFRS purposes).
Free operating cash flow (**FOCF**) at 31 December 2006, not counting non-recurring events, was positive (generation of cash) in the amount of €mil. 506, compared with positive €mil. 501 at 31 December 2005. As in 2005, the 2006 figure was obtained through constant control of the company's cash flow needs and concerted efforts concerning both customers and suppliers. Therefore, FOCF made it possible to distribute (ordinary and extraordinary) dividends.

Compared with 31 December 2005, debt as at 31 December 2006 was also subject to a series of non-recurring events, with both positive and negative impacts, that did not, however, substantially alter the balance. As described in detail in the "Financial Position" section below, the following are the most significant events, the net effect of which (€mil. 19) confirms the above:
Decreases:
- inflows on the sale of the 60% stake in Ansaldo STS S.p.A. for €mil. 458;
- inflows from the sale of the 30% stake in AvioGroup S.p.A. and the 15% repurchase of a special-purpose company – BCV Investment S.A. – from Cinven investment funds for €mil. 302;

Increases:
- the outflow of €mil. 109 for the purchase of a further 46% stake (approximately) in the company Datamat S.p.A.;
- the outflow in September 2006 for a €mil. 47 balancing payment to the French firm Alcatel Partecipations S.A.;
- the inclusion of the put and call option with the BAE Systems group for a 25% stake in Selex Sensors and Airborne Systems, with a value of roughly €mil. 401 as at 31 December 2006;
- the inclusion of the effect of the recognition of finance costs by AnsaldoBreda S.p.A. in the amount of €mil. 114 (included in the figure below under "other");
- the inclusion of the reclassification of Finmeccanica S.p.A. taxes receivable in the amount of €mil. 106 (included in the figure above under "other").

Finally, with regard to the funds raised with the Ansaldo STS flotation, on 28 March 2006, Finmeccanica's Board of Directors asked the shareholders, at the meeting to approve the 2005 financial statements, to approve the pay-out of an extraordinary dividend of €0.19 per share, equal to a maximum of €mil. 81 (€mil. 80 was actually disbursed). Combined with the ordinary dividend, this entailed an overall outlay of €mil 211.

Net financial debt at 31 December 2006



Consolidated **net invested capital** at 31 December 2006 came to €mil. 6,188, compared with €mil. 5,670 at 31 December 2005. The net increase of €mil. 518 is entirely attributable to capital assets, as **working capital** declined significantly by €mil. 451 (from the positive €mil. 17 at 31 December 2005 to a negative €mil. 434 at 31 December 2006) due primarily to the overall improvement in the management of operating capital.

The €mil. 969 increase in capital assets is due to the recognition of goodwill from the acquisition of activities from BAE (€mil. 326), Datamat (€mil. 64), LFK (€mil. 43), and Alcatel Alenia Space (€mil. 41). The rest is due to investment in property, plant and equipment and intangible assets, net of amortisation and depreciation, and the €mil. 66 decrease due to the fair value measurement of the investment in STMicroelectronics N.V.

Research and Development costs, which stood at €mil. 1,783 at 31 December 2006, compared with €mil. 1,742 for 2005, increased by approximately 2%. This represented roughly 14% of revenues.

20% Helicopters
30% Defence Electronics
27% Aeronautics
4% Space
16% Defence Systems
1% Energy
2% Transportation

Research and Development costs

€millions	2006	2005	change
Helicopters	356	436	-18%
Defence Electronics	541	501	8%
Aeronautics	486	405	20%
Space	64	79	-19%
Defence Systems	279	268	4%
Energy	17	13	31%
Transportation	40	40	0%
	1,783	**1,742**	

Activity was related mainly to the following programmes:

- Helicopters: in the context of research funded by Italian Law 808/85, the development of technologies for a new six/seven-ton class helicopter named A149 and the BA 609 convertiplane;
- Defence Electronics: in avionics, programmes including the continuing development of the EFA programme concerning the common modules for new electronic-scan radar systems, both for surveillance and combat (Vixen, Captor, etc.) and the fine-tuning of prototypes of the UAV Falco system; in radar and command and control systems, the development of the modular sea combat system and the new Kronos 3-D naval surveillance radar; in integrated communication systems and networks, the start of activities on the new product families, such as ad hoc networks, WiMAX, software radio, and switch all IP, the Future Soldier programme, and the continuation of development of Tetra technologies; finally, in security and information technology, the development of the range of secure access systems and the improvement of the performance of the main postal automation machines;
- Aeronautics: the development of civil programmes including the B787 and A380, and military programmes with the C27J, EFA and the M346 training aircraft;
- Space: the main satellite programmes, future on-board testing for the International Space Station, and the (network/architecture) solutions for advanced telecommunications;
- Defence Systems: ongoing development of the Meteor air-to-air missile in the missiles segment, the land and sea guided munitions system, and the Black Shark heavy torpedoes and A244 Mod. 3 light torpedoes, in the underwater systems sector;
- Energy: in systems, the continuation of the technological autonomy programme in the field of steam and gas turbines; in services, activities to increase remote diagnostics capabilities and the development of both special tools and software packages to improve machine and system performance;
- Transportation: in signalling, work to meet new, emerging requirements in rail transport and mass transit, and the development of on-board equipment.

The number of **employees** at 31 December 2006 was 58,059, up 1,456 compared with the 56,603 employees at 31 December 2005. This rise is due in part to the consolidation of LFK GmbH (246 employees) within the Defence Systems division and Thomassen Turbine Systems B.V. and Energy Service Group Ltd (145 employees) in the Energy division, in addition to positive turnover, primarily within Aeronautics, Helicopters, and Transportation.

16% Helicopters
33% Defence Electronics
21% Aeronautics
6% Space
7% Defence Systems
5% Energy
12% Transportation

Employees

no.	2006	2005	change
Helicopters	8,899	8,531	4%
Defence Electronics	19,185	19,786	-3%
Aeronautics	12,135	11,198	8%
Space	3,221	3,194	1%
Defence Systems	4,275	4,104	4%
Energy	2,856	2,529	13%
Transportation	6,677	6,321	6%
Other	811	940	
	58,059	**56,603**	

3. Financial position

Net consolidated financial debt at 31 December 2006 is reported in the following table, with comparative information at 31 December 2005.

€millions	31 December 2006	31 December 2005
Short-term financial payables	159	190
Medium/long-term financial payables	1,865	1,879
Cash and cash equivalents	(2,003)	(1,061)
BANK DEBT AND BONDS	**21**	**1,008**
Securities	(21)	(20)
Financial receivables from Group companies	(26)	(17)
Other financial receivables	(452)	(443)
FINANCIAL RECEIVABLES AND SECURITIES	**(499)**	**(480)**
Financial payables to Group companies	500	372
Other short-term financial payables	722	104
Other medium/long-term financial payables	114	96
OTHER FINANCIAL PAYABLES	**1,336**	**572**
NET FINANCIAL DEBT (CASH)	**858**	**1,100**
Net financial debt (cash and cash equivalents) from discontinued operations	6	5

The Group's net financial debt at 31 December 2006 amounted to €mil. 858, compared with €mil. 1,100 at 31 December 2005, after posting net debt figures of €mil. 1,481 at March 2006, €mil. 1,462 at June 2006, and €mil. 2,184 at September 2006. The debt figure reflects the following effects attributable to the application of IAS 32 and 39:

- as regards the Finmeccanica Finance S.A. €mil. 501 bond paying a 0.375% coupon and maturing in August 2010 exchangeable for STM shares, IAS 39 requires, as per the split accounting method, the separation of the financial debt component from the call option embedded in the instrument. The debt component is measured using the market interest rate at the issue date rather than the nominal rate (i.e. the effective interest rate method), while the option component, separated from the debt position, is subject to periodic measurement at fair value. At 31 December 2006, as a result of the application of this methodology, the debt recognised was €mil. 69 less than the face value of the bond. This difference will gradually narrow as the maturity date approaches;
- inclusion in the financial position of liabilities in respect of the unpaid portion of part of trade receivables assigned without recourse to factoring companies in a manner that prompted Finmeccanica to take the precaution of entering these amounts as part of its debt in accordance with the IFRSs. The remaining amount was equal to €mil. 10, compared with €mil. 39 at 31 December 2005;
- for the December 2006 figure, consistent with the approach adopted in the presentation of the accounts in 2005, it was decided not to recognize as debt the balancing entries resulting from fair value measurement of the derivatives on the date that the accounts were closed in view of the fact that a significant part of these transactions are designed to hedge "underlying" commercial positions. At 31 December 2006, these transactions had a positive balance.

Taking account of these adjustments, as well as the operational and non-recurring events described below, the Group's net financial debt went from €mil. 1,100 at 31 December 2005 to €mil. 858 at 31 December 2006.
The trend in net debt for 2006 confirms the traditional performance of cash inflows and outflows, with significant absorptions of cash in the first part of the year and noticeable recovery in the latter part of the year. As a result, average debt levels were higher than the figure posted at year-end. Free operating cash flow (FOCF) at 31 December 2006 settled at €mil. 506 after completing non-recourse transfers in December for a nominal value of some €mil. 800, which, given the regular progress in invoicing achieved by the companies of the Group, were done essentially to face significant delays in payment by various customers, particularly those that related to the public sector.

The debt figure was significantly impacted by the positive and negative effects of the following operations:

- a payment by Finmeccanica S.p.A. in January 2006 as part of the mandatory public tender offer launched in 2005 to acquire the remainder of Datamat, which was completed in early January 2006 with an outlay of €mil. 89, which in addition to the €mil. 151 paid in 2005 for 52.7% of the company, brought the total outlay to €mil. 240 and the overall stake in the company to approximately 89% (including the treasury shares owned directly by the company). Following a subsequent public announcement, additional shares were acquired on the market, bringing Finmeccanica's holding in Datamat above 90%, which means that Finmeccanica was required to launch an offer for the remainder of the shares, less the shares Finmeccanica already held and the treasury shares held by Datamat. The public tender for the remainder, which took place in the fourth quarter of 2006, was completed in early January 2007, after which Finmeccanica held a total stake in Datamat of approximately 98.6%, which made possible to Borsa Italiana S.p.A. to delist the security from the Italian MTAX market effective 9 January 2007. The cost of the transaction was roughly €mil. 20. Having surpassed the 98% shareholding threshold in Datamat shares, and in line with declarations made in the documentation for both the mandatory and residual public tenders, Finmeccanica now intends to exercise its right to purchase the remaining Datamat shares in a squeeze-out operation under Article 111 of the Finance Act. In that regard, upon the request of Finmeccanica, the Rome court has appointed an expert to determine the price of such remaining shares, after which they will be acquired by Finmeccanica at the price set by this expert;
- the payment by Finmeccanica S.p.A. of an ordinary dividend of €mil. 131, in addition to an extraordinary dividend of €mil. 80 paid to shareholders following the successful listing of Ansaldo STS, as described below;
- the €mil. 47 balancing payment by Finmeccanica S.p.A. in September 2006 to the French firm Alcatel Participations S.A. as part of the joint venture agreement signed in 2005 within the Space division;
- the €mil. 18 payment by the subsidiary Ansaldo Energia to acquire Calpine European Finance LLC from Thomassen Turbine Systems B.V. Ansaldo Energy also acquired a 55% stake in the Swiss firm Energy Service Group Ltd (ESG) for €mil. 2, after having previously acquired a 45% stake in 2005;
- the €mil. 260 payment by MBDA (a joint venture in the missiles segment in which Finmeccanica holds a 25% stake) concerning the acquisition of LFK GmbH, which was partially (€mil. 237) offset by the acquisition of the cash held by the company acquired. As a result, and taking account of the fact that MBDA was consolidated on a proportionate basis, the overall cash impact for the Group was not significant (some €mil. 6);
- the payment by Alenia Aeronautica S.p.A. to the Russian firm Sukhoi for an initial amount of €mil. 10 related to the announced partnership with this firm for the design, construction, distribution, and post-sale assistance for new regional 75 to 100-seat SuperJet 100s;
- the receipt by Finmeccanica of roughly €mil. 398, net of commissions, in March 2006 following the placement of 52.17% of Ansaldo STS S.p.A., the Group's lead company in the Transportation sector, which holds investments in companies operating in rail systems (Ansaldo Trasporti - Sistemi Ferroviari S.p.A.) and rail signalling (Ansaldo Signal N.V.), with the sale of 52,174,000 shares at a price of €7.80 each. In April, an additional net receipt of about €mil. 60 was posted following the exercise of the greenshoe option by the banks coordinating the placement. A further 7,826,000 shares, equal to 7.83% of the company, were sold. Upon completion of the two transactions, 60% of the share capital of Ansaldo STS was traded on the open market, with 40% being held by Finmeccanica S.p.A. The public listing of the company did not result in it being deconsolidated, and net debt as at 31 December 2006 therefore includes the net financial position of the listed company;
- the receipt of some €mil. 432 in December as part of the sales agreement signed on 6 August 2006 with the other partner, Carlyle, resulting from the sale of the entire 30% stake held by Finmeccanica in AvioGroup S.p.A., the holding company of the Avio group, to a company specially established by the British Cinven investment funds. As described in greater detail in the section concerning industrial transactions, subsequent to the signing of this sales agreement, but before it was actually executed, Finmeccanica exercised its option to partially reinvest in the Avio group by acquiring a 15% stake in a company specifically established by the Cinven funds in conjunction with the acquisition. This reinvestment was performed by Aeromeccanica S.A. for a total of €mil. 130 at the same time as the sale of the AvioGroup S.p.A. shares by Finmeccanica. The financial benefit of the transaction at the consolidated level therefore reached €mil. 302, and as a result of these two transactions, Finmeccanica now holds a 15% stake in Avio S.p.A. indirectly through Aeromeccanica S.A. Finmeccanica also purchased for roughly €mil. 6 from Avio S.p.A. the option to acquire its Space division.

It should also be noted that the Group's net financial debt also includes:

- the value of the put and call option with the BAE Systems Group for the transfer to Finmeccanica in 2007 of the remaining 25% stake in Selex Sensors and Airborne Systems S.p.A. for a total outlay of roughly GBPmil. 269, or an equivalent of some €mil. 401 as at 31 December 2006;
- €mil. 114 resulting from financial costs for advance payments by customers that a Finmeccanica subsidiary will be required to pay during the coming year and which have been recognised as a financial liability given the nature of the contract giving rise to such costs;
- €mil. 106 resulting from the renegotiation currently under way with a bank concerning certain contract clauses related to the sale of tax receivables arranged with the bank in 2004 so as to align the contract with the provisions of IAS 39 concerning derecognition (Note 20).

Finally, it should be noted that, as for the previous year, the financial position again benefited from the offsetting effect of the Italian consolidated taxation mechanism, with lower outlays of some €mil. 216 for the year.

As regards the composition of debt, bank borrowings (both short and long-term) and bonds went from €mil. 2,069 at 31 December 2005 to the current €mil. 2,024 due essentially to a decline in short-term borrowings.

Cash and cash equivalents went from €mil. 1,061 at 31 December 2005 to €mil. 2,003 at 31 December 2006. This figure benefited from the favourable trend in cash flows as mentioned above, which, as is typically the case, were highly concentrated towards the end of the year and which, as a result, finance the significant outlays in the first part of the subsequent year. Liquidity is largely (€mil. 1,647) held by the Group Parent, with the exception of cash temporarily held by subsidiaries, which transferred the funds to the centralized treasury system immediately after the closing of 2006. The figure for cash and cash equivalents also includes the balances of the companies that are no longer a part of the centralized treasury system (i.e. Ansaldo STS and its subsidiaries and the Alcatel Alenia Space joint venture).

As regards the composition of the remaining debt items, it should be noted that "other short-term financial liabilities" also include €mil. 401 for the aforementioned put and call option with BAE, and "other financial receivables" include some €mil. 429 in respect of the portion of financial receivables that the MBDA and Alcatel Alenia Space joint ventures hold vis-à-vis the other partners in implementation of existing treasury agreements. In accordance with the consolidation method used, these receivables, like all the other items, are included in the Group's scope of consolidation on a proportionate basis. "Financial payables to Group companies" include the debt of roughly €mil. 385 of Group companies to the joint ventures for the unconsolidated portion.

The reclassified cash flow statement as at 31 December 2006, compared with that of the previous year, is shown below.

€millions	2006		2005	
Cash and cash equivalents at 1 January	**1,061**		**2,055**	
Cash flow from operating activities - gross	1,565		1,413	
Changes in working capital	347		204	
Changes in other operating assets and liabilities	(594)		(662)	
Cash flow generated from (used in) operating activities	**1,318**		**955**	
Cash flow from ordinary investing activities (*)	(812)		(454)	
Free operating cash flow		**506**		**501**
Strategic investments	580		(807)	
Changes in other financial assets	(30)		56	
Cash flow generated from (used in) investing activities	**(262)**		**(1,205)**	
Dividends paid	(214)		(111)	
Cash flow from financing activities	102		(640)	
Cash flow generated from (used in) financing activities	**(112)**		**(751)**	
Translation differences	**(2)**		**7**	
Cash and cash equivalents at 31 December	**2,003**		**1,061**	

(*) Net of receipts for interventions relating to Italian Law 808/85 in 2006.

Fiscal year 2006 closed with free operating cash flow, confirming the trend of gradual growth (€mil. 506 compared with the €mil. 501 of the previous year), despite the significant increase in investments. Total cash flow for the year was also positively affected by certain extraordinary transactions, which are described below. Specifically:

- operating cash flow was positive at €mil. 1,318. This significant increase from the previous year (when operating cash flow was positive at €mil. 955) is essentially due to the different method of recognising non-recurring costs (see Note 6.1). In 2006, operating cash flow benefited from cash flows generated by the Aeronautics, Defence Electronics, and Energy divisions, as well as from the cash flows generated by the Ansaldo STS Group, which is consolidated on a line-item basis within the Transportation division;
- cash flow from investing activities came to a net outflow of €mil. 262 (outflow of €mil. 1,205 for 31 December 2005), which was the net effect of cash flows generated by the Avio and Ansaldo STS transactions (totalling €mil. 761) and investments in non-current assets, which resulted in a cash outflow of €mil. 873. In that regard, as compared with 2005, it should be noted that investments in "non-recurring costs" (see Note 6.1) are now classified among investing activities, rather than among cash flow from operating activities. Finally, the 2005 figure also included the effects of the significant level of acquisitions, which led to a net cash outlay of €mil. 769 (€mil. 181 in 2006);
- cash flow from financing activities came to a net outflow of €mil. 112 (outflow of €mil. 751 in 2005). The improvement over the previous year, due to the redemption of the convertible bond in June 2005 (€mil. 927), was partially offset by the greater dividend distributed to shareholders (€mil. 214 as compared with the €mil. 111 in 2005), which included €mil. 3 distributed to minority interests.

4. Performance by division

Helicopters

Main data

€millions	31 December 2006	31 December 2005
New orders	4,088	3,712
Order backlog	8,572	7,397
Revenues	2,727	2,413
EBIT	290	272
ROS	10.6%	11.3%
Working Capital	392	309
Net invested capital	2,085	2,023
ROI (*)	13.9%	13.4%
Research and Development	356	436
Employees (no.)	8,899	8,531

(*) Calculated on invested capital at period-end.

HIGHLIGHTS

New orders: higher (+10%) due both to the orders received from the UK Ministry of Defence – of particular note being the Future Lynx programme for the provision of 70 helicopters to the British Armed Forces, the MCSP order for the upgrade of the EH101 Merlin MK1 helicopters being used by the Royal Navy, and the IMOS order for the transformation of the modus operandi for the provision of logistics support for the fleet of EH101 in service with the Royal Air Force and Navy – and to civil sales that saw new orders for 210 units (AW139/A109/A119).
Revenues: up from 31 December 2005 (+13%) due to the production which has begun on the US101 contract, known as VH71, for the President of the United States, as well as to the increase in the rate of production on the AW139 line and the increase in volumes for the support activities generated primarily in the UK. It should also be noted that 2006 saw deliveries for a total of 170 helicopters, for an increase of 28% over the previous year.
EBIT: up 7% from 31 December 2005. This improvement is due, in part, to the aforementioned growth in volumes, as well as to the effect of efficiency enhancement actions undertaken last year as part of the process of integrating British and Italian activities.

The outlook for the global helicopter market, both civil and military, over the coming years is for strong growth. For 2007-2015, the forecast is for deliveries for a total of some €90 billion, nearly 80% of which for military applications. These figures do not include the update and remanufacturing programmes, which will be particularly significant in the US, or technical support and training, which tend to nearly equal the figures for new products. The growing demand for training services using simulators is increasing the importance of this service compared with other post-sale activities.
In the military segment, a large part of the growth in demand is being generated by growth in the domestic market in the US. After a period of relative stability, in recent years, a number of requirements have been defined, some of which related to ongoing programmes, with others to be open to international competition. In a number of cases, European industry appears to be well positioned thanks to the availability of a portfolio of recently designed products. In Europe, the leading national market is that of the UK, where the helicopter segment has been confirmed as being of strategic importance for national security, and AgustaWestland has been named as a key partner to the UK Ministry of Defence.
The civil sector is characterized by high volumes of production, but values that are more limited than those of the military segment. As such, we are seeing a trend towards renewing fleets with the introduction of helicopters of higher capacity and higher average costs. Demand within the segment, which involves a wide variety of applications (VIP/executive transport, offshore shuttles, emergency medical service, civil security and defence), also tends to feed itself, as the introduction of new products with more advanced features and greater performance tends to stimulate demand in the various areas of product application. For these reasons, the segment, which has been essentially stable in recent years, will tend to increase significantly in the coming years.
A potential 'technological revolution' could arise over the medium to long term with the introduction of the convertiplane, which is now in the advanced stages of development.
In terms of supply, although the segment shows a high degree of concentration with the leading western European and US competitors, it would appear to be possible, over the medium term, to develop significant local manufacturing capacity in certain Asian countries (China, India, South Korea, Japan), initially so as to meet the growing local demand and subsequently to compete globally, particularly in civil and paramilitary applications.

Finmeccanica is, together with AgustaWestland N.V. and its shareholdings, a leader in the extremely restricted circle of systems designers in the world helicopter industry.

Total volume of **new orders** for AgustaWestland, which reached €mil. 4,088 as at 31 December 2006, is sharply higher (+10%) over the same period of the previous year (€mil. 3,712).
The year ended 31 December 2006 saw a number of particularly significant commercial developments in the military segment, including the following orders received from the UK Ministry of Defence:

- the €mil. 1,394 programme for the provision of 70 Future Lynx helicopters to the British Armed Forces (Q2), the first group of which, for the development phase, has a value of roughly €mil. 557. This contract, which calls for the delivery of 30 helicopters to the Royal Navy and 40 to the Royal Army beginning in 2011, is part of the strategic partnering agreement between the UK Ministry of Defence and AgustaWestland, which calls for close collaboration in the helicopter programmes of the British Armed Forces as also defined by the UK government's Defence Industrial Strategy. This agreement, together with the Future Lynx contract, will ensure that the high-profile engineering and systems skills required by the UK Ministry of Defence are maintained at the AgustaWestland facilities in Yeovil in order to provide the needed support to the British Armed Forces;
- the contract for the Merlin Capability Sustainment Programme (MCSP) of a value of roughly €mil. 578, which includes upgrading 30 EH101 Merlin Mk1 helicopters in service with the British Royal Navy, with an option for a further 8 helicopters (Q1);
- the Integrated Merlin Operational Support (IMOS) contract, in the amount of roughly €mil. 634 for the first 5 of a total of 25 years, for the transformation of the modus operandi for the provision of logistics support for the fleet of EH101 in service with the Royal Air Force and Navy (Q1).

Other orders of note for the year within the military segment include a further 2 EH101 helicopters for the Italian Navy (Q4), the contract for the provision of a further 34 NH90 helicopters to the Australian Armed Forces (Q4), and the order for 8 AW139s for the United Arab Emirates Armed Forces (Q3).

Even in civil aviation, given its unique and virtually complete range of modern and competitive products, AgustaWestland has proven its ability to compete in increasingly broad market segments.
Of note in that regard are the following:

- orders for an additional 62 AW139 helicopters, including the provision of 12 helicopters to Mitsui Bussan (a Japanese civil aviation firm) and 8 to Hawker Pacific (an Australian government agency) in Q1. The portfolio of orders for the AW139 continues to grow, with some 135 helicopters currently on order;
- orders for an additional 108 A109 light twin-turbine helicopters, including the contract signed in conjunction with establishing the LIATEC joint venture between AgustaWestland, Finmeccanica, and the Libyan Company for Aviation Industry, for the provision of an additional 10 helicopters (Q1) in a configuration specific to border patrols, and the contract with the Japanese national police force (Q2) for the provision of an additional 4 helicopters. The Company has met with significant success for this type of craft, as demonstrated by the continuing growth in orders for this product, with currently 140 helicopters currently on order;
- orders for 40 A119 helicopters, including 20 to Seacor (Q2) for oil platform support and transport links and 5 to the Libyan Red Crescent (LRC) for emergency medical services (Q4);
- the agreement with Aerolineas Ejecutivas, Mexico City, which calls for an initial order of 5 A119 Koala, A109 Power, Grand, and AW139 helicopters, plus 37 options for the next 5 years (Q3), as well as the signing of a multi-year agreement with the Brazilian company Synergy Aerospace (a division of the Synergy group), which calls for the delivery in three years of A119 Koala, A109 Power, Grand, and AW139 helicopters for a total of 6 craft plus 56 options (Q3). The helicopters are to be used and leased by Ocean Air Taxi Aéreo, a subsidiary of Synergy Aerospace responsible primarily for offshore and VIP transport. In both agreements, the helicopters are to be produced in the AgustaWestland plants in Philadelphia (USA) and Vergiate (Italy).

Comparing the two periods, the three types of helicopters mentioned above posted orders for a total of 210 craft, as compared with the 127 units sold as at 31 December 2005.

As a result of the high volume of new orders for 2006, the value of the **order backlog** as at 31 December 2006 came to €mil. 8,572 for an increase of approximately 16% over the same figure of 31 December 2005 (€mil. 7,397).
The orders as at 31 December 2006 can be broken down into 68% for helicopters, 27% for

support activities, and 5% for engineering and other activities.

Revenues as at 31 December 2006 reached €mil. 2,727, up 13% over 31 December 2005 (€mil. 2,413). This improvement is primarily attributable to the production begun on the VH71 contract for the President of the United States, as well as to the increase in the rate of production on the AW139 line and the greater volumes for the support activities generated primarily in the UK. AgustaWestland output focused on the following main programmes:

- the EH101 for the Italian Navy, which saw continuing activities for the second lot and the delivery of 4 units; the completion of orders to both the Danish and Portuguese governments; and continuing activities for the provision of the EH101 to the Japanese Navy with the delivery of the first helicopter;
- the Super Lynx 300 helicopter, with work continuing on contracts with the South African Navy, as well as the completion of the contract with the Air Forces of Oman;
- the A109 Power helicopter for the civil/government market, of which 29 units have been delivered;
- the A109 Grand helicopter, of which 20 machines have been delivered;
- the A129 Mangusta helicopter upgrade in the combat (CBT) configuration, which is currently in service with the Italian Army;
- the single-turbine A119 Koala helicopter, of which 18 machines have been delivered;
- the AB412 helicopter for foreign government agencies, of which 5 units were delivered;
- manufacturing of the A109E Power variant, light utility helicopter (LUH) configuration, for contracts with the Swedish Armed Forces and the South African Air Force, with an additional 25 units delivered;
- activities concerning the production of the NH 90 helicopter;
- logistics and support services for existing civil/governmental and military fleets.

The year ended 31 December 2006 saw deliveries for a total of 170 helicopters, for an increase of 28% over the previous year.
EBIT as at 31 December 2006, in the amount of €mil. 290, posted an increase of 7% over the same period of the previous year (€mil. 272). This improvement is due, in part, to the aforementioned growth in volumes, as well as to the effect of efficiency enhancement actions undertaken last year as part of the process of integrating British and Italian activities. It should also be noted that EBIT includes €mil. 8.7 in amortisation related to assets moved to intangibles in line with the application of IFRS 3.
ROS settled at 10.6% for a slight drop from 31 December 2005 (11.3%). This decline was due to the decrease in profitability for product support activities related to the new contracts received in the UK.

Working capital, which reached €mil. 392 as at 31 December 2006 from the €mil. 309 of 31 December 2005, posted an increase of €mil. 83 due to the increase in current assets as a result of the aforementioned increase in production volumes.

Net invested capital as at 31 December 2006, in the amount of €mil. 2,085, posted an increase of €mil. 62 over 31 December 2005 (€mil. 2,023), which was essentially due to the aforementioned increase in working capital.
Return On Investment (**ROI**), which reached 13.9% as at 31 December 2006, increased over the figure at 31 December 2005 (13.4%) due primarily to the increase in EBIT.

Research and development costs at 31 December 2006, amounting to €mil. 356 (€mil. 436 at 31 December 2005), primarily concerned:

- research as part of programmes financed through Law 808/85, which include the development of innovative technologies for military purposes for a new helicopter of the 6/7-tonne class known as the A149, development of the BA609 convertiplane, which led to the first flight in helicopter mode for the PT2 prototype in November and in airplane mode in December 2006;
- research into upgrading products, where activities continued on the development and certification of the customisations for the AW139 and Agusta Grand helicopters;
- research and development into variants of base models in connection with government/military contracts.

AgustaWestland **employees** as at 31 December 2006 numbered 8,899, for a 4% increase from 31 December 2005 (8,531 employees), which was necessary in order to meet the technical/production needs related to the increase in business volumes.

4. Performance by division

Defence Electronics

Main data

€millions	31 December 2006	31 December 2005
New orders	4,197	4,627
Order backlog	7,676	6,946
Revenues	3,747	3,164
EBIT	300	269
ROS	8.0%	8.5%
Working Capital	734	802
Net invested capital	2,778	2,154
ROI (*)	10.8%	12.5%
Research and Development	541	501
Employees (no.)	19,185	19,786

(*) Calculated on invested capital at period-end.

HIGHLIGHTS

New orders: launch of the programme to create the Tetra secure interforce digital communications network, as well as significant orders in the area of upgrading Tornado avionics for Saudi Arabia and the UK Ministry of Defence, for the InfraRed Search and Track (IRST) avionics system for the second EFA lot, for communications and command and control systems for the FREMMs, and for communication systems in the UK, particularly for the FALCON programme. The decrease from the previous year is due to the order acquired in June 2005 by Selex Sensors and Airborne Systems Ltd for the production of the Defensive Aids Sub System (DASS) for all Eurofighter Typhoon jets for the second lot (roughly €mil. 1,200).
Revenues: increase attributable to the contribution of the UK avionics component and of Datamat.
EBIT: growth due to the change in consolidated companies and the improvement in business in command and control systems and in security and information technology.

As already detailed above, the agreement signed with BAE Systems (BAE) at the end of April 2005 deeply altered the structure of Finmeccanica's Defence Electronics division. This agreement entailed:

- the formation of a new company, Selex Sensors and Airborne Systems S.p.A., 75% owned by Finmeccanica and 25% owned by BAE Systems, which groups together the activities of Galileo Avionica S.p.A. and Selex Sensors and Airborne Systems Ltd;
- the acquisition by BAE Systems of the military and secure communications business, which was absorbed by Selex Communications S.p.A.;
- the termination of the AMS joint venture and the return of the Italian business, now Selex Sistemi Integrati S.p.A., under full control of Finmeccanica.

From the fourth quarter of 2005, the Defence Electronics division also includes Datamat S.p.A., a group involved in the design and creation of information technology solutions, particularly in the Defence, Space and Government markets. Finmeccanica S.p.A. currently holds a 98.6% stake in Datamat S.p.A., taking account of treasury shares.

Also last year, Finmeccanica S.p.A., through its subsidiary Selex Service Management S.p.A. (SE.MA.), finalised participation in the consortium Innovazione e Progetti S.c.p.A., which is to develop the programme for the realisation and dissemination of the Electronic ID Card.
The different times when these transactions took place, the varying contributions to consolidated results of these new enterprises and a lack of data regarding the prior period performance of the incoming entities means that it has not always been possible to provide a like-for-like comparison of the figures, particularly earnings figures.

The division includes activities concerning the manufacture of avionics equipment and systems, unmanned aircraft, radar systems, land and naval command and control systems, air traffic control systems, integrated communications systems and networks for land, naval, satellite and avionic applications, and private mobile radio communications systems and IT and security activities. This segment also includes Finmeccanica's International Naval Systems division, the contracts of which, as part of the rationalization of business concerning the Orizzonte programme, were transferred to Selex Sistemi Integrati in December 2006.

It should further be noted that, in addition to the realisation of electronic equipment and systems for defence and security, the division also continued its intensive efforts concerning the provision of large-scale integrated systems based on complex architectures and network-centric techniques.
The goal is to meet the increasingly pressing needs of customers to possess large-scale systems that integrate a variety of functions, platforms, and sets of sensors in order to ensure effective performance in the surveillance, control, and protection of critical areas and infrastructures.
To that end, Selex Sistemi Integrati S.p.A. has begun numerous sales campaigns, especially in the export market, in order to promote large-scale homeland protection systems, particularly for applications related to border control and security management in conjunction with major events. This offering involves all of the competencies of the various Group companies and takes advantage of the consolidated presence of a number of these companies in the various countries concerned.

On a worldwide level, the Defence Electronics division is taking on an increasingly important role within the scope of the entire defence and security industry. This is due not only to its shear size (with a market estimated at some €bil. 56 to €bil. 57 in 2006 and with a 2006-2010 growth rate of 6-7%), but also to the increasing need for coordinated large-scale operations that are making new demands of the armed forces. The goal is to ensure a higher level of intelligence, create a shared awareness among the forces involved, increase command and reaction times, and create the capacity for self-synchronization.
Integrated, secure, broadband communication systems for both military and homeland security applications, information superiority systems and advanced sensors (avionics radar, multipurpose/surveillance radar, optoelectronics, electronic warfare systems) are the fundamental components of the new integrated multi-platform systems (air-to-air and air-to-ground surveillance and airspace management) necessary to satisfy increasing demand from end users for operational solutions. There is an increasing interest in dual-use systems and solutions (personal mobile radio, software-defined radio, etc.) and for battlefield and training simulation systems.
The demand for defence electronics systems is being driven by the gradual introduction of a new category of complex systems (i.e. systems of systems) based on the integration of various types of platforms (fixed-wing and rotary aircraft, unmanned systems, ground vehicles, etc.), as well as on the need to reduce threat reaction times (i.e. sensor-to-shooter) and on the development of a new type of system based on common network-centric digital data communication architectures.
Global demand is also conditioned upon the continuation of the leading international programmes for traditional aeronautic platforms, both fixed-wing and rotary-wing (both the latest generation multi-role programmes and specialized programmes for combat or naval uses) and upon the development of new unmanned platforms, both in Europe and in the US.
Another determinant factor is the development of avionics systems with open architectures for the gradual introduction of advanced subsystems throughout the platform's operating life (e.g. JSF).
We are also seeing signs of a gradual development of programmes to upgrade avionics, with important opportunities for the provision of radar systems, optoelectronics, and self-protection systems.
In the naval sector, demand is being driven by the need for combat management systems that are scalable, modular, and interoperable and that can be integrated into next generation systems (deepwater, littoral combat, etc.) for close-to-shore operations and defence from low radar cross section threats.
In a landscape in which security plays a key role, demand for homeland security systems is becoming increasingly pressing (with a market estimated at some €bil. 55 to €bil. 60). This segment is characterized by varying levels of maturity. In the US, the customer is well defined and has taken a long-term view with related funding, whereas in Europe the approach is much more fragmented, given that there is not yet a centralized body coordinating initiatives in national security.
As part of its Seventh Framework Programme, the European Commission expects to fund a broader range of research programmes, which will begin in 2007 (with the European Security Research Program). EU Member States have also reached unanimous agreement on a series of anti-terrorism measures, including the creation of specialized task forces, the exchange of information between the EU and the US, coordinated intelligence actions, and strengthening of the entire Schengen information system.
The opportunities arising from these new homeland security needs, including the protection of a nation's critical infrastructures and coastal and border control, will enable the Finmeccanica companies operating in the sector to access national and international funding that could compensate for the stagnation of European defence budgets.
With the BAE agreement and the Datamat

acquisition, Finmeccanica has become the number two player in the European Defence Electronics market and has also increased its industrial presence both in Italy and the UK.
The Datamat acquisition and its integration into Elsag has increased the Group's competencies in software development for naval, aeronautical, and helicopter applications and has consolidated the Group's capacity for providing integrated logistics services.
Finmeccanica is now positioned as a systems manager, steering its operations towards the supply of integrated solutions, and now aims to fulfil the role of preferred supplier to large-scale systems integrators, as well as reaching highly attractive markets such as the United States.

At 31 December 2006, **new orders** totalled €mil. 4,197. In December, an agreement was signed with the Italian Ministry of the Interior for the start of the programme to create the Tetra secure interforce digital communications network, which is to be completed in approximately six years and should gradually cover the entire national territory. The other main new orders include the following:

- avionics: particularly significant orders related to upgrading Tornados for Saudi Arabia and for the UK Ministry of Defence, as well as the initial success on the international market of the ATOS surveillance systems (Q4), which join the new orders for the EFA (Eurofighter Typhoon) programme for the provision of some 200 Infrared Search and Track (IRST) PIRATE systems for the vehicles of the second lot (Q1 and Q2); logistics activities and work on the Defensive Aids Sub System (DASS); development of the Helicopter Integrated Defensive Aids System (HIDAS) for AgustaWestland's Future Lynx helicopters; and activities as part of the Capability Sustainment Plus programme for the EH 101 Merlin helicopter and the provision of Mirach 100/5 targets;
- land and sea command and control systems: orders for the FREMMs related to the Combat Management System (Q3); other command and control systems and the Empar radar for the frigate missile systems (Q1); the new order by the Yemen government for a complete VTS system (Q4); additional orders for the Poland VTS project; and the Libyan order for patrol boats.
- Air-traffic control: ENAV orders in the domestic market; the provision of radar to 5 locations in Kota Bahru, Malaysia (Q1); the Systematic Modernization of ATM Resources in Turkey (SMART) related to the creation of 12 control systems plus 19 towers (Q3); the extension of the Pakistan project to a further two sites; and the provision of air-traffic control systems to two new airports in Bangalore and Hyderabad, India (Q4);
- integrated communication networks and systems: the first lot of the Tetra Interpol programme; the order received in December for the Armasat programme for the Italian Carabinieri; the significant orders in the UK for the main strategic communications programme of the UK Ministry of Defence, FALCON; the second batch of Type-45 vessels; the FREMM and EFA communication systems; the provision of a new mobile radio relay station (MRRS) as part of the Theatre Independent Tactical Army and Air Force Network (TITAAN) for the Dutch Armed Forces (Q1 and Q2);
- security and information technology: the EDS order for work on the INPS network (Q4); the Telecom order for the "Rete sicura Poste Italiane" (Poste Italiane secure network); the Poste Italiane "Nuova Rete" (new network) order variation (Q2); the "hybrid mail" order from the Russian postal service (Q3); the automation of postal service in Greece (Q1); orders concerning the FREMM command and control systems (Q1 and Q2); and the extension of logistics support services to the Italian Air Force.

As at 31 December 2006, total **order backlog** reached €mil. 7,676, half of which related to the avionics division, while activities for radar, command and control systems and communications activities each accounted for approximately 20% of the total.

Revenues came to €mil. 3,747 at 31 December 2006, an increase of 18% or €mil. 583 in absolute terms compared with the previous year. This increase is essentially due to the acquisition of the British avionics business and of Datamat. Revenues increased principally due to the following:

- avionics: the continuation of activities relating to DASS production and the production of avionics equipment and radar for the first and second lots of the EFA programme, as well as systems for countermeasures, avionics for the helicopter programmes, devices for the space segment, and Grifo combat radar and PAR systems;
- radar and command and control systems: the continuation of activities relating to contracts with the Italian Navy, particularly for naval systems on the Nuova Unità Maggiore vessel and for the modernisation of the Maestrale Class and De La Penne frigates; FSAF and Orizzonte international cooperation contracts; the Baynunah contract with the United Arab Emirates; the continuation of activities for the Nato FADR land-based radar; the MEADS programme; and air traffic control programmes both in Italy and abroad;
- integrated communication networks and systems: activities relating to the development and manufacture of equipment for the NH90 and EFA aircraft (V/UHF, MIDS interface unit, interrogator, transponder); the provision of communications systems for the FREMMs and Type-45 vessels; radio systems for NATO's AWACS aircraft; and the production of personal role radios;
- security and information technology: activities related to the security segment, systems and automation services – particularly for the Italian and Russian postal services – and the information technology division for defence programmes.

EBIT at 31 December 2006 came to €mil. 300 for an increase of €mil. 31 over the same figure posted for December 2005. This growth is the result of both the change in consolidated companies, as well as of the improvement in command and control systems and in the security and information technology segment, which benefited from the increase in industrial profitability as a result of the strategic repositioning of Elsag and the sale of a number of properties. As a result, **ROS** at 31 December 2006 came to 8.0% for a half percentage point drop from 31 December 2005.

Net invested capital at 31 December 2006 came to €mil. 2,778, an increase of €mil. 624 over 31 December 2005 due to the increase in capital assets relating to goodwill recognised in relation to BAE's avionics business (€mil. 326) and Datamat (€mil. 64). **Working capital** benefited from the improvement in the UK avionics component and fell by €mil. 68 from the figure posted at the end of 2005 to settle at €mil. 734.

Research and development costs at 31 December 2006, amounting to €mil. 541 (€mil. 501 for the previous year), primarily concerned:

- avionics: programmes including the continuing development of the EFA programme concerning the common modules for new electronic-scan radar systems, both for surveillance and combat (Vixen, Captor, etc.), Laser and Electronic Warfare systems (for JSF in particular), the Mission Core System, surveillance systems, and the fine-tuning of prototypes of the UAV FALCO system and sub-systems;
- radar and command and control systems: the development of the modular sea combat system and the new Kronos 3-D naval surveillance radar; the finalization of long-range fixed (FADR) and deployable (DADR) 3-D land-based surveillance radar; and work on the EUROCONTROL and European Commission contracts for air-traffic control systems;
- integrated communication systems and networks: the start of activities on new product families, such as ad hoc networks, WiMAX, software radio, and switch all IP, along with the continued development of multilevel switching stations for IP-based communications networks, the Future Soldier programme, Sicral network supervision systems, the back-up radio (BuR) for the JSF programme, and the NGIFF interrogators, as well as the continuation of development of Tetra, ARC, and GSMR technologies, whereas completed projects include the study, development, and creation of automatic flight control systems (AFCSs) for helicopters and broadband UAV data link;
- security and information technology: the development of the range of Secure Access Systems, the improvement of the performance of the main postal automation machines, the development of a digital terrestrial TV set-top box, and the development of a next generation mobile licence plate reading system.

At 31 December 2006, there were 19,185 **employees**, representing a decrease of 601 employees from 31 December 2005, related essentially to the information technology and security division due to the sale of Elsag Gest S.p.A., Elsag STI S.p.A., Elsag Business Process S.r.l., and the ERP division of Datamat Soluzioni per le Imprese S.r.l., as well as the workforce reduction under way in the communications area.

4. Performance by division

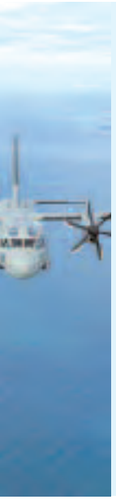
Aeronautics

Main data

€millions	31 December 2006	31 December 2005
New orders	2,634	3,230
Order backlog	7,538	6,865
Revenues	1,908	1,789
EBIT	203	166
R.O.S	10.6%	9.3%
Working Capital	(1,034)	(764)
Net invested capital	(249)	(227)
R.O.I (*)	insig.	insig.
Research and Development	486	405
Employees (no.)	12,135	11,198

(*) Calculated on invested capital at period-end.
insig.: insignificant

Note that the figures for the GIE-ATR consortium are consolidated on a proportionate basis at 50%.



HIGHLIGHTS

New orders: important new orders both in the military segment, with exports of the C27J, ATR ASW, and MB339 craft, and in the civil segment, with a further 100 B787s ordered by Boeing and positive trends in new ATR orders by the GIE-ATR consortium.
Revenues: civil production higher for ATR craft and aerostructures.
EBIT and ROS: both higher due to the greater contribution of the civil programmes and the reduction in risk due to the positive trends in sales and in the commercial outlook for the ATR programme, which have resulted in the release of an excess portion of the provision that had been accumulated. The use of this provision was partially offset by the worsening of Alenia Aeronavali S.p.A. related primarily to the allocation of charges on contracts and the expensing of development costs.
Working capital: improved due to the increase in advances received from the Eurofighter consortium for the EFA and from Boeing for the B787, which offset the increase in capital assets due to higher levels of investment.
The Aeronautics division includes Alenia Aeronautica S.p.A. (production of military aircraft for combat, transport and special missions, as well as civil applications such as aerostructures and regional turboprop aircraft) and its subsidiaries, including: Alenia Aermacchi S.p.A. (production of military training aircraft and engine nacelles for civil aeronautics), Alenia Aeronavali S.p.A. (aircraft conversions and maintenance), and the GIE-ATR consortium, in which a 50% equity stake is held (marketing and assembly of ATR aircraft).

In the global military market, the area of combat aircraft, specifically last-generation multi-role aircraft designed both in Europe and the United States, will continue to represent the largest share of demand. This will also include the expected growth in programmes for updating aircraft to improve and prolong the working life of active fleets. Moreover, the new operating requirements for international operations and the demand for protection and security are underpinning demand for aircraft designed for transport, special missions (airspace and battlefield surveillance, sea patrol, tankers, etc.) and for a new generation of advanced training aircraft. In the medium to long term, the most important development in the military sector will be the development of unmanned systems, for which major programmes are under way in Europe and the United States.
In Europe, the main military programme is the Eurofighter Typhoon (EFA) managed by an international consortium in which Alenia Aeronautica S.p.A. has a 21% holding. Of particular importance for the commercial performance of the craft is the preliminary agreement reached at the end of December 2006 between UK and Saudi Arabia, whereby Saudi Arabia will purchase 72 Eurofighters. Furthermore, during the first half of 2006, the Eurofighter Typhoon consortium, along with other competitors, replied to a request for information (RFI) by the Turkish government for 120 craft.

Between the end of 2006 and the first part of 2007, as part of the JSF-F35 programme, a large part of the nations participating in the development phase, including Italy, signed on for the production phase, committing to incur the programme's development costs and indicating the number of craft to be purchased. Italy expects to purchase 131 craft and to achieve industrial returns that are essentially equivalent to the value of the products supplied. Alenia Aeronautica S.p.A., which is already working on the design of the wing box, is negotiating with the prime contractor, Lockheed Martin, to define additional opportunities for involvement in the development and manufacturing phases.

In the Unmanned Air Vehicle/Unmanned Combat Air Vehicle (UAV/UCAV) sector in Europe, on 15 February 2006, the French government completed negotiations with the other European partners (Italy, Greece, Sweden, and Switzerland) for the development and production of the UCAV demonstrator known as Neuron. Alenia Aeronautica S.p.A. is already involved in these activities, having signed the contract with the prime contractor, Dassault, on 21 April 2005 for participation in the programme.

In the military transport craft segment in 2006, Alenia Aeronautica S.p.A. achieved important commercial successes with the sale of 5 C27J craft (plus three options) to Bulgaria and 3 to Lithuania. With these orders, the programme has reached a total of 32 orders (plus 6 options), and further promotional activities are under way in various countries, including Romania, the Czech Republic, and Slovenia.

Furthermore, as regards sales of the C27J to the US, in June 2006 the proposal was submitted in response to the request for proposal (RFP) related to the joint programme of the US army and air force known as the Joint Cargo Aircraft (JCA). In August 2006, after an initial selection process, EADS-CASA's C27J and C-295 are the only aircraft to remain in the running. The provision could increase to more than 200 aircraft if the US air force confirms the selection of the C27J for its own needs. Partnering with Alenia Aeronautica S.p.A. are both L3 Communications and Boeing Integrated Defense Systems, the latter of which will be involved in producing the final line of the C27J in the US if the craft are selected.

In 2006, the main activities in the military division were as follows:
- Alenia Aeronautica S.p.A.: EFA development, production, and logistics with the delivery of 8 craft to the Italian Air Force; activities for the C27J craft, particularly production for Greece, for the Italian Air Force, and for Lithuania, for which the first craft was delivered at the end of December; the continuation of the Tornado retrofit pre-mid-life upgrade and the AMX avionics upgrade (ACOL); design activities for the JSF craft commissioned by Lockheed Martin; modifications to the third ATR 42 MP craft for the Italian *Guardia di Finanza*; and testing for the Sky-X UAV prototype;
- Alenia Aermacchi S.p.A.: production and logistical support for the MB339 and SF260 training aircraft, further development of the new M346 training aircraft, and studies for the M311 aircraft;
- Alenia Aeronavali S.p.A.: development and production for the B767 tanker programme, overhaul and logistical support for the B707 tanker and AWACS aircraft, and G222 return to airworthiness.

On the worldwide civil market, in addition to the positive impact of the increase in air traffic, new models of aircraft featuring advanced performance and new technological solutions are about to enter production, offering excellent growth opportunities for those companies that design and build structural components. The general trend also continues among prime contractors to outsource an increasing proportion of their business. Alenia Aeronautica S.p.A. is participating in new development programmes, involving major responsibilities, with both Boeing and Airbus, and is involved in talks to take part in future programmes as well.
In 2006, expectations for further development of air transport and the expanding role of low-cost carriers led to a considerable increase in production rates and in aircraft deliveries by both Boeing and Airbus.

At the end of 2006, as regards the new B787 aircraft, for which Alenia Aeronautica S.p.A. is involved in the development and production of major fuselage segments in composite materials, as well as assembly and integration, Boeing received orders for a total of 448 aircraft from 33 commercial airlines. In a joint venture with the US firm Vought Aircraft Industries, Alenia Aeronautics S.p.A. will produce roughly 60% of the fuselage, acting as the independent prime partner.

For regional aircraft in the turboprop division, which is experiencing a period of marked expansion due in part to the growing demand from low-cost carriers, the GIE-ATR consortium again achieved important commercial success in 2006, recording sales of 63 aircraft.

In November 2006, Finmeccanica and Sukhoi Aviation Holding, and their respective subsidiaries Alenia Aeronautica S.p.A. and Sukhoi Civil Aircraft Company (SCAC), signed a strategic partnership agreement for the Superjet 100 programme. Based on this agreement, Alenia Aeronautica S.p.A. will acquire a 25% plus one share stake in SCAC and a corresponding share of the financing for the development of the Superjet programme for a family of next-generation 75-100 seat regional jets. Alenia Aeronautica S.p.A. and Sukhoi will also establish a joint venture (51% Alenia Aeronautica S.p.A and 49% Sukhoi Civil Aircraft Co.) either in

France or in Italy, which will be responsible for marketing, sales, and delivery for the western hemisphere, as well as post-sales assistance for the aircraft throughout the world.
Alenia Aeronautica S.p.A. will also contribute to developing the programme with its technical competencies and will produce parts and components using advanced composite materials, while also handling aspects related to aircraft certification in Europe.

With regard to Airbus, talks are under way to research new opportunities for collaboration, such as participating in the production of the new A350 aircraft and additional activities involving the aircraft currently in production.

In 2006, the civil activities of Alenia Aeronautica S.p.A. mainly involved the following orders:
- Boeing: production of components for fuselages and control surfaces for the B767 and B777 aircraft. For the new B787 aircraft, development and sales activities continued, as well as the start of the first manufacturing activities at the new facilities at Grottaglie (central sections of the fuselage) and Foggia (horizontal tail wings) at the end of 2006. Furthermore, at the new Global Aeronautica LLC (a joint venture with Vought Aircraft Industries) facilities in Charleston, South Carolina, the sections of the fuselage manufactured will then be assembled;
- Airbus: the design of components for the central section of the fuselage of the A380, of the tail cone for the A300, of mechanical wing components for the A340, and of a fuselage section for the A321;
- GIE-ATR, in partnership with EADS-ATR: the production of the ATR 42 and 72 turboprops;
- Dassault Aviation: the fuselage section of the FALCON 2000 Extended Range and the engine nacelles for the FALCON 900EX.

The activities of Alenia Aeronavali S.p.A. involved the transformation from passenger to cargo craft of the MD10, MD11, B767, and ATR, while those of Alenia Aermacchi S.p.A. concerned the production of engine nacelles.

New orders in 2006 totalled €mil. 2,634, as compared with the €mil. 3,230 of the previous year, which benefited from substantial orders including the first 200 units of the B787 order. The main orders received during 2006 included the following:
- in the military segment: new orders for 10 ATR72 ASW aircraft for sea patrol and anti-submarine uses to the Turkish navy; 5 C27Js to Bulgaria; 3 C27Js to Lithuania; AMX logistics activities; orders related to the EFA, JSF, and Tornado programmes; the provision of 8 MB339 training craft to Malaysia; and the maintenance and upgrading of the avionics of 12 MB339 aircraft already in use by Nigeria;
- in the civil segment: orders to Boeing for an additional 100 B787s; those of the GIE-ATR consortium which received orders for 63 aircraft (of which 15 ordered by the Indian airline Kingfisher, 10 by the Irish airline Aer Arann, and 7 by the Brazilian Trip Air); and the additional lots of the A380, B777, B767, and FALCON programmes, engine nacelles, and transformations of the MD10 and B767 aircraft.

The **order backlog** as at the end of 2006 came to €mil. 7,538 with a significant portion for the EFA (46%), B787 (23%), C27J (5%), and AMX (4%) programmes. The backlog grew by €mil. 673 from the €mil. 6,865 at the end of 2005, and is expected to continue expanding over the medium to long term.

Revenues for 2006 came to €mil. 1,908, representing an increase of €mil. 119 compared with the €mil. 1,789 recorded for 2005. As forecast, civil activities contributed to this growth with increases in ATR, A380, B777, and Falcon sales and manufacturing and the launch of production on the first B787s at the end of the year. Production for Alenia Aermacchi S.p.A. and Alenia Aeronavali S.p.A. was lower, having been affected, in particular, by the reduced aircraft business with the Italian air force for the completion of the MB339 and SF60 aircraft orders and for a decrease in overhaul activities for the B707 tanker and inspections for the Brequet Atlantic, respectively.

EBIT at 31 December 2006 came to €mil. 203 for an increase of €mil. 37 over the €mil. 166 posted at the end of the previous year, as well as an increase in **ROS**, which went from the 9.3% of 2005 to 10.6% in 2006. Contributing to this improvement in EBIT, which benefited from the growth in civil production, were both Alenia Aeronautica S.p.A. and the GIE-ATR consortium. For the latter, the reduction in risk due to the positive trends in sales and in the commercial outlook for the ATR programme has resulted in the release of an excess portion of the provision that had been accumulated. This result was partially offset by the worsening of Alenia Aeronavali S.p.A. related primarily to the allocation of charges on contracts, the expensing of development costs, and lower than expected productivity. Given these performance trends, at the end of 2006, Alenia Aeronavali S.p.A. launched a plan for reorganization and efficiency improvements. Similarly to the previous year, EBIT and profitability benefited from the conclusion of negotiations, which resulted in the acquisition of the expected payments from Boeing for the close of production.

Working capital at the end of 2006 came to a negative €mil. 1,034, down €mil. 270 from 31 December 2005 (a negative €mil. 764), which can be attributed to the increase in advances received on a number of military programmes, primarily the second lot of the EFA programme and on the B787 received from Boeing.

Net invested capital as at 31 December 2006 came to a negative €mil. 249 and remained essentially in line with the same figure at 31 December 2005 (a negative €mil. 227). This trend is related to the aforementioned change in working capital, which offset the increase in capital assets resulting from net investments for the year, particularly investments related to the new facilities in Grottaglie, equipment and machinery for the start of B787 production, and for non-recurring activities during the year involving programmes being developed and industrialized.

Research and Development costs for 2006 totalled €mil. 486, up from the €mil. 405 of 2005, and reflect the level of commitment to the B787, C27J, M346, EFA, with the related activities for the second lot, Tornado, AMX, UAV, A380, engine nacelles, and B767 tanker programmes. Technical research and development also continued along two main strands, namely aerostructures and systems integration.

The number of **employees** at 31 December 2006 stood at 12,135, representing an increase of 937 over the 11,198 employees at 31 December 2005. This increase was due primarily to new hires by Alenia Aeronautica S.p.A. in order to meet the needs of higher workloads, particularly for engineering and new programmes, as well as to the first 100 employees hired for the Grottaglie facilities of the subsidiary Alenia Composite S.p.A.

4. Performance by division

Space

Main data

€millions	31 December 2006	31 December 2005
New orders	851	599
Order backlog	1,264	1,154
Revenues	764	735
EBIT	44	26
R.O.S	5.8%	3.5%
Working Capital	(66)	(18)
Net invested capital	318	309
R.O.I (*)	13.8%	8.4%
Research and Development	64	79
Employees (no.)	3,221	3,194

(*) Calculated on invested capital at period-end.

Note that the information at 31 December 2005 includes the first 6 months of activity of the companies Alenia Spazio and Telespazio, both wholly-owned subsidiaries, and the following 6 months of activities concerning the two new joint ventures (Alcatel Alenia Space S.A.S. and Telespazio Holding S.r.l.), consolidated using the proportionate method at 33% and 67%, respectively, while the figures for 31 December 2006 refer to the two new joint ventures. Therefore, the figures for 2006 cannot be compared with those of the previous year.

HIGHLIGHTS

New orders: up more than 42% from the same period of 2005 thanks to the strong performance of the commercial telecommunications satellites segment and the solid performance of satellite services.
Order backlog: up some 10% over 31 December 2005 due to the increase in new orders. The order backlog, based on the amount of work ready to begin, guarantees coverage of approximately 70% of production expected for the coming year.
EBIT: significant increase over the previous year (+69%) due to increased production efficiency and a lower level of restructuring provisions, net of higher labour costs in France.

Finmeccanica S.p.A. operates in the space industry through two companies (held together with Alcatel), one dedicated to satellite services (Telespazio Holding S.r.l., headquartered in Italy with its main production facilities in Italy, France and Germany, in which Finmeccanica S.p.A. holds a 67% stake) and the other to manufacturing (Alcatel Alenia Space S.A.S., headquartered in France with its main production facilities in France, Italy, Belgium, and Spain, in which Finmeccanica S.p.A. holds a 33% stake).
Telespazio Holding S.r.l. and its two subsidiaries focus on defence and security services, as well as navigation, infomobility, earth observation, the provision of telecommunications networks and services, the management and orbital control of satellites and of terrestrial centres, and multimedia and high-value applications.
Alcatel Alenia Space S.A.S. focuses on the design, development and production of space systems, satellites, orbital infrastructures, space transport systems, equipment, instruments, and terrestrial systems for civil and military applications.

In the satellite market (both commercial and governmental), following on the technological progress that has led to an increase in the operating life of satellites and an excess in satellite capacity available at a lower cost, recent years have seen a decline in demand and have been difficult for the leading US and European space-related firms, which have had to reorganise and consolidate in order to be more competitive. Nonetheless, 2006 showed signs of recovery with, for example, new orders for 34 geostationary satellites, 24 of which within the commercial segment alone, and the outlook for the coming years in terms of satellite launches (commercial, governmental, civil and military) confirms this slight recovery in the market, despite the lack of further significant technological innovations. This growth will likely be driven by the launch of the Galileo constellation (2009-2011), the replacement of a number of commercial satellites (particularly in geostationary orbit) that have reached the end of their operating lives, and the development of micro- and nano-satellites.
Excluding the management costs of the agencies and launch centres and certain types of advanced research done by specialist centres, some 50% of the global market for space systems and services is focused on manufacturing, with 35% on services. In the manufacturing segment (primarily satellites, launch systems, manned orbital infrastructures, and ground segments), the government market is the leading component, with higher growth forecasts than for the manufacturing of systems for commercial applications. In particular, the greatest growth is expected in the military segment thanks, above all, to security investment in the US and for similar initiatives in Italy and the rest of Europe. However, we are also seeing increasing involvement by governmental and civil intergovernmental bodies through funding for certain strategic programmes, such as the Galileo satellite navigation and global positioning system and the Global Monitoring for Environment and Security (GMES) system. Driven by this comes the development of national remote sensing programmes (Pleiades in France and Cosmo-SkyMed in Italy, for which the first two satellites are expected to be put into orbit in 2007) and military telecommunications (Sicral 1B in Italy, Syracuse 3C and Helios II in France).
Interplanetary space exploration and the new moon race have taken on new life, with the involvement not only of the US (with the Constellation Program), the EU, and Russia (with the Russian space agency Roscosmos seeing a considerable increase in its budget), but also emerging powers in the space race such as China, Japan, and India. More than 60% of the satellite services market targets commercial television broadcasting and telecommunications services, which are the most consolidated businesses. This segment is characterized by the joint presence of market players that, having their own satellite capacities, are able to work directly with the end user and competitors that resell satellite capacity to the end user at much lower margins. Whereas in the manufacturing segment competition revolves around a limited number of large-scale global players, the services segment is more fragmented on the supply side, with a great many local players that are often active in limited product niches.
Given that the commercial segment is highly saturated, development for the market over the medium term should come from important government programmes, with a key role being played by the aforementioned European initiatives for navigation and global positioning (Galileo), and security and earth observation (Cosmo-SkyMed and GMES). Many of these programmes also have high “dual” capacities and extensive user bases in both the civil and military segments. Over the longer term, further developments are expected in high-value broadband telecommunications services based primarily on interactive video applications (distance learning, telemedicine, and integrated voice, data and image communication) and on operations (management and orbital positioning services).

With regard to the Galileo programme, on 19 January 2006, a contract was signed in Berlin between the European Space Agency (ESA) and European Satellite Navigation Industries (formerly Galileo Industries and a company in which Finmeccanica, EADS Astrium, Thales S.A., and Galileo Sistemas y Servicios all have an interest) worth some €bil. 1 for the development and construction of the first four satellites and the associated ground infrastructure (In-Orbit Validation stage, 2005-2009, with an estimated value of €bil. 1.6). The Galileo project, which is the response of the EU and the ESA to the American GPS satellite system, includes the involvement of Telespazio, as well, in the provision of services related to launching the satellites, putting them into orbit, and managing the subsequent operations.
In addition to the production of the Galileo Constellation (the fully operational capability phase, 2007-2011, estimated at €bil. 2.2), Finmeccanica is involved in the grouping born out of the merger of the two consortiums Eurely (comprised of Finmeccanica, Alcatel, AENA, and Hispasat) and iNavSat (comprised of EADS, Thales, and Inmarsat) currently involved in negotiating the contract for the system’s operations. This grouping is currently being incorporated in order to establish a dedicated contracting firm. The public-private partnership scheme adopted by the European Commission to manage the Galileo programme is currently being reconsidered by the various public and private stakeholders in order to either confirm or revise it by mid-2007, which should led to more efficient and more effective management of the programme, for which the strategic priority for Europe was recently reiterated in a letter by Commissioner Barrot to the Transport Council and to the companies. Any delays in finalising these agreements could lead to delays in programme activities and could, therefore, impact upon the profitability of the entire programme.
Finmeccanica’s involvement in the contracting company represents a key opportunity for the satellite services business, thereby enabling the Group to play a leading role in a project of global importance and strategic to new value-added applications (such as public regulated services, or PRSs, infomobility, security, etc.). Indeed, with a constellation of 30 satellites in three separate medium earth orbits (MEOs) at 24,000 km above the Earth’s surface, with 9 satellites in each orbit, in addition to one backup satellite, Galileo will guarantee high-precision positioning services for air, sea and land satellite navigation applications.
An important milestone in the project has also been reached with Italy being assigned one of the two Constellation Mission Control Centres, the infrastructure of which is to be built by 2008 at the Fucino Space Centre based on the convention signed by Telespazio and the Region of Abruzzo.
Italy has also been assigned the Performance Evaluation Centre, which is to be created near Rome making use of the competencies of Telespazio, Galileo Industries Italia, and the Galileo Test Range (GTR), the centre of technological excellence in satellite navigation, which includes a controlled environment that is able to reproduce

the main characteristics of the Galileo system in terms of its navigation signals, services, and performance. The first stage of the creation of the GTR has been entrusted by the Region of Lazio, via Filas S.p.A., to the temporary business grouping comprised of Telespazio S.p.A. (as agent), Alcatel Alenia Space Italia S.p.A. and Finmeccanica S.p.A. (as principals).

Furthermore, in September 2006, Telespazio S.p.A., together with Telecom Italia, Hughes, and Intelsat, announced the creation of the new "Marco Polo" satellite platform for the provision of value-added broadband services for the business and government markets in eastern Europe and northern Africa. The platform, which is based on the capacity of the Intelsat IS-901 satellite, is being managed by Telespazio at its own Fucino Space Centre.
From a commercial perspective, in 2006, the group acquired **new orders** of €mil. 851, up €mil. 252 from the same period of 2005 (€mil. 599), thanks, above all, to the recovery in the commercial telecommunications satellites market and the strong performance of satellite services, particularly for defence and telecommunications. The most significant new orders for the period were:

- in the commercial segment: orders related to the Turksat 3A (Q1) and Ciel 2 (Q1) telecommunications satellites and the Eutelsat orders for the W2A (Q3 and Q4) and W7 (Q4) satellites; the first lot in the provision of 48 low-earth orbit (LEO) satellites for the Globalstar second-generation constellation (Q4); the orders related to the payloads for the Kompsat (Q1), Arabsat 4AR (Q2), and AMC21 (Q2) satellites, and for the provision of two payloads for the Express AM33/44 programme (Q3), as well as two altimeter radar systems as part of the Siral 2 programme (Q3); the renewal of the multi-year contracts for TV services, particularly W3/Express for RAI (Q1 and Q2); new orders for satellite orbit management, particularly for Eutelsat AB1 and Satelcom Geo (Q1); and new orders for the provision of telecommunications satellite services (Q2) and terrestrial centre management (Q4);
- in the military segment: orders related to the BW Satcom programme for the provision of two telecommunications satellites to the German Ministry of Defence (Q3); the further lot (MAP2 contract) related to the Sicral 1B satellite to the Italian Ministry of Defence (Q4); and new orders for the provision of security and defence networks and services (Q4);
- in the earth observation segment: the contracts related to the Cosmo programme for the launch of the first three satellites and the first lot for the production of the fourth satellite (Q4); new orders for the provision of services, particularly the Agrisian contract (Q2);
- in the navigation and infomobility segment: additional orders related to the Galileo (the in-orbit validation phase) and EGNOS programmes (Q2 and Q4);
- in the science programmes segment: the additional lot related to the Herschel/Plank programme (Q1) and new orders in the equipment and transport infrastructures sector (Q2).

At 31 December 2006, the **order backlog** for the division totalled €mil. 1,264, an increase of €mil. 110 over the same figure as at 31 December 2005 (€mil. 1,154). The order backlog, based on the amount of work ready to begin, guarantees coverage of approximately 1.6 years of production. The backlog at 31 December 2006 is composed of manufacturing activities (50% satellites and payloads, 14% infrastructures and equipment) for 64% and satellite services for the remaining 36%.

Revenues for 2006 came to €mil. 764, an increase of €mil. 29 over the previous year (€mil. 735) due essentially to the higher level of production in the manufacturing segment. The principle sources of production revenues were:

- the start of activities for the project related to the telecommunications satellites Turksat 3A, Ciel 2, BWSatcom, W2A, and W7, the satellites of the Globalstar Constellation, and phase 1 of the third-generation Meteosat programme;
- the continuation of activities relating to:
  - the Cosmo-SkyMed and Pleiades earth observation programmes;
  - the StarOne C1/C2, Alphabus, Thaicom 5, Chinasat 6B/9, Galaxy 17, Rascom and Koreasat 5 commercial satellites;
  - the Syracuse and Sicral 1B military telecommunications satellites;
  - science programmes (Alma, Goce, and Herschel/Plank);
  - the Galileo and EGNOS navigation programmes;
- the continuation of the programmes connected with the International Space Station;
- the development of equipment and devices for EQS France/Italy and for the Koreasat 5 satellite, and the payloads for the Arabsat 4A/4B/4R, Express AM33/34, and AMC21 satellites, and Kompsat radar;
- the provision of defence services and telecommunications satellite networks, and, in the television sector, the resale of satellite capacity and provision of value-added services using the digital platform;
- the provision of earth observation products and services, as well as satellite orbit and terrestrial infrastructure management.

EBIT at 31 December 2006 was €mil. 44, representing an increase of €mil. 18 compared with the figure posted at 31 December 2005 (€mil. 26), due to synergies resulting from joint ventures and lower provisions for restructuring, net of increased labour costs. Given the above, **ROS** improved significantly, passing from 3.5% for 2005 to 5.8% for 2006.

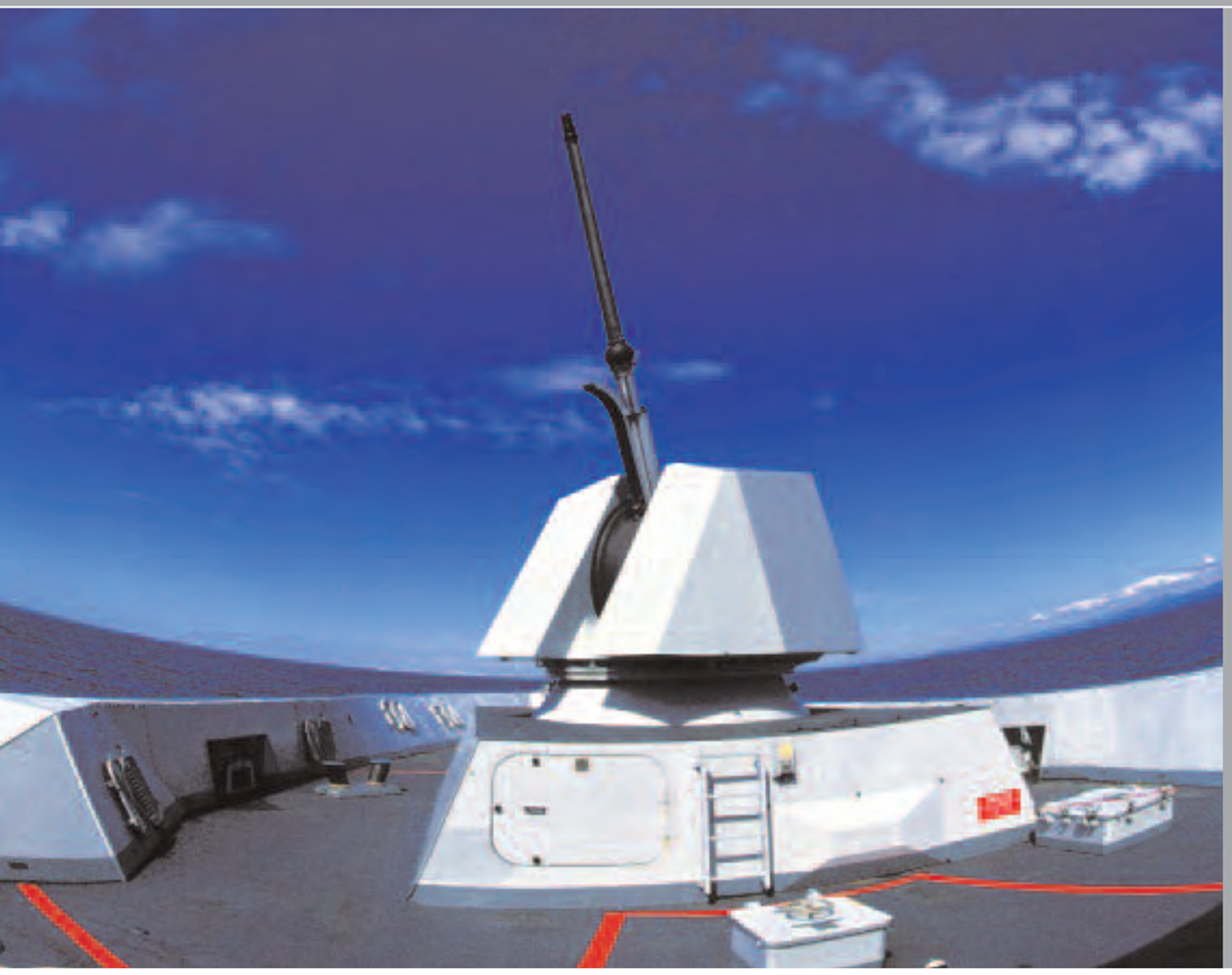
Net invested capital at 31 December 2006 came to €mil. 318, for an increase over 31 December 2005 of €mil. 9, attributable primarily to capital assets, while **working capital** of a negative €mil. 66, posted a decrease for 2006 of €mil. 48 from 31 December 2005 (a negative €mil. 18) due primarily to a reduction in trade receivables and net inventories related to greater receipts on trade receivables, as well as in increase in trade payables in the manufacturing segment.

Research and Development costs for 2006 came to €mil. 64, down roughly €mil. 15 from the same figure of 2005 (€mil. 79) primarily as a result of the synergies achieved with the establishment of joint ventures. Key activities in this area included:

- research and development phases for programmes such as:
  - Syracuse 3, Sicral 1B, and Sentinel 1 (SAR radar, altimeter and radiometer);
  - dual-use systems for security and civil protection (Cosmo and Sentinel);
  - science programmes (Alma, Spirale/Melissa, Bepi-Colombo, Goce, and Herschel/Plank);
- the development of:
  - platforms and solutions for the provision of navigation and infomobility services (Galileo and GNSS), as well as dual-use civil and military navigation systems;
  - emergency and security systems (GMES);
  - algorithms and processors for the production of earth observation data (Cosmo) and GIS platforms;
  - flexible payloads in the C/Ku band for new mobile TV applications;
  - C4 and B2 spacebus platforms (from 2008), platforms for LEO applications, and further developments in the SB4000 platform for GEO applications;
  - production technologies (equipment, micro-gravity payloads, etc.), particularly for mobile and/or broadband applications;
  - architectures and technologies for radar and optical instrumentation;
- studies relating to:
  - future experiments on board the International Space Station;
  - capsules, orbital infrastructure and manned re-entry craft;
  - advanced telecommunications solutions (networks and architectures).

At 31 December 2006, the number of **employees** totalled 3,221, for an increase of 27 over the 3,194 of 31 December 2005 due both to the consolidation of Mars S.r.l., a subsidiary of Telespazio S.p.A. which was previously consolidated using the equity method, as well as to delays in France in the implementation of the approved Alcatel Alenia Space S.A.S. restructuring plan.

4. Performance by division



Defence Systems

Main data

€millions	31 December 2006	31 December 2005
New orders	1,111	763
Order backlog	4,252	3,869
Revenues	1,127	1,143
EBIT	91	112
R.O.S	8.1%	9.8%
Working Capital	(374)	(321)
Net invested capital	104	111
R.O.I (*)	insig.	insig.
Research and Development	279	268
Employees (no.)	4,275	4,104

(*) Calculated on invested capital at period-end.
insig.: insignificant

Note that the figures relating to the MBDA S.A.S. joint venture have been consolidated on a proportionate basis at 25%.

HIGHLIGHTS

New orders: important commercial successes in the land-based and naval weapons and missiles segments, particularly for the contract to provide the Italian army with armoured combat vehicles through the IVECO FIAT -Oto Melara S.c.r.l. consortium.
EBIT: lower due to a contraction in production volumes and a reduction in profitability in the underwater systems segment.

Defence Systems includes MBDA S.A.S. for missile systems, the joint venture with BAE Systems and EADS in which Finmeccanica S.p.A. holds a 25% stake, Oto Melara S.p.A. for land, naval and air weapons systems, and WASS S.p.A. in underwater weapons (torpedoes and counter-measures) and sonar systems.

In February, as part of the integration of the European missiles industry, MBDA S.A.S. finalised the acquisition of the German firm LFK GmbH, which was consolidated as of 1 March 2006.

The Defence Systems division continues to show strong cyclical demand associated with the progress made in the division's main programmes.

In the missiles division, global demand is estimated at some €13 billion per year, roughly half of which for new missiles and the rest for systems and logistics. The main drivers of growth in demand are the production of new platforms (multi-role aircraft, helicopters, and surface vessels), both in Europe and the US, with additional opportunities in certain countries of the Middle East, Asia, and the Pacific rim, as well as the new requirements for air-to-surface missiles and smart bombs for precision attacks, used primarily in peace enforcement operations. Conversely, defence budgets, particularly in Europe, appear to be rapidly contracting, thereby placing considerable limitations on market expansion and making it necessary to formulate more conservative estimates for the production of new missile systems. Air defence systems are the most important segment within the missiles business, accounting for some 35-40% of the global market. In this segment, the previous trend of rapid growth has been largely held back by delays and downsizing of important US programmes (NMD, Thaad). The air-to-surface missiles segment, where traditional systems are showing decline, is showing signs of rapid growth over the short term thanks, in particular, to the mass introduction of a new generation of low-cost, yet highly efficient, guided bombs (using GPS) in "surgical" attack operations. The air-to-air segment will remain essentially stable despite the introduction of a new generation of European-designed missiles, due to the gradual reduction in the number of aircraft delivered, as well as to extremely high integration costs.
Supply in the missiles segment is highly concentrated, both in the United States and Europe. In Europe, MBDA has taken a further step towards rationalising its supply structure thanks to the acquisition of the German company, LFK, in 2006.

In the land and sea weapons systems segment, there is increasingly strong political pressure in Europe towards establishing international partnership programmes. Compared with the other defence segments, this segment has always been characterized by a lack of significant partnership programmes, which are less susceptible to budget cuts, and by the presence of national programmes in response to domestic needs. Recent engagements have helped to revitalize the segment, as they have demonstrated the importance of physically occupying the battlefield and the increasingly stringent requirements of protecting military personnel within the scope of peace-keeping and peace-enforcement operations. This has also led to the initiation of important programmes for the development of a future generation of combat systems based on a network-centric approach, including the US Future Combat Systems (FCS) programme and the British Future Rapid Effects System (FRES) programme. In the vehicles segment, we are seeing a gradual trend of replacement towards the development of armoured and secure vehicles, which are being designed in "families" using a modular approach. The primary needs remain total personnel protection, maximum transportability, and high levels of flexibility in the field.

In recent years, we have seen a recovery in the demand for naval artillery, with the start of upgrade programmes and the development of a new generation of "smart ordnances" with self-guidance capabilities as they approach the target. Despite the increasing development of missile systems (surface-to-air, ship-to-ship, for ground attacks), naval cannons are most used in responding to changes in operating needs, particularly those of security (asymmetric threats, smuggling, drug trafficking). The relaunch of the land and sea weapons systems segment may favour the start of a process of consolidation in supply, as the sector is still fragmented, particularly in Europe. The constant defence budget cuts are making it necessary to begin this process of consolidation in Europe, where we are seeing a gradual penetration by US manufacturers, primarily by acquiring European firms, as well as the creation of the number two player behind General Dynamics as a result of BAE Systems' acquisition of the US firm United Defense.

In the underwater segment, the growing demand for both surface and underwater heavy torpedoes, as a result of programmes to acquire new naval platforms, is also creating greater potential for anti-torpedo countermeasures, as the presence of next-generation systems is making it essential for navies to acquire adequate platform defence systems. The light torpedoes segment, on the other hand, is seeing a decline in the demand for new systems and a consequent increase in demand for updates and upgrades of existing and recently purchased systems. Opportunities for light systems could come from the growing demand for helicopters in combating submarines and surface vessels. Supply in the sector is still highly fragmented, particularly in Europe, with a high level of small and medium-sized businesses both in the torpedoes and anti-torpedo defence systems segments.

In 2006, **new orders** reached €mil. 1,111 for an increase of 46% over 2005 thanks to the successes achieved in the land and sea weapons and missiles segments. The main new orders for 2006 period included the following:

- in missile systems: orders in the fourth quarter for the development and production of 250 SCALP Naval missiles to equip the FREMMs and French Barracuda submarines; for Exocet missile systems to the United Arab Emirates; and the first batch of Mistral anti-air defence missiles to Saudi Arabia, which join the order related to the newly-acquired German component of MBDA for the third-generation Trigat long-range anti-tank missile system to be mounted on German helicopters (Q2), as well as the FREMM missile systems, the Mistral anti-air defence missiles to France, the Taurus long-range air-to-ground missiles (Q3), and customer support activities;
- in the land, sea, and air weapons segment: the order for the provision to the Italian Army of 49 armoured combat vehicles equipped with 25mm HITFIST turrets, 4 special versions, 44 Spike anti-tank missiles, and logistics support (Q4); the order related to FREMM naval weapons for the Italian and French Navies; the first lot of 19 12.7mm Hitrole turrets to be mounted on Puma vehicles for the Italian Army; 6 30mm HITFIST turrets for Ireland; and the provision of 35 additional component kits for the construction of 30mm HITFIST turrets in Poland to be mounted on armoured vehicles for the Polish Army;
- in the underwater systems segment: the FREMM activities and the Black Shark order by the Singapore Navy (Q4).

The **order backlog** as at 31 December 2006 came to €mil. 4,252, more than two-thirds of which related to missile systems, for an increase of approximately 10% over 31 December 2005.

Revenues as at 31 December 2006 totalled €mil. 1,127, which is in line with the previous year thanks to the consolidation of the German component in the missiles segment, which offset the drop in business in underwater systems and the completion in 2005 of important missile programmes related, in particular, to the Mica and Jernas systems.
Revenues benefited from the following activities:

- activities relating to the following: the production of Storm Shadow air-to-surface missile systems for the British Ministry of Defence, SCALP EG for the French Ministry of Defence, and Black Shaheen for exporting; the production of Aster missiles for FSAF/PAAMS systems; the production of MICA air-to-air missiles and

Brimstone anti-tank missiles; the development of Meteor air-to-air missiles; and customer support activities;
- in land, naval and aeronautical weapons systems: the provision of PZH 2000 howitzers to the Italian Army; the production of turrets for the Centauro armoured car for the Spanish Army; and the production of HITFIST turrets for the Polish Army;
- in underwater systems: activities relating to the new Black Shark heavy torpedo and the production of MU 90 light torpedoes.

EBIT for 2006 came to €mil. 91 for a decline of €mil. 21 from 2005 due to the aforementioned contraction in production volumes and the worsening of profitability recorded in the underwater systems segment, which was partially offset by the contribution of the newly acquired German missiles firm. As a result, **ROS** at 31 December 2006 settled at 8.1%, down 1.7 percentage points from the previous year.

Working capital came to a negative €mil. 374 at 31 December 2006 due principally to advances from customers in the missiles segment, for an increase of €mil. 53 over 31 December 2005 (a negative €mil. 321) following, in part, the consolidation of the newly-acquired German firm, which had negative working capital.

Net invested capital as at 31 December 2006 came to €mil. 104 and remained essentially in line with the €mil. 111 of 31 December 2005. This was due, in part, to the recognition of the goodwill related to the acquisition of LFK GmbH (€mil. 43) and investing activities net of depreciation and amortisation, which was offset by the recognition of the share of pension deficit on the plans related to the UK businesses net of deferred tax effects (€mil. 53).

Research and Development costs for 2006 came to €mil. 279 for an increase of 4% over 2005. Some of the key activities included the continuation of development of the Meteor air-to-air missile in the missiles segment, guided munitions in the land and naval weapons segment, and the Black Shark heavy torpedo and the A244 Mod. 3 light torpedo in the underwater systems segment.

At 31 December 2006, the number of **employees** totalled 4,275, for a 171-employee increase from 31 December 2005, due to the acquisition of LFK GmbH (246 employees), which was offset by the continuing effort to reduce the workforce in the missiles segment, particularly in France.

4. Performance by division

Energy

Main data

€millions	31 December 2006	31 December 2005
New orders	1,050	1,032
Order backlog	2,468	2,329
Revenues	978	764
EBIT	63	39
R.O.S	6.4%	5.1%
Working Capital	(282)	(193)
Net invested capital	(254)	(184)
R.O.I (*)	insig.	insig.
Research and Development	17	13
Employees (no.)	2,856	2,529

(*) Calculated on invested capital at period-end.
insig.: insignificant

HIGHLIGHTS

Revenues: the increase is related to the systems-related nature of production for the year and to the service to develop business in scheduled maintenance contracts, as well as current maintenance and the sale of replacement parts.
EBIT: growth due to increased revenues and higher margins on the individual contracts;
Working capital: continued to decline due to the overall improvement in the financial management of contracts, which was favoured by the receipt of significant advance payments on systems orders, as well as to a constant control over payments and collections.

In 2006, Ansaldo Energia S.p.A. concluded a number of important company acquisitions aimed at consolidating the strategic plan undertaken by the company to both significantly develop services through acquisitions of small and medium-sized businesses active in the field and to greatly strengthen its internal technological capacity in support of organizational growth.

Given such a context, in 2006, the following equity interests were acquired:
- an option was exercised for a 55% stake in Energy Service Group AG, a Swiss firm active in on-site maintenance and repairs of Alstom steam turbines and generators. This interest joins the 45% stake previously purchased in 2005;
- the entire equity package of the Dutch firm Thomassen Turbine Systems B.V., a company active in servicing General Electric heavy-duty gas turbines, was purchased from the US Calpine Group;
- as part of the reorganization of Finmeccanica Group business, a 100% stake in Ansaldo Ricerche S.p.A., a company that operates in the field of innovative technology research and testing (particularly alternative energy and energy efficiency), was acquired from SO.GE.PA. S.p.A.

The first two acquisitions listed above will enable Ansaldo Energia S.p.A. to increase its competencies in new technologies, while Ansaldo Ricerche S.p.A., which focuses on areas that are strategic to the Energy division, will provide important support to technological development thanks to its skills in engineering and testing.

As a result of the above, as of the end of 2006, the Energy division is comprised of Ansaldo Energia S.p.A. and its direct subsidiaries, i.e. Ansaldo Nucleare S.p.A., Ansaldo Ricerche S.p.A., Sagemi S.r.l., Asia Power Project Private Ltd, Energy Service Group Gmbh, and Thomassen Turbine Systems BV.

Despite the contraction of the Chinese market (which is inaccessible for Ansaldo Energia S.p.A.), the global power generation market showed slight growth, which was supported by the trend in global energy demand, which is expected to grow at an average annual rate of approximately 4% over the next 5 years. The growth in power consumption and generation will be primarily supported by the high-growth nations in the Middle East (5.4%) and Asia (7.1%), while demand in Europe and North America will remain decidedly lower (at around 2%).

The European market in particular will remain stable in the gas turbine segment, but will see a significant decline in orders for steam turbines starting in 2007, which will be followed by a market recovery for the subsequent five-year period, although at a modest rate of growth. This trend will come from the increasing focus on the environmental impact of power generation systems and on the high costs associated with fossil fuels. Given these environmental needs and the spread of green certificates, power generation systems using renewable sources (particularly hydroelectric power and wind farms) will play a leading role in the power generation market.

The Asian market should post the highest growth rates, even though the Chinese “bubble” burst some time ago. China continues to support high levels of orders for local power generators, while also acting as a great business opportunity for large-scale power companies. For the first nine months of the year, orders reached a total of some 9GW, two-thirds of which from steam-based plants. The considerable gas resources in the Middle East make it one of the leading markets for gas turbines, second only to Europe, with some 5GW of orders for the first nine months. The prevalence of demand for combined-cycle generation reflects the greater penetration of this type of plant even in developing markets in Asia and the Middle East (with roughly 60% of the global gas turbine market).

The global market for power generation services continues to be a driver and to grow at a rate of roughly 6% thanks to new installations that have begun their maintenance schedules, as well as to life-extension and plant conversion projects from steam to combined-cycle.
For these reasons, which have a significant impact on the market for new plants, packages for performance increases and, above all, reductions in toxic emissions are gaining a great deal of commercial ground.
In particular, the competitive landscape is evolving towards an ability to provide services for all technologies. This strategy is being pursued by the leading original equipment manufacturers (OEMs) that service the machinery they install, as well as that of their competitors.
The nuclear market, too, is showing signs of development, particularly in markets with high rates of growth, such as China and India, which will see 5 and 7 new installations, respectively, over the next five years, with a consequent increase in capacity by some 8GW. Interesting opportunities are also expected in the nuclear plant decommissioning market, as plants built in the 1960s and 1970s, particularly in western Europe, Russia, and North America, reach the end of their life cycles.

In such a context, Ansaldo Energia S.p.A. is continuing its focus on growth and, after achieving full technological autonomy in 2005 after the termination of the Siemens licence, has acquired important new orders in Italy that testify to the market’s acceptance of the company as an independent manufacturer.
For Ansaldo Energia S.p.A., the foreign market, where actions tend to be focused on specific targets, is taking on an increasingly important role in achieving the company’s objectives.
In the service sector, Ansaldo Energia S.p.A. can grow by competing locally in a focused manner with determined coverage of its installed base and a gradual extension to the installed base of its competitors (Alstom and General Electric). In particular, the company can grow with respect to the other independent service providers by taking advantage of its technological skills, while both developing partnerships and acquiring other companies in order to accelerate the process of repositioning itself as a full-service provider by expanding its portfolio of capabilities.
The aforementioned acquisitions in 2006 of Energy Service Group Ltd, a company specialized in on-site services, and Thomassen Turbine Systems B.V., a company that provides post-sale services and spare parts for GE gas turbines, are an initial step towards the transformation of Ansaldo Energia S.p.A. into an independent service provider.

As at 31 December 2006, **new orders** reached €mil. 1,050 (with 65% in Italy, 13% in the rest of Europe, and 22% in the rest of the world), for a slight increase of approximately 2% over the previous year, although with a varying distribution among the various business areas, as follows: 52% systems and components; 44% services; and 4% nuclear (at the end of 2005, service orders represented 38% of the total).

The systems and components segment posted a 6% decrease in new orders from 2005. This decline was due to both the decrease in demand for new plants on the domestic market and the company’s policy that tends to limit new orders for systems. This product strategy is necessary to balance both the workloads of the engineering units and the risks related to this type of contract. The most significant orders for the systems and components segment include the following:
- an 800MW combined-cycle plant for the Rizziconi plant in Reggio Calabria (Q1);
- a steam turbine for Belgian firm Electrabel to be installed at the existing Amercoeur plant in Belgium (Q3);
- a gas turbine assembly (model V64.3A plus) for the Indian firm G.E.A. for the combined-cycle plant in Valuthur, India (Q3);
- a gas turbine assembly (model V94.3A4) to Enel for the Algeciras plant in Spain (Q3);
- three model V94.2 gas turbines and related generators to the Korean firm Doosan Heavy Industries and Construction Co., Ltd, to increase

the size of the Barka plant in Oman (Q4);
- a steam turbine assembly for the conventional plant in Nueva Ventanas, Chile, for the Korean firm Posco Engineering & Construction (Q4);
- two gas turbine assemblies (model V94.2) for the Amman East plant in Jordan to the Korean firm Doosan Heavy Industries and Construction Co., Ltd (Q4).

For the services segment in 2006, Ansaldo Energia S.p.A. continued pursuing growth in new orders on both the domestic and international markets.
In terms of the product mix, important growth was posted both in long-term service agreements (LTSAs, which increased 13% over 2005) and in flow service agreements (spare parts, maintenance, revampings, repowerings, and upgrades), which increased 11% over the previous year.
In absolute terms, at 31 December 2006, the LTSAs totalled €mil. 274 and accounted for 62% of all new orders for the segment, while flow agreements came to €mil. 168 for 38% of all new orders. It should also be noted that Ansaldo Energia has increased its presence not only within its own installed base, but also in that of other OEMs.
The main orders for the service segment in 2006 included the following:
Long-term service agreements
- EGL Rizziconi Energia – 12-year GTF for the Rizziconi plant (2 V94.3A2 800MW combined-cycle gas turbines) – Q1;
- Centro Energia Ferrara – 9-year LTSA for a V64.3 gas turbine (Q1);
- Centro Energia Teverola – 9-year LTSA for a V64.3 gas turbine (Q1);
- Electrabel Rosen – 10-year LTSA for the Rosignano plant (2 V94.2 combined-cycle gas turbines) – Q4;

Flow agreements
- Enel – maintenance and strategic spare parts supply for V94.3A2/4 gas turbines installed in Italy and Spain (Escatron and Algeciras);
- Enel – repowering of two 320MW steam units in Fusina;
- Enel – provision of three bladed rotors for geothermal plants;
- Suez – provision of strategic spare parts for V94.2 gas turbines in Oman;
- Sonelgaz – provision of strategic spare parts for V94.3A1 gas turbines in Algeria;
- Centrica – general maintenance services and provision of spare parts for V94.2 gas turbines in Barry (UK);
- GPEC – general maintenance services and provision of spare parts for V94.2 gas turbines in Paguthan (India);
- Kapco – provision of strategic spare parts for V94.2 gas turbines in Pakistan;
- NASA – provision of strategic spare parts for steam generators in Argentina.

The new orders for the nuclear segment at 31 December 2006 reached €mil. 46, for an increase of roughly 5% over the figures for 2005 and may be broken down by geographic area with Italy accounting for 21% (3% for 2005) and the remaining 79% relating for foreign purchases essentially in eastern Europe.
In terms of the offering mix in the nuclear segment, growth in waste and decommissioning was particularly high (more than 100% higher than in 2005), partially offsetting the physiological decrease in engineering business in Cernavoda, Romania, with new orders from Nukem, Ignalina, Iberdrola, and Ispra related to waste treatment.
Services in the nuclear segment also posted an increase over the previous year, growing by more than 60% thanks to new orders for engineering services for the programme to extend the useful life of the Candu plant in Embalse (Argentina).

As a result of these new orders, the **order backlog** at 31 December 2006 totalled €mil. 2,468, for a 6% increase over 31 December 2005 (€mil. 2,329), thereby providing the Group coverage equal to 2 years of production.

Revenues came to €mil. 978 at 31 December 2006, an increase of 28% over the previous year (€mil. 764). Of this total, 74% related to work on systems and components, 21% came from service activities, and 5% from nuclear work processes.
Volumes as at 31 December 2006 were reached in line with the primary contract milestones and the profitability and cash-flow targets of the individual contracts.
Of particular importance was the Enipower contract for which the final Provisional Acceptance Certificate (PAC) was received for unit 3 of the Brindisi site, as well as the Final Acceptance Certificate (FAC) for units 1 and 2 of that site. Also in 2006, work continued on resolving the outstanding critical issues concerning a number of foreign contracts.

Production for the service segment, in terms of total number of actions performed, continued the upward trend with growth of 12% over the previous year. Making a particular contribution to this increase was the greater number of general actions on gas turbines (+34% over the previous year) due to the start of LTSAs. The revamping of the Torrevaldaliga steam turbines was completed, and a number of emergency interventions were carried out upon request of the customer.

Production for the nuclear segment in engineering activities included the continuation of the second unit at the Cernavoda plant and engineering activities for the *"Reattori Innovativi"* (innovative reactors) line.
Activities in the area of waste and decommissioning concerned the Phadec plant in Caorso for Sogin, the completion of inspections for the new storage tanks in Salluggia, and the completion of the Chernobyl contract.
In the area of nuclear services, work continued at the Superphenix plant in France, in addition to other activities in Chernobyl for the IAMS project.

EBIT at 31 December 2006 came to €mil. 63 for an increase of 60% over the same figure posted for 31 December 2005 (€mil. 39). This was made possible by the increase in volumes and the higher margins on certain contracts. This result can also be attributed to the ongoing improvements in efficiency and productivity.
ROS at 31 December 2006 came to 6.4% for an improvement of 1.3 percentage points over 2005.

The capital structure posted further significant improvements in **working capital**, which showed a negative value of €mil. 282 at 31 December 2006, compared with a negative €mil. 193 for the previous period. This was due essentially to the positive financial management of contracts thanks in part to the collection of advances on new orders (Rizziconi) and the maintenance of normal conditions in payments to suppliers. As a result, **net invested capital** improved to a negative value of €mil. 254 at 31 December 2006, compared with a negative €mil. 184 for 31 December 2005.

Research and Development costs came to €mil. 17 at 31 December 2006, increasing by more than 30% over the previous year (€mil. 13). This represents roughly 1.7% of revenues, as compared with 1.6% for 2005.
In 2006, following the achievement of full technological autonomy, a series of important projects were begun in the area of research and innovation. The leading results achieved include the following:
- for *gas turbines*, research programme were completed concerning low-emission (Low NOx) combustion systems, which are to be sold with the V64, V94.2, and V94.3A turbines beginning next year;
- for *steam turbines*, development activities made it possible to complete the prototype for the new extremely high temperature exhaust blades. The testing stages were also completed for the new *Ultrasupercritica* turbine (with a capacity of over 300MW). Finally, work began on the project to develop highly durable, highly reliable materials for steam turbines used in geothermal applications;
- for *generators*, the development cycle has been completed, and production has begun on the new air-cooled 350MW model for the new large-sized gas turbines. At the same time, the design phase has begun for the new 400MW model, which will also be air-cooled;
- for *services*, there was a sharp increase in the development of new products, particularly as concerns: the strengthening of remote diagnostics capacity to help with the management of LTSA scheduled maintenance; the development of special tools; and studies into upgrade packages to be mounted on machines and systems installed by Ansaldo Energia and other third parties.

At 31 December 2006, the number of **employees** stood at 2,856, compared with 2,529 at 31 December 2005. The increase of 327 employees is essentially due to the consolidation of the aforementioned companies within the Energy division (260 employees), as well as to normal hiring and turnover.

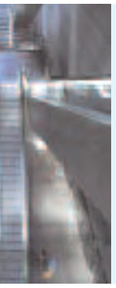
4. Performance by division

Transportation

Main data

€millions	31 December 2006	31 December 2005
New orders	2,127	1,615
Order backlog	4,703	3,956
Revenues	1,368	1,226
EBIT	15	(48)
R.O.S	1.1%	(3.9%)
Working Capital	61	235
Net invested capital	312	441
R.O.I (*)	4.8%	insig.
Research and Development	40	40
Employees (no.)	6,677	6,321

(*) Calculated on invested capital at period-end.
insig.: insignificant



HIGHLIGHTS

New orders: up 32% over 2005 with increases particularly in the Systems and Vehicles segments, which also recorded the contracts related to the driverless metros in Thessaloniki and Milan (Line 5) valuing €mil. 280 and €mil. 153, respectively.
Revenues: up €mil. 142 (+12%) due primarily to the increase in Signalling business and improvements in Vehicles over the particularly poor performance of 2005.
EBIT: up €mil. 63 over the previous year, which was severely impacted by the loss in the Vehicles segment. In 2006, this segment again posted a loss, but improved €mil. 51 over 2005. Performance in Signalling and Systems was positive, with EBIT increases of €mil. 10 and €mil. 3, respectively, over 2005.

The Transportation division includes the companies Ansaldo STS S.p.A. and its subsidiaries (Systems and Signalling) and AnsaldoBreda S.p.A. and its subsidiaries (Vehicles).

On 24 February 2006, Ansaldo STS acquired stakes in Ansaldo Trasporti Sistemi Ferroviari S.p.A. (Systems) and Ansaldo Signal N.V. (Signalling) from Finmeccanica S.p.A., while in April 2006 Finmeccanica S.p.A. completed a public tender for the sale of a 60% stake in Ansaldo STS. Since 29 March 2006, the company's shares have been traded on the STAR segment of the Italian Automated Stock Exchange.

Global demand for guided transport systems, both in urban/suburban and railway segments, confirms the sector's interesting growth prospects over the medium term. The factors driving demand include the need to relieve traffic congestion in large urban and metropolitan areas, the demand for reducing the environmental impact of transport systems, the need to replace a significant part of the aging fleet of vehicles, and the growing trend towards the outsourcing of management and maintenance services by the main operators.

The year 2006 was characterized by a slight recovery both in the demand for rolling stock – particularly regional trains, cargo locomotives, and urban vehicles – and in investments related to new high-speed lines and the modernization of national railway networks. The metro market remains strong, both for existing lines and for new projects. Demand for metro transit systems continues to be a driving force for the market.

Europe remains the leading market in terms of investment, particularly Italy, the UK, Spain, and France. In eastern Europe, Russia is also a dynamic force in the market.

The US market showed some signs of recovery in the urban and suburban segment, whereas Asia, and China and India in particular, driven by economic growth and urbanization, continue to post interesting rates of growth in demand and are destined to play an increasingly important role in the international marketplace.

In 2006, overall performance for the Transportation division was affected by critical issues in the Vehicles segment, which posted a loss at the EBIT level of €mil. 77, which is an improvement over the previous year, but which is still lagging behind the expected profitability gains as defined in the 2005 Development Plan. This was due primarily to the greater difficulties encountered in resolving the technical and implementation issues related to certain contracts. At the net profit level for 2006, AnsaldoBreda S.p.A. posted a loss of €mil. 168, as the company was affected both by the loss at the EBIT level and the recognition of finance costs (€mil. 114) for financing advances received from customers, which were not followed by deliveries made within the timeframes established by contract.

As a result, in December 2006, Finmeccanica performed a €mil. 270 capitalisation operation for AnsaldoBreda S.p.A. in return for this company's commitment to rectify the situation and to accelerate change along three lines of action:
- the implementation of a "crash programme" of short-term actions, with an emphasis on rapid implementation times;
- the definition and implementation of a more extensive "process programme" concerning operations, so as to have a more deeply structural impact on the main business processes (particularly on design, procurements, production, organization, and contract management);
- a review of the missions of the four production facilities in order to define solutions that would make it possible to transform them into centres of excellence in specific areas.

In 2006, the three business segments therefore showed the following performance:
- Signalling: positive trends with improvements both in financial standing and performance, especially thanks to the Italian subsidiary Ansaldo Segnalamento Ferroviario S.p.A.;
- Systems: strong commercial performance both in Italy and abroad, particularly in the area of driverless metro transit systems, and an increase in EBIT over 2005;
- Vehicles: as mentioned previously, financial performance continues to be characterised by operating losses, being affected by a worsening in estimates for certain contracts, which is primarily connected with the extra costs related to product fine-tuning.

New orders acquired in 2006 totalled €mil. 2,127, an increase of €mil. 512 over the previous year (€mil. 1,615), reflecting increased orders in Systems and Vehicles in particular. The key orders included the following:
- Signalling: orders placed by Rete Ferroviaria Italiana for the provision of ground systems relating to the 2c phase of the automated train control systems (SCMT, for *Sistemi di Controllo Marcia Treno*) framework agreement; the order by Trenitalia concerning the fourth contract for supplying SCMT devices for use on board trains; the orders related to the Ghaziabad-Kanpur line in India and for the Chicago subway line, all acquired in Q1; the order related to the high-speed Perpignan-Figueras line in Spain (Q2); the order placed by Trenitalia for the fifth contract for supplying SCMT on-board devices (Q3); contracts as part of the agreement signed with the Australian Rail Track Corporation (ARTC) in Q1, Q2 and Q3; and the high-speed Taegu–Pusan line in Korea (Q4);
- Systems: the extension of the operation and maintenance contract for the driverless metro transit system in Copenhagen (Q1); the orders related to the driverless metro transit systems in Thessaloniki and Milan (line 5) received in Q2; and the order for the Piscinola–Capodichino regional metro line in Campania (Q3);
- Vehicles: the Sirio trams for Kayseri in Turkey and the options for line 1 of the Milan metro (Q1); the contract for line 2 of the Milan metro and the orders related to the driverless metro transit systems in Thessaloniki and Milan (line 5) acquired in Q2; the contract for vehicle maintenance for the Madrid metro (Q3); and the contract for the provision of regional trains for Ferrovie Nord Milano (Q4).

At 31 December 2006, the **order backlog** for the division totalled €mil. 4,703, an increase of €mil. 747 over the same figure as at 31 December 2005 (€mil. 3,956).

Revenues at 31 December 2006 amounted to €mil. 1,368, an increase of €mil. 142 compared with 31 December 2005 (€mil. 1,226), which is attributable to Signalling and Vehicles. Among the noteworthy orders in the Transportation division were the following:
- Signalling: the high-speed train orders and automated train control systems (SCMT), both ground and on-board, for Italy; the second phase of the Channel Tunnel Rail Link; the project for the realisation of the Optimizing Traffic Planner (OTP) system and the next-generation computer-aided dispatch (CAD) system for Union Pacific Railroad; and the manufacture of components;
- Systems: the metro systems of Naples and Copenhagen; the Alifana regional line; and high-speed rail orders in Italy;
- Vehicles: trains for the Madrid metro; DMU trains for the Danish railways; high-volume passenger trains for Morocco; trams for the city of Los Angeles; high-speed trains for the Dutch and Belgian railways; trains for regional service for Ferrovie Nord Milano; E403 locomotives and ETR500 Politensione trains for Trenitalia; and service and revamping activities.

EBIT at 31 December 2006 came to €mil. 15, for an increase of €mil. 63 over the loss posted for 31 December 2005 (€mil. 48) due primarily to the reduction in the loss for the Vehicles segment and

the improvement in the Signalling segment. **ROS** for the sector improved as a result, reaching 1.1% as compared with the negative 3.9% recorded for the previous year.

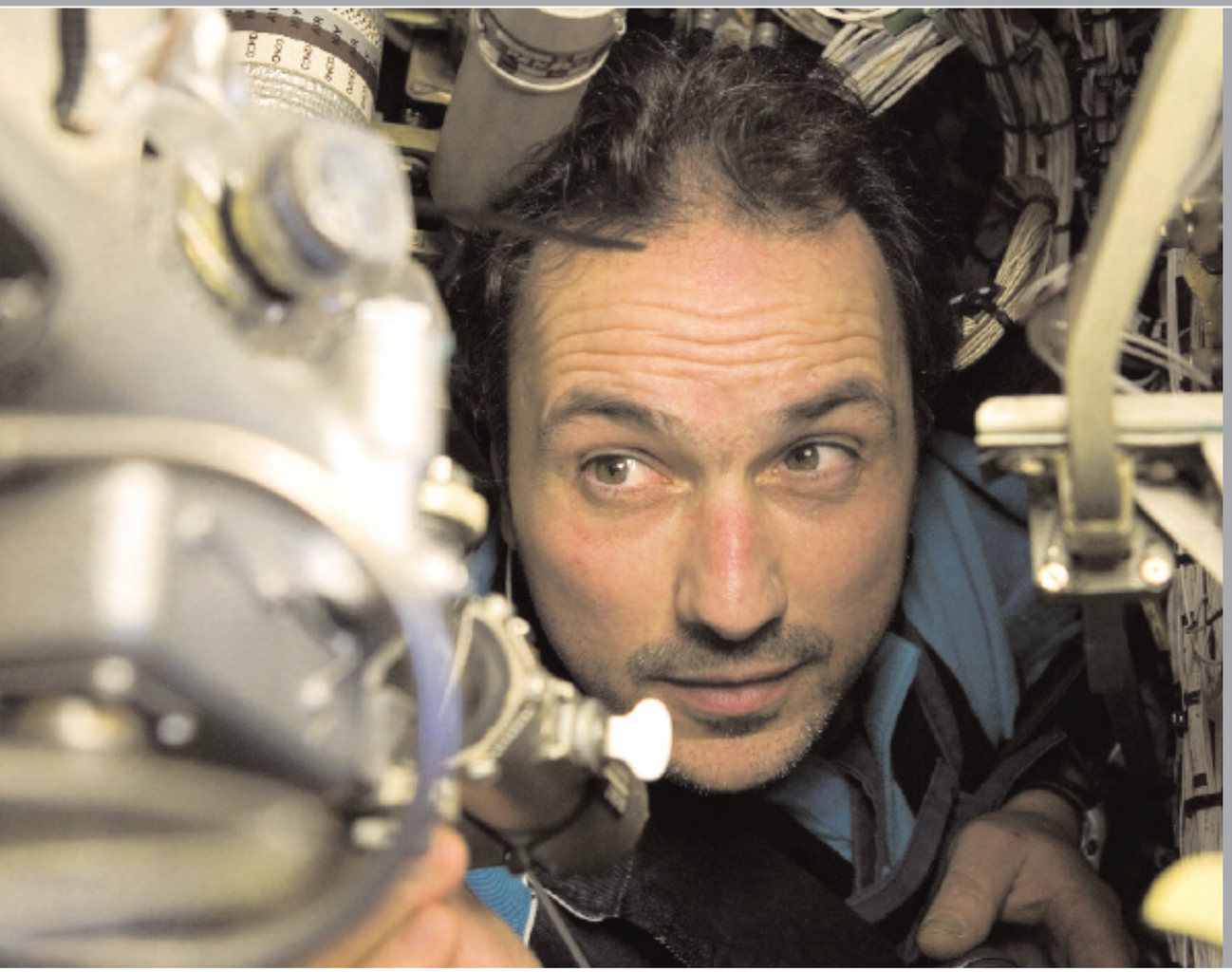
Working capital at 31 December 2006, in the amount of €mil. 61, marked a reduction of €mil. 174 compared with the total at 31 December 2005 (€mil. 235), with generalized improvements across all business segments.

Net invested capital at 31 December 2006 came to €mil. 312, down €mil. 129 from 31 December 2005 (€mil. 441), as the aforementioned reduction in working capital was attenuated primarily by an increase in equity investments in the Systems segment due to investments in the companies receiving the contracts related to the new Rome (line C) and Milan (line 5) metro lines.

Research and Development costs at 31 December 2006 totalled €mil. 40 and were in line with the figure posted for 31 December 2005 (€mil. 40). In particular, these activities concerned Signalling projects, aimed primarily at alignment with the new requirements emerging both in the railway segment (level 2 of the European Rail Traffic Management System, or ERTMS rbc) and the mass transit segment (Communications Based Train Control, or CBTC), as well as the development of certain on-board equipment (the next-generation cab).

The number of **employees** at 31 December 2006 stood at 6,677, representing an increase of 356 compared with 31 December 2005 (6,321 employees), principally due to hiring in the Signalling segment, particularly in Australia, India, and the US.

4. Performance by division



Other activities

Main data

€millions	31 December 2006	31 December 2005
New orders	99	465
Order backlog	346	487
Revenues	229	175
EBIT	(128)	(101)
ROS	insig.	insig.
Working Capital	135	(33)
Net invested capital	745	975
ROI (*)	insig.	insig.
Research and Development	-	-
Employees (no.)	811	940

(*) Calculated on invested capital at period-end.
insig.: insignificant

The division includes: the Elsacom N.V. group, which manages satellite telephony services; Finmeccanica Group Services S.p.A. (formerly Mecfin S.p.A.), a service management company for the Group; Ansaldo Fuel Cells S.p.A. for the production of energy using fuel cells; Finmeccanica Finance S.A. and Aeromeccanica S.A. (formerly Telespazio Luxembourg S.A.), responsible for providing financial support to the Group; and SO.GE.PA. - Società Generale di Partecipazioni S.p.A., responsible for centrally managing the pre-winding-up/winding-up and rationalisation processes of companies falling outside the business sectors through transfer/repositioning transactions.

The division also includes Fata S.p.A., for which the reorganisation process that began during the year can be considered definitively complete and which operates in the area of plants for processing aluminium and steel flat rolled products and engineering design in the power generation field for Engineering, Procurement and Construction (EPC) activities. It should also be noted that during the year this company acquired a contract for the provision of smelter to Bandar Abbas with a value of €mil. 315.

As of 2004, Bredamenarinibus S.p.A., which manufactures urban and intercity buses, was deconsolidated, with the recognition of the income and expense items under discontinued operations and of the assets and liabilities as held for sale. This company's operations are undergoing a process of reorganisation in order to make the business more attractive to potential buyers.

Effective 1 July 2006, the shareholdings ALS S.p.A. and Iritech S.p.A. were merged into SO.GE.PA. S.p.A.

This division's figures also include those of the corporate division of Finmeccanica S.p.A., which for some years has been undergoing an extensive transformation process, altering its focus from a financial company to that of an industrial company. This process, which is not yet complete, received a boost during the previous year with a commitment from management to press on with a series of actions concerning industrial, technological and commercial integration. The Group will then be able to benefit from an additional impetus in improving its own productivity through processes to increase efficiency and rationalisation.

In order to ensure that the financial objectives set by the Group would be met, the corporate division has conducted various initiatives, including the following:

- further strengthening of the mechanisms for the coordination of companies, including through development of specific Central Management structures, so that the individual parts could operate through a single policy, not just in financial terms, but particularly in industrial terms, involving the key processes of product engineering, technology and commercial strategy. This was within the framework of optimising the allocation of resources within the Group in order to maximise returns and avoiding overlapping, which restricts effectiveness and efficiency.
- the assignment of specific objectives to the companies: firstly, the constant growth of EBIT, thanks to increased volumes and significant efficiency-enhancement efforts, such as the optimisation of procurement, the rationalisation of production sites, as well as company restructuring leading to the containment/reduction of working capital and general and administrative costs and maximizing sales, with the consequent strengthening of production margins. The constant focus on trends in working capital in addition to the above will make it possible to generate the significant cash flows needed to finance the high level of investment in product development;
- review of processes from a Group perspective, in particular those that could have an effect on the optimisation of areas with possible synergies, such as information technology and real estate management;
- the issuance of specific directives aimed at the progressive alignment of cash flows with income and expenses. In that regard, it should be noted that, in 2006, the following new directives were issued: "Directive on the process for formulating and obtaining commercial offers", "Directive on risk management for orders", "Directive on the investment approval process of the Finmeccanica Group"; "Directive on the preparation and approval of the Product Business Plan"; and "Governance of information and communication technology processes in Finmeccanica Group companies";
- continued development of a process for the dissemination of a Group methodology for controlling and managing programmes, based on the integration of the international standards of life cycle management, phase review, project control, and risk management. The unification and implementation of control processes, scheduled to occur by the end of 2007, will reduce the level of risk, improve the quality of profitability and manage more efficiently reduction in inventories and increases in production efficiency;
- the implementation of managerial and administrative processes and the information systems necessary for the definitive assimilation of the new International Financial Reporting Standards (IFRSs) within the company, as well as the review of administrative flows, including from the perspective of simplification/integration with other company functions, and for providing greater support for industrial processes.

The efficiency of policy and coordination activities in the Corporate Affairs department was further strengthened in its goal of reaching these objectives over the medium term with a broad-based incentives policy, which involved top management and key resources from all companies within the Group. The correct application and monitoring of the promotion of these objectives will represent one of the principal aims in achieving the goals.

5. Reconciliation of net profit and shareholders' equity of the Group Parent with the consolidated figures at 31 December 2006

€millions	Shareholders' equity	of which: Net profit for the period
Group Parent shareholders' equity and net profit at 31 December 2006	**6,158**	**719**
Excess of shareholders' equities in the financial statements compared with the carrying amounts of the equity investments in consolidated companies	(1,821)	560
Consolidation adjustment for:		
- difference between purchase price and corresponding book equity	2,520	(11)
- elimination of intercompany profits	(1,741)	(45)
- deferred tax assets and liabilities	133	34
- dividends	-	(268)
- translation differences	35	-
- other adjustments	(8)	(1)
Group shareholders' equity and net profit at 31 December 2006	**5,276**	**988**
Minority interests	81	32
Total shareholders' equity and net profit at 31 December 2006	**5,357**	**1,020**

6. Finmeccanica: Research and Development

Following the major initiatives to expand and rationalise the Group that were completed last year (which primarily involved **AgustaWestland, Selex Sistemi Integrati, Selex Sensors & Airborne Systems Ltd** (**S&SA**), **Alcatel Alenia Space, Telespazio** and **Datamat**), in 2006 we increased the amount of attention devoted to organic growth, which also involved placing a greater focus on core research and development, accompanied by an effort to standardise and select activities in this area. One initiative in this direction was the process of recasting the strategies and activities of **Datamat** and its integration with **Elsag** in order to create a critical mass in Security, Logistics, Automation and IT services and Defence.

Aerospace, Defence and Security

In these areas, technological development requires sizeable investments, cutting-edge skills, and medium-to-long term time horizons.
The consolidated subdivision of R&D into the areas of **technological Research and Development** (a) and **Research and Development applied to products** (b) allows for proper planning of both risks and benefits and therefore the optimisation of the technological transfer, which enables Group products to achieve success on international markets.

a) Technological Research and Development

These are technological developments that are sometimes described as "basic", in that they are highly strategic and long-term, and that by nature require highly-qualified staff and specialised facilities.

Technological developments based on **highly-integrated components**, ranging from on-chip integration (MMIC - Monolithic Microwave Integrated Circuit) using cutting-edge materials such as gallium nitride, to multi-chip integration on organic and ceramic substrates (LTCC - Low Temperature Cofired Ceramic), to the new frontiers of electro-mechanical integration for electronics and sensors (MEMS - Micro Electro-Mechanical Systems) involve various Group companies (**Alcatel Alenia Space, Galileo Avionica, MBDA, Selex Communications, Selex S&AS Ltd** and **Selex Sistemi Integrati**). Their application and spread enable "quality" radio frequency processing components to be miniaturised, reducing costs and producing benefits for satellites, radars, missile systems and avionics systems, and in general any applications where a small footprint and minimal power absorption are key factors. Also in development are certain technologies known as MOVPE (*Metal Organic Vapor Phase Epitax*) in relation to the design and production of infra-red sensors in the next generation bi-dimensional arrays components for advanced thermal imaging cameras (**Selex S&AS**).

In addition, technologies of **new materials and structures** stimulate future developments and production capabilities, both with low infra-red and electromagnetic footprints and those with high resistance thanks to the use of composite materials and specific welding treatments (**AgustaWestland, Alenia Aeronautica, Alenia Aermacchi, Avio, Selex S&AS Ltd**, and **Oto Melara**). **MBDA** is currently conducting studies of high resistance nano-structured ceramics to create radomes operating in the millimetric band. The future development of innovative UAV/UCAV (Unmanned Air Vehicle and Unmanned Combat Air Vehicle), convertiplanes, radomes, rockets and passive protection structures lies with these technologies.
Highly advanced Research and Development activities in the field of nanotechnology also continued, especially regarding sensors for revealing chemical agents (**Selex Communications**), already in advanced stages of experimentation, as well as carbon nanotubes for the manufacture of nano-electronic devices such as nanovalves and nanotransistors (**Selex Sistemi Integrati**) and heat conducting materials for microelectronic packaging (**Alcatel Alenia Space** and **Selex Sistemi Integrati**).

b) Research and Development applied to products

All of our companies are heavily involved in maintaining, improving and streamlining their range of products to maintain and increase their competitiveness and customer satisfaction ratings thanks to technological research and development in the following areas:

- the **radar segment**, with modern electronic phased array scanning systems with integrated personal mobile radio module arrays for detection and aerial defence, including those used for air traffic control (**Selex Sistemi Integrati**). In this field, **Selex S&AS Ltd**, with its new Sea Spray radars entirely designed with solid state active modules, has posted a major commercial success, including in the US market, thanks to the advanced level of the system's technology. Placing these technologies on a common basis has paved the way for the development of a new radar denominated PICOSAR, which is specifically designed for surveillance with UAVs (Unmanned Air Vehicles) and a multiple-mode avionic radar called VIXEN-E with active electronic scanning that will form the future system for combat aircraft (**Selex S&AS**). Meanwhile, **Galileo Avionica** has begun making developments to revamp the exciter receiver processor which, using new digital technologies, will improve performance with regard to mechanical scanning radars (which have retained a level of market penetration) and to new electronic scanning radars. The development of the synthetic aperture radar (SAR) installed on the Cosmo-Skymed satellites (**Alcatel Alenia Space**) was also completed. With regard to the first system, the final installation on the new satellite platform was completed with launch scheduled for the first half of 2007. This system is enjoying a measure of success, with considerable expectations for national and European security;
- the **electronic warfare segment**, together with the 'sensitive' and extremely important associated technologies, has become part of the Group's assets, thanks again to **Selex S&AS Ltd.** With the DASS (Defensive Aids Sub-System) for electromagnetic defence against radars and missiles, the Group's product range of aerial platforms underwent significant expansion, allowing Finmeccanica to complete its integrated onboard defence and surveillance range for all air platforms. During the year, development began on the next generation of self-protection systems in the radar field called Radar Warning Receivers (RWR) based on advanced building blocks such as the broadband digital receiver (DRX) and the compact receiver module which contains a complete receiver in just one card;
- the **missiles segment**, with special reference to advanced seeker missiles, both infra-red (**Selex S&AS Ltd**) and radar and the active proximity fuses and related command and control systems (**MBDA**); preliminary and planning activities have begun on the project for new FREMM frigates for which surface-to-surface and surface-to-air systems must be installed on board (**MBDA**). Important developments are also taking place in the application of new digital receivers to improve existing seekers (Aster Meteor) and the use of passive phased array antennas for missile-based applications (**MBDA**);
- **electro-optics** for battlefield applications and for both land and sea integrated weaponry systems, and fixed-wing and rotary-wing aircraft applications (**Galileo Avionica, Selex Communications** and **Selex S&AS Ltd**). During the year, development began on a new generation of Direct Infrared Counter Measures (DIRCM) for active protection against shoulder-fired missiles for both military and civil aircraft (**Selex S&AS Ltd**) in cooperation with a well-known American company. **Selex S&SA Ltd** has also continued to develop active image observation systems based on burst illuminator laser (BIL) techniques, combining a laser source with a thermal imaging camera, allowing long-distance, high-resolution night time surveillance.
Development of an obstacle detection system is at an advanced stage. The system, called LOAM (*Laser Obstacle Avoidance*) is primarily for use in civilian helicopters. Based on laser/EO technologies, the system provides safety for the aircraft by detecting obstacles such as posts and high-voltage power lines which pose the greatest risk for low-flying aircraft (**Selex Communications**).
Development continues on the EO Hyperspectral system for space and avionics applications. Thanks to the analysis of the high-resolution image captured, this system, using hundreds of channels, will permit determination of even the type of material of which the object observed is made even from a distance (**Galileo Avionica**);
- naval, land, aeronautics and satellite **communications**, particularly secure tactical and strategic communications networks. Important projects are going ahead in the field of the architectures of future communication networks and services in a network-centric environment

and in the development of software radios, a vital aspect for the emerging, inexorable need for integrated global communications (**Selex Communications** and **Selex Service Management**). During the year, operational testing was successfully completed on the WiMax system in collaboration with the Ministry of Communications. The system has the potential to make a major contribution to mobile broadband communication for government agencies, such as the police, the Carabinieri, etc. (**Selex Communications, Selex Service Management**). Significant research has begun on full IP (Internet Protocol) convergence permitting the creation and dynamic, flexible management of networks in an open environment (**Selex Communications**).
During the year, development and testing was completed on new devices for the Sicral 1B military communications satellite system, adding sophisticated protection capabilities against intentional interference (nulling) and advanced digital techniques over communications channels to the product's existing operating features (**Alcatel Alenia Space**);

- the field of **orbital infrastructures** and useful loads (**Alcatel Alenia Space**), especially for scientific payloads, space robotics, satellite observation and navigation. In the planet exploration area, development has been completed on radio communication equipment for Ka-band telemetry and command systems for deep-space missions that will be used on the Bepi Colombo mission and X-band systems for use in the ESA LISA and GAIA scientific missions. In 2006, development also began in the area of automation and robotics, particularly in the field of vision and image processing for navigation and manipulation purposes, to be used for the Exomars and Eurobot exploration programmes. With regard to on-board technologies for satellite navigation payloads, during the year development and testing was completed on the device that generates the navigation signal for the Galileo Constellation;
- in the **orbital and space services management** sector, including the monitoring of sensitive areas (including security through the GMES programme) using differential radar interferometry and the innovative 3-D digitalisation based on space photography (**Telespazio**); important research began on navigation and infomobility which will generate significant returns in the areas of logistics and telecommunications (**Telespazio**);
- the area of highly complex, highly integrated land, naval and ATM (Air Traffic Management) **command and control systems** (C2-C4) with the design of a modern Flight Data Processor (**Selex Sistemi Integrati**), as well as highly specialised systems based on advanced processing and presentation devices (including platform control systems and advanced Flight Management/Control Systems for flight management) for application on fixed-wing and rotary-wing aircraft (**AgustaWestland**, **Alenia Aermacchi**, **Alenia Aeronautica** and **Galileo Avionica**).
Simulation is increasingly important in this area, especially for **Galileo Avionica**, which has begun designing a new generation of flight simulators, and for **Selex Sistemi Integrati** which is developing a modular simulator to be integrated with large systems.
In the second half of the year, in the naval sector, development began on a new Standard CMS (Combat Management System) system that will provide an effective modular solution for the advanced command and control systems market (**Selex Sistemi Integrati**);
- the field of **aeronautical platforms**, where **AgustaWestland** uses the latest technology and systems solutions to develop the BA609 in the helicopters division, the first convertiplane for civil use for which the initial pre-flight tests were completed at the end of the year; **Alenia Aermacchi**, with crucial developments regarding training aircraft, especially relating to the ultra-modern M346 trainer, which is successfully completing the final qualification stages; **Alenia Aeronautica**, with research on **aerostructures** that have successfully led to components of the new A380. Concurrently, development continues on some of the main components of Boeing's 787 aircraft. More specifically, we are building the central section of the fuselage, made entirely out of carbon fibre composite materials, with the prototype now in the final stages of production. A brand new plant has been built near Grottaglie to manufacture the components.
Work continued on the Sky-X (**Alenia Aeronautica**), an unmanned aircraft designed to demonstrate the feasibility of an advanced prototype with a mainly UCAV (Unmanned Combat Air Vehicle) role.
The development of the UAV Falco (**Galileo Avionica**) system for surveillance and tactical observation (500 kg class) entered the final stages (testing and fine-tuning). The Falco system was designed and built for "dual" purposes (both civil and military), including activities for territorial security, and is winning widespread acclaim thanks to its versatility and high useful load ratio;
- finally, in the **security** (or homeland security) area, which is becoming increasingly important, the Group has intensified efforts to provide tangible solutions in the short run.
A major R&D effort has gone into the **Zeus** project. The project is coordinated by **Selex Sistemi Integrati**, which has been given the mission of developing major systems for defence and homeland security applications. The Major Systems division of **Selex Sistemi Integrati**, which was recently formed to pursue business opportunities in integrated systems based on complex architectures and network-centric approaches, has undertaken a number of joint studies with all the other companies of the Group with a view to achieving the following objectives:
  - developing the operational specifications and functional architecture of a major integrated system and all of its components in order to translate them into competitive solutions that fully meet the needs of customers in the various applications requested by the market;
  - leveraging the know-how, technologies and products available within the Group so as to enable their effective integration within a major homeland security system.

In the area of protecting critical national infrastructures (CNI) related to the Transportation and Energy divisions (where there is an increasing need for infrastructure control and protection from the dangers posed by international terrorism, large-scale organised crime or severe natural disasters), **Ansaldo Energia**, **Ansaldo Sistemi Trasporti e Segnalamento**, **Elsag**, **Selex Communications** and **Selex Sistemi Integrati** are jointly involved in defining and formulating cross-technological solutions that can be implemented over the short term.
R&D activities related to the observation of human behaviour through the analysis of TV images and the monitoring of biometric sensor data (**Elsag**) is continuing and evolving, while investment is also continuing in data protection using traditional (**Selex Communications**) and quantum (**Elsag**) proprietary cryptography.
Targeted investments also continued in the advanced concept of network-centric operations used in the management of security operations with adaptation and integration between Crisis Management Rooms and secure communications components (**Elsag, Selex Communications, Selex Sistemi Integrati** and **Telespazio**).

Transportation and Energy

Group companies that operate in the civil sector also continue to carry out significant R&D activities, in addition to those described above, in collaboration with companies operating in the Defence and Security sectors.
Specifically, important activities are carried out in the following areas:

- **Energy**: with advanced processes to optimise the performance and maintenance of power plants. Innovative programmes on gas turbine and combustion system technologies are currently under way, focusing on low environmental impact, and the configuration of combined-cycle gas and steam plants (**Ansaldo Energia**). Progress continues to be made in the field of fuel cells which represent a better solution for eco-friendly transportation in the future (**Ansaldo Energia**).
An innovative high-output electric axial-flow engine is in an advanced stage of development. Participating in the project are **Ansaldo Energia**, which was responsible for its design through its **Ansaldo Ricerche** research centre, as well as other Group companies including **WASS**, **Oto Melara** and **Ansaldobreda**;
- **Transportation**: with developments in hybrid propulsion systems and components for handling, comfort and safety (including crash safety) in tracked transportation systems for city, suburban and rail vehicles (**Ansaldo Sistemi**

Trasporti e Segnalamento and **Ansaldobreda**). The main activities (**Ansaldo Sistemi Trasporti e Segnalamento**) focused on urban systems overall and on related railway signalling systems. The details of the projects are as follow:

- SIMMI for the improvement of the operational availability of railway instrastructures through a preventive diagnostic;
- SITI for infrastructure diagnostics and safety (with the TRAIN consortium);
- INTEGRAIL regarding a support decision system for railway operations.

The developments in the field of entirely automated subway systems (driverless) continued and confirmed their effectiveness, which led to the winning of major important national and foreign orders in 2006 (**Ansaldobreda** and **Ansaldo Sistemi Trasporti e Segnalamento**).
With regard to railway signalling, significant activities regard the development of components for high-speed railway line applications and high-density conventional lines through the radio block centre (RBC) and automated train control systems (SCMT) projects. The projects aim to improve the functional integrations of various related subsystems (**Ansaldo Sistemi Trasporti e Segnalamento**).
Ansaldobreda is developing an advanced high-speed new generation train with a European partner.

Group governance of Technologies and Products

The development of **Inter-company Technological Communities** (within the *MindSh@re*®[1] platform) is becoming a key resource and a breakthrough method to share and steer development, research and integration activities.
In 2006, seven communities had been started with activities involving over 600 researchers and technicians from among the company's top professionals:

- **Radar**: advanced radar system technologies;
- **CMM** (Capability Maturity Model): development and project management process;
- **Security**: R&D of technological systems and projects for **homeland security**;
- **Materials and Nanotechnology**: R&D on innovative materials and support nanotechnologies;
- **Design tools and methods**: analysis and rationalisation of design support methods and tools.
- **Simulation for Training**: simulation and training technologies and systems, including all the associated processes and the possible supply of advanced future turnkey systems.
- **Logistics**: technologies and systems for the management of logistics systems within the scope of providing integrated services.

Three major initiatives involving the communities of the *MindSh@re* project were launched during the year:

- **Corporate Projects** that are intended to foster collaboration between the various Finmeccanica companies and universities, research centres and end users in new technology and market segments. These projects, which are being coordinated directly by the Central Technical Department and are partially financed by the Group Parent, have achieved considerable success, thanks especially to the participation of many potential customers. The opportunity to collaborate on technology with Finmeccanica has given them a new insight into the Group and appreciation of its strengths in new and emerging sectors. During the year, 10 corporate projects were begun, involving the participation of 15 Group companies, of which 7 research centres and universities and 8 end users.
- Phase 2 of the ***MindSh@re***® project, which is evolving from "collaboration" on technologies to a greater focus on stimulating "innovation".
- The ***MindSh@re® event 2006*** organised in November at the CASD (Defense Studies Centre) by all the communities was a huge success, with over 600 internal and external experts and end users attending. In line with the goal of serving as the engine of an innovation culture, capable of valuing research and of representing the driving spirit of a collaboration network, the event offered 16 seminars, dedicated to the various technologies being developed by the Group, and a stand for each community to present the latest technological initiatives under development.

Finally, work on compiling the Group's integrated product catalogue was completed. With the use of a series of IT tools and the significant amount of information collected, this project gives access to extensive aggregated data both at the level of products on the basis of systems/platforms and commercial data by geographic area or individual company.

European programmes

The Group is also active in R&D activities at the European level (European Commission, EDA, NATO).
Finmeccanica's involvement in a range of ongoing programmes is continuing:

- **Sixth Framework Programme**. Development work is continuing on the LIMES project, led by **Telespazio**, which seeks to integrate satellite surveillance within the broad context of complementary solutions and systems, within the scope of the GMES programme.
- **Galileo Programme** for the new global positioning system, for which Finmeccanica was selected, with other European partners, to design and place in orbit the satellite constellation. During the year, the first of the "Giove A" pre-series satellites was launched (**Alcatel Alenia Space**).
- **Preparatory Action Programme** for European technological development in the Security field (**PASR**). Development of the two European projects awarded to Group companies continues: border protection (**Galileo Avionica** with the SOBCAH project) and rail transport security (**Ansaldo Sistemi Trasporti e Segnalamento** with the TRIPS project).
- **EDA** (**European Defence Agency**) with which relations were tightened, for the provision of new technological development in the areas of UAV and software radio.

Finmeccanica's strategy for the upcoming **Seventh Framework Programme** (2007-2013) has been consolidated, with broad initiatives on defining the programmes and on possible collaborative consortiums:

- Strong participation in **Collaborative Research** in the **aeronautical** area and the related **JTI** (Joint Technology Initiative called Clean Sky) which will have a total financing of over €mil. 2,000, proposing two technological platforms with development to be led by Finmeccanica: the Green Regional Aircraft (**Alenia Aeronautica**) and the Green Rotorcraft (**AugustaWestland** in a consortium with Eurocopter). **Avio** and **Galileo Avionica** are also involved.
- The **SESAR programme**, now that the pre-development phase has been completed, will be implemented within the Seventh Framework Programme with about €mil. 1,000 in financing from the Commission and Eurocontrol. This project will allow the development of the new European ATM system for an efficient air traffic control management system by 2020 and **Selex Sistemi Integrati** and **Alenia Aeronautica** (likely top-level leaders), **Galileo Avionica**, **Selex Communications** and **Telespazio** are actively involved. In 2006, the work programme broken down by main activities was prepared.
- The **Security programme**, which, with an investment of about €mil. 1,400, will permit the designing of homeland security products and systems. Thanks to its excellent positioning on PASR projects, in 2006, Finmeccanica began a number of technologically-based initiatives and international cooperation activities with the support of the ASD (Aeronautic, Space and Defence) association in Brussels. Ten top-tier Group companies will be directly involved in the programme.

Finally, in addition to our long-standing collaborative relationships with leading **Italian universities** (**Genoa, Naples, Parma, Pisa, Rome**, and **Turin**), cooperation with the **CRUI** (**Conference of Italian University Rectors**) has expanded with a number of important initiatives, such as the major joint workshop on nanotechnologies held in Turin with the participation of experts from Group companies and more than 40 academics from 30 Italian departments/universities. Exchange relationships with the most important **US universities** (**MIT–Cambridge, University of California at Berkeley, Carnegie-Mellon–Pennsylvania**) also continued.

7. Finmeccanica: Human Resources

Organisation

The intensive revision and adjustment of our Group's organisation, aimed at meeting the new challenges of our competitive environment,

[1] *MindSh@re*® is a registered trademark of Finmeccanica S.p.A.

continued in 2006: consolidation of international business forecasts; the integration of strategic assets; leveraging of international acquisitions and partnerships concluded in 2002-2005 in terms of greater productivity and synergies, cultural and industrial conversion of the Group based on the global player model.

The following section reviews some of the most significant organisational developments in this financial year.

In February, the organisational model for **Ansaldo STS** was finalised. Ansaldo STS is the Signalling and Railway system company floated at the end of March, which comprises the Group companies Ansaldo Signal and Ansaldo Trasporti Sistemi Ferroviari.

As regards the integration of **Elsag** and **Datamat**, after the top position of each company was given to the same top manager, at the start of 2007, the new unified organisational model of the two Group companies operating ICT and Security, within the Defence Electronics segment, was drawn up.

Ansaldobreda has also undergone a thorough restructuring aimed at implementing a new organisational approach and operational mechanisms: greater effectiveness in governance, guidance and control processes through the centralisation of certain skills and strategic activities; the harmonisation of company processes and methodologies; and efficiency drives in the production structure.

As part of the turnover in top management, the organisational structures of **Finmeccanica Group Services** (formerly Mecfin), the Group company responsible for shared services, and **Alenia Aeronavali** have been redefined. In addition, **Alenia Aermacchi** has had its business model revised in light of new challenges in its reference market, with a consequent reconfiguration of its organisational arrangements.

The organisational structure of **Selex Communications** has also been revamped to face the evolutionary dynamics of its reference market, in accordance with the ongoing change management process.

Therefore, during the summer the organigrams of **Selex Service Management** and **Seicos**, companies operating in the communications network and related added value services and applications sector for military and police forces, were formalised.

Ansaldo Energia, too, was involved in a significant organisational restructuring, consistent with and in furtherance of the new strategic policies and business development objectives, especially with regard to strengthening the service area (i.e. customer support and technological maintenance and upgrading of plants).

Additionally, the organisational structure of **BredaMenarinibus** has been redefined, making it more focused and simple than the previous structure.

During the final part of the year, in-depth study and preparation was undertaken to define new organisational structures for **Selex Sistemi Integrati, Elsag-Datamat** (as indicated above), **Telespazio, WASS** and **Ansaldobreda**, which were implemented in January and February of 2007.

The most significant organisational changes at the **Group Parent** in 2006 were, in brief:

- the restructuring of organisational units under the **Technical Department, Marketing and Commercial Affairs Department**, and **Legal and Corporate Affairs Department**;
- new responsibilities for the **Transportation Department**;
- the establishment of the **FNM Masters in International Business Engineering**, with the related Strategic Policy Committee, consisting of the top management of Finmeccanica and well-known experts in the academic world, to oversee all Masters-related activity (discussed in more depth further on).

With regard to initiatives designed to promote and boost the Group's corporate culture, March saw the creation of the **Group Targeted Projects Committee**. The latter supports top management in overseeing key programmes for business development and guarantees the uniform implementation of common Group methodologies and cross-cutting enabling systems.

Resource development and Compensation

On the issues of human resources strategic management and development, Finmeccanica further extended the infrastructure of its **Group Managerial System** by planning and developing an integrated system for **assessing management abilities** expressed in performance intended for all Group managers and executives. Through this system, called **GEAR** (Group Executives Advanced Review), the Group's portfolio of human resource development and management tools was completed, consistent with the most advanced international practices and with human resource activities and initiatives already begun by several Group companies.

All the planning activities tied to the development of GEAR were carried out by work groups in which representatives of the Human Resources Professional Family of the Group companies actively participated. This not only permitted us to leverage the Group's best internal practices, but to also practically experiment with a significant degree of sharing and integration, even at the international level, concerning the selection of the main project issues.

The planning of a Group management abilities assessment system involved the establishment of a distinctive Finmeccanica manager or executive profile through the complete reassessment of the abilities model in use since 2001 and which is currently the main conceptual reference for all the management development activities of the various companies.

The new MBO/GEAR 2007 project therefore envisages the inclusion of a specific management objective, accounting for 10% to 15% of the total MBO value, where the latter replaces the current objective assigned to members of the Professional Families, permitting the leader of a Professional Family to make a uniform, comparable merit assessment for all members of the same Family. The assessment will be performed by analysing a number of conduct indicators expressed in the context of annual performance and associated with each ability, using an entirely computerised system, which will regard the entire MBO project, and will permit significant optimisation compared with the current situation.

Between July and September one-to-one meetings were held with the companies within the context of the established **Management Review** process. These meetings play a fundamental role in analysing, sharing and verifying corporate policies to develop human resources. It is also the ideal forum for the periodic meetings of the Professional Families to plan, agree and implement Special Group Projects and inter-group human resources activities.

The 2006 format of the Management Review meetings was expanded and enriched specifically to gather information and discuss issues to support and facilitate **intragroup management mobility**. This implements the specific policy established and released in May to promote the development of Group managerial resources by introducing individualised development programmes.

With a view towards selective and differentiated promotion to permit the development and implementation of activities aimed at homogeneous target populations, special attention was focused on segmentation, based on the reference macro-profile, the critical segment of "Middle Managers in Development", divided into categories of Managerial, Scientists and Key Professionals Investments.

In 2006, with regard to initiatives to analyse and improve skills, the **Future Leaders' Review** was introduced. The Future Leaders' Review is an appraisal process targeted at a very select segment – identified within the context of the Management Review – of about 100 management employees of the Group companies who demonstrate high development potential and which will involve the integrated contribution of a leading international consulting firm and the Human Resources Department. This innovative action model allows us to effectively combine aspects of skill analysis and diagnosis and the planning and sharing of development and professional and managerial growth paths. Thus far, 60 interviews have been conducted. The aforementioned Management Review meetings also provided an opportunity for an initial restoration of the main facts that emerged from the individual interviews.

The remaining 40 interviews are scheduled for 2007.

The primary challenge in the area of **Compensation** continues to be the need to establish standard incentive policies and systems at the Group level that are consistent with company-level policies and are in line with the most recent trends and standard packages in the compensation market in order to attract and retain all the human resources and professional skills deemed critical by the Group.

In 2006, there was an increase in the number of participants in the **MBO System**, which currently includes about 90% of the Group's executives and managers and continues to represent an important component of the compensation package. In defining and assigning the MBOs, special attention was given to the need to ensure, consistent with the varying levels of responsibility and individual management tools, an optimal balance in the system of objectives, in order to preserve the tool's effectiveness in stimulating motivation while maintaining the focus on results and corporate performance.

With regard to **long-term incentive systems**, specifically the **Performance Share Plan 2005-2007**, the Share Grant plan approved by the Board of Directors of Finmeccanica S.p.A. on 29 September 2005, in 2006, upon verification of the performance objectives (for the company or the Group, as appropriate) the first instalment of Finmeccanica S.p.A shares were freely allocated and delivered up to a maximum of 25% of the total shares awarded under the Plan. It should be noted that Plan participants were identified based on the results of the Management Review process and include young management employees who, although they do not currently hold positions that have a high impact on corporate business, represent strategic Group assets based on their long-term development potential.

In 2006, the **2006-2008 cycle of a Cash Incentive Plan** targeted at the top management of Finmeccanica S.p.A. and of the main Group subsidiaries, based on the achievement of ambitious Group objectives. Under the traditional rolling-scheme approach, this Plan runs concurrently with the 2005-2007 cycle, with the goal of maintaining a high level of attention and motivation towards the joint achievement of results among the highest level of management.

The year 2006 saw the successful creation of the **CHANGE** (Challenge Hunters Aiming at New Generation Excellence) project, an innovative initiative to leverage the skills and develop our "**Rockets**". These are young people of excellence, identified by their companies, with international visibility who have clear growth potential in more complex roles.

This initiative, which has involved 81 young employees across Group companies in Italy and abroad, develops a highly original model of action learning. Participants analyse and create innovative proposals on strategic issues chosen by top management, working through a virtual network. Projects last around one month from introduction to completion and are held at one of the Group companies, depending on the issue being examined.

Finally, the year saw the upgrade of **Finmeccanica Group premises across the world**: at the end of 2006, the Group operated through **302 offices**, of which 152 in Italy and 150 around the world. These included 131 so-called "operational" sites (manufacturing plants and other sites used mainly for production), around 43% of the total. A census of Group sites is updated every six months, in concert with the human resources staff of the operating companies, and published on the Finmeccanica website.

Professional Families and Practice Communities

With regard to the **System of Professional Families**, the Group model for the integrated development of inter-group activities within homogeneous professional environments, 2006 saw activities continue on different fronts in a variety of ways. Specifically, on the occasion of the 23 June workshop, the ***Marketing and Sales*** Professional Family, comprising about 1,600 Group employees, began its activities.

With regard to the ***Legal and Corporate*** Professional Family, at the end of October during a continuing education seminar in which top-tier representatives of the academic and professional world, in addition to top Group management, participated, the 2007 programme of training activities for the Professional Family was decided.

Finally, with regard to the ***Procurement*** Professional Family, the Group is currently designing a **dedicated specialised skills model**, which could serve as a prototype to potentially be applied in the future (with the necessary adjustments) to other Professional Families.

As to the ***MindSh@re***® [1] **Project**, on 22 and 23 November, CASD (Defense Studies Centre) hosted *"MindSh@re® Event 2006"*, attended by hundreds of people. The event signalled the growth of the strategic initiative, aimed at leveraging the Group's technological knowledge and best practices, towards the **Open Innovation** paradigm, i.e. the "opening" of the Group's Technological Community network. The new model plans to increase the combination of internal contributions to innovation with suggestions and ideas from customers, institutions, universities and research centres. This step strengthens the potential of the *MindSh@re*® Project in terms of image and business.

The *MindSh@re*® project, launched in September 2003, is the main Innovation & Knowledge Management initiative of the Finmeccanica Group, a model/methodological approach for improving the skills and technological excellence of the Group through the introduction of Practice Communities. There are currently active communities in the following areas:

- **Radar;**
- **Homeland Protection** (Security);
- **Materials;**
- **SW & CMMI** (Capability Maturity Model Integrated);
- **Integrated Environment for Design & Development** (Methodologies and tools for designing and developing products) (IED)[2];
- **Simulation for Training** (simulation and training technologies);
- **Logistics & Services.**

Overall, *MindSh@re*® project activities involve **about 700 Group employees** at various levels of coordination and operations representing the main Group companies, international joint ventures and several research centres in which Finmeccanica participates.

In the seven active Communities *hundreds of different most valuable and experienced Group employees* are involved in activities that promote the generation and circulation of technological learning as well as the professional and personal enrichment of the participants thanks to an intense "in person" encounter or using tools and methods for long-distance sharing/cooperation made possible by technology. This is a great opportunity for professional growth, especially for young employees who will have the opportunity to work side-by-side with the Group's primary experts in various technological fields (so-called "Champions", i.e. senior employees who are custodians of the strategic know-how and leaders in their respective areas).

Among the primary objectives of this strategic Group project (with a registered trademark), are:

- the development of culture, processes and methodologies for strengthening the Group's technological innovative skills;
- the leveraging of the Group's strategic know-how and technological practices and excellent products and processes;
- the joint development of new business opportunities namely optimisation through sharing resources/assets available within the Group (skill centres, technological platforms, facilities, etc.);
- the coordination and rationalisation of the technological investments of the Group companies;
- the development and leveraging of personnel;
- the creation of panels of experts which shall ensure vision and the ability to analyse issues of strategic importance (high-level advising).

The project format envisages a **meta-organisational division**, to be adapted from time to time to the specific needs of the family of products/systems/services considered which includes a Technology Council (the Community's policy body that drives and controls activities) and the Community Focus Groups, which are

[1] MindSh@re® is a registered trademark of Finmeccanica S.p.A.

responsible for gaining a deeper understanding of and developing an issue or a defined area of activity correlated with specific objectives to be achieved. Each Focus Group is led by a Mentor, who is a key figure in *MindSh@re®* 's planning architecture designated by the Technology Council if necessary.

Training and Knowledge Management Systems

The **Training and Knowledge Management Plan** is designed to support the processes of change, growth and internationalisation of the Group and leveraging its human and intellectual capital, in a manner consistent with business needs in close collaboration with all the Group's companies. This systemic model, first introduced in 2004 and gradually consolidated, will be fully realised in 2007 through the implementation of all the initiatives developed in view of strong interaction and integration between the Group Parent and the Group companies.

The Education & Knowledge Management model envisages identifying the companies' requirements and integrating these with the priorities derived from the Group's objective (*value creation, internationalisation, integration, change management and innovation*), monitoring, and measuring the outcomes and the impact of actions implemented.

The System comprises three principal macro areas:

1. Corporate Culture and Knowledge Management;
2. the Group's Culture and Identity;
3. Change Awareness and Life-Long Learning.

1. Corporate Culture and Knowledge Management

To consolidate the Group's *Corporate Culture*, in 2006, the **Finmeccanica Economics Programme** was implemented to strengthen economic and financial management skills and to foster the application of tools to monitor and measure performance on the basis of a value creation approach. Since October, 11 sessions have been held, comprising 180 employees from various departments and levels of the approximately 750 total employees expected to take part from all the Group companies.
The approach for the Finmeccanica **Project Management** programme, which will begin in the first quarter of 2007, was also defined. The objective is to ensure the application of methodologies that support order management using the specific models and best practices of programme/project management and risk management.

During the year, the Training and Knowledge Management Systems Department, in concert with the Finmeccanica Group Service's ICT Department and Finmeccanica's Technical, Marketing and Commercial Affairs and Strategy Departments, began developing the **Group Knowledge Management System**. A pilot programme will be launched in 2007 to be subsequently rolled out to the various Group companies. The progressive activation of common tools to held capitalise and share knowledge among the Professional Families and Technology Communities to facilitate integration and innovation.

Within the **Intellectual Property Governance** programme, aimed at stimulating the protection and leveraging of the products and processes of the Group companies, in concert with the Technical Department, workshops and training was begun for positions that influence "patentability" and innovators/researchers. The aim is to develop awareness of the importance of protecting intellectual property. As from October, at total of 160 employees have been trained, with 750 employees to be involved overall.

In order to stimulate and leverage the skills, abilities and technologies of the various companies, Finmeccanica has, since 2004, sponsored the **Innovation Award**, an international award open to all employees who present innovative ideas and projects for corporate business areas.

The third annual edition of this award, run with the Technical Department, saw an ever-increasing number of participants with more than 4,000 persons involved worldwide and around 1,400 innovative projects received, of which many were patented with a positive effect on the business and the creation of value not just for the Group, but for all stakeholders. Out of the total number of projects presented over the past three years, the year 2006 accounted for nearly 50% with 25% of the year's entries submitted by employees at our international sites.

2. The Group's Culture and Identity

In order to meet the challenge posed by internationalisation, to highlight the distinctive cultural elements of each Group company and to make them strong points in the process of change, the Finmeccanica's Human Resources Department performed a **survey** of its employees under the **Business Culture project**. The survey involved all Group employees from around the world. An online questionnaire, offered in seven languages, was completed by 22,000 employees. The results reveal that employees have a strong professional motivation, that they love their work and recognise their contributions to achieving business objectives. The leadership provided by top management is strong and employees have faith in the Group's future, since they understand that the changes occurring will lead to new market opportunities, increased competitiveness and new professional development opportunities. There is dialogue, cooperation among colleagues, freedom of expression and a perception of job security.

The challenges for the future concern controlling change and leveraging the Group's intellectual and human assets at the international level in order to achieve integration based on the development of the specificity and construction of a distinctive shared, multicultural identity.
The results, already reported to all the organisational levels of the Group Parent and the Group companies, will allow us to identify, within the areas covered by the survey, the best practices to be shared at the Group level and the actions capable of providing a practical response in areas requiring improvement. These actions will be duly communicated, implemented and monitored throughout 2007.

To promote the thorough, optimised flow of information within the Group at the international level, the **Integrated Project on Internal Communication and Group Identity** has begun. It involves close integration on all planned initiatives between Human Resources, Training and Knowledge Management Systems, External Relations and Communication and Corporate Image. The project is aimed at developing integration and a sense of belonging to the Group, leveraging corporate best practices and creating synergies, through the gradual implementation within each company of Internal Communication initiatives and tools (Finmeccanica *Feelers*, Noticeboards and Portal Rooms), namely through the improvement of existing communication tools (*Infragroup Portal, Finmeccanica Magazine, Company House Organ*). An international network of company contact people (one for External Relations and another for Human Resources in each company – only the Italian part was involved for subsidiaries and associates – for a total of 50 contact people), who work in groups to develop specific initiatives, has also been created.

In May the new configurations of the **Finmeccanica website** (www.finmeccanica.it) and the **Group portal** (www.webportal.finmeccanica.it) were rolled out. The Training and Knowledge Management Systems Department was responsible for developing content for sections on human resources, highlighting ongoing initiatives to leverage human resources (Training and Development) at Group level, as well as intra-group projects for all employees (such as Job Posting, the Innovation Award, the Corporate Culture Project, and Finmeccanica Masters).

With regard to support initiatives for the **Professional Families**, a cycle of workshops was completed for the managers of the Procurement and ICT Professional Families from all Group companies (around 60 Italian and British employees were involved). There were also three HR professional workshops geared towards executives (20) and middle managers (47) from the HR Professional Family. Interactive study seminar cycles began on the "Tax Community" (around 60 people) and on the "Administration and Control Community" (around 90 people). Community functions were activated on the Intragroup Portal for these Professional Families.

A cross-functional group comprising the Marketing and Commercial Affairs Department, External Relations and Human Resources developed a project entitled **Show Management: Integrated Finmeccanica Model**. The aim is to define and implement a "Finmeccanica model" for integrated

management among companies and the Group Parent for Group **exhibition activities** and those who participate in them, like Stand Managers, Stand Manners and Hostesses. In June and July, training courses were held for 18 Stand Managers, 74 Stand Manners and 43 Hostesses (Italian and British), with the aim of developing an integrated, systematic vision of the Finmeccanica Group, a sense of belonging to the Group, and the skills necessary to perform their tasks efficiently.

3. Change Awareness and Life-Long Learning

Initiatives aimed specifically at corporate employees, particularly newly hired young people and high-potential young people and executives continued.

With regard to training for young people, the four-month long **FLIP** (Finmeccanica Learning Induction Programme) continued. FLIP is tailored for new graduates hired by the Group and is aimed at *sharing Finmeccanica distinctive values*. In the first six months of 2006, there were five editions of FLIP for a total of 117 participants. To date, the initiative, launched in 2005, has involved 275 new employees from 18 companies in 12 editions.

BEST, an online Masters in General Management for outstanding graduates at all Group companies with around 3 years' seniority which lasts 18 months, continued. Fourteen editions involving around 275 participants were completed. Launched in 2003, BEST has involved 388 young employees to date.

High-potential executives were the target of an in-house seminar, **From Technology to Values**, designed to develop a systematic view of the business with regard to macroeconomic and international strategic scenarios. There were three editions in 2006 (one Italian and two international) for a total of 57 participants. This was in addition to the 147 participants in the second half of 2004 and during 2005. There was a **follow-up** event in May for 128 executives (Italian and foreign) who had taken part in previous seminars. Entitled, "New Competitors and Business Areas", the event focused on the "India phenomenon" from a macro-economic and social, cultural standpoint. A specific Community was also set up on the Group Portal.

There was also an important initiative aimed at middle managers, who form a strategic organisational "hinge" during change. Funded by Fondimpresa, the training and skills development project, called **Innovate to Compete**, involved over 1,000 middle managers from all Group companies, joint ventures and Finmeccanica. The project entailed over 72,000 training hours to develop skills in *innovation management, change management and interfunctionality*. The project took place between January and May 2006, with the collaboration of 60 HR representatives from all participating companies. Project participants produced 208 improvement projects in Communication, Knowledge Management, Process Improvement and Human Resource Development.

Within the framework of the Group's initial Job Posting project, 13 professionals took part in **International Sales Manager** training, which was aimed at supporting the sharing and management of market principles and culture through knowledge of clients, the market and tools important to the Finmeccanica Group. The training course lasted three months and introduced participants to the complexity of the Group and brought them into contact with important market leaders and institutional representatives.

As regards training at the Group Parent, **legislative training/information** (which was extended to Finmeccanica S.p.A. employees in addition to those of Finmeccanica Group Services and SO.GE.PA.) continued with a number of targeted initiatives:

- training course for employees and managers who handle personal information, in compliance with Legislative Decree 196/03 and our corporate Security Policy Statement for a total of 280 persons involved;
- online training (accessible from the corporate intranet) on the "Compliance Model" adopted by Finmeccanica S.p.A. in accordance with Legislative Decree 231/01, for a total of 200 persons involved. The course was appropriately customised for all Group companies (AgustaWestland, Ansaldo STS, Ansaldo Energia, Selex Sistemi Integrati and Selex Communications have already signed up).

The **International Behaviour & Skills Programme** is an integrated model aimed at improving participants' knowledge of their foreign business language and presentation and negotiation skills in multicultural contexts. In 2006, the project involved 210 personnel from Finmeccanica S.p.A., Finmeccanica Group Services and SO.GE.PA. Project learning objectives were tied to participants' professional activities.

The programme used innovative, flexible teaching methodologies:

- **seminars for Functions/Professional Families** (e.g. legal English, financial English, etc.);
- **foreign-language workshops on specific themes** for those with advanced-level language knowledge (*Working in a Multicultural context, Presentation & Negotiation Skills, Customer Satisfaction, Time Management*);
- **blended courses** (classroom and online).

Industrial Relations and Social Affairs

Having completed negotiations of the two-year compensation part of the Metalworkers' National Collective Bargaining Agreement, in 2006 Finmeccanica focused its attention on the correct implementation of both the pay and, especially, the regulatory aspects of the Agreement within Group companies. In relation to this, the position supported by Finmeccanica within the delegation was fully adopted within the context of the renewal of the Agreement, especially with regard to the new Professional Apprenticeship contract.

In confirmation of the Group's position during the contract renewal process and in light of the new rules established by the Metalworkers' National Collective Bargaining Agreement, the new **Professional Apprenticeship contract** was developed in a Group project aimed at embracing and harnessing opportunities from the targeted use of this tool to bring new personnel into the world of work.

This initiative – innovative in Italy and developed with the contribution and support of **Federmeccanica** – led to the signing of a **Protocol of Understanding** with the **national trade unions** agreeing to the principles and criteria for implementing the new type of contract within the Group at a policy level, and to ensure its general effectiveness at the system level.

Following the national policy agreement, in 2006, a number of Group companies (for example, Alenia Aeronautica, AnsaldoBreda and AgustaWestland) drew up specific agreements with the trade unions to regulate the technical and applicative aspects of using apprentices. This led to the immediate hiring of young employees. Around 1,000 are expected to be hired at the Group level during 2006-2007. **It should be noted that in 2006 alone, more than 600 young employees were hired through this programme**.

In addition, Finmeccanica representatives involvement in **the Standing Groups for Trade Union Dialogue** has increased. Following renewal of the Metalworkers' National Collective Bargaining Agreement last January, the groups were formalised to promote shared management and efficiency in work relations as a fundamental condition for reviving the competitiveness of the productive system. The groups discussed in-depth issues related to competitiveness, productivity, working hours and the labour market, with a focus on reviewing contract regulations on part-time work.

Finmeccanica and the main Group companies' presence on the **Joint Technical Committees** has been confirmed. Specifically, the Committees discussed **revision of the job classification system** through the study and identification of an innovative model better tailored to the requirements of new situations and of the new organisational models characterising the Group. The results of these discussions will be important in view of the next four-year renewal of the National Collective Bargaining Agreement.

A **Large Company Working Group** was also set up this year with the participation of the heads of industrial relations at the Group's leading Italian companies, with the direct, constant involvement of Finmeccanica. The group will analyse the key issues affecting such companies. It seeks to address common problems on specific areas and current issues in order to preventively define, where possible, common, homogeneous positions, particularly with regard to institutional and trade-

union counterparts. Within the scope of this initiative, it should be noted that Finmeccanica organised an internal meeting with the General Secretariat of the CISL union attended by all the heads of the large company groups.

As to **corporate agreements**, activities continued on the **renewal of second-tier bargaining**, through the Group Parent's constant monitoring of the principal lines to follow concerning the regulatory and compensation demands supported by the unions as part of the negotiations. Finmeccanica confirmed its pivotal role in spurring innovation, while protecting the specific features of each different entity.
These processes led to the definition of additional agreements (**Ansaldobreda** and **Alenia Composite**), significant progress in other negotiations which should be completed soon (**Alenia Aeronautica**), as well as new further negotiations for the renewal of supplementary contracts at **AgustaWestland** and **Oto Melara**.

Definition of certain temporary agreements, as amnesties for past years, was also achieved.

These results were achieved by paying close attention to costs (always within the budget for subsequent years) and, especially, without any dispute with the unions (no strike and the broad consensus of the employees involved), thereby undoubtedly having a positive impact on the corporate atmosphere, union relations and the "external" perception of the Finmeccanica Group.

Finmeccanica also continued to provide support, at both institutional and union levels, to a number of companies involved in **integration/reorganisation/outsourcing**.
Specifically, a positive conclusion was reached in several disputes that were especially complex for political or union-relation reasons (such as, for example, the first Supplementary Agreement of Alenia Composite, the sales of Elsag STI and Elsag GEST, Telespazio's switch from the Telecommunications Workers' National Collective Bargaining Agreement to the Metalworkers' National Collective Bargaining Agreement), through a series of interventions designed to help individual companies manage the different processes involved, particularly with regard to possible employment and social impacts.

As in previous years, the Group continued to promote and implement a variety of contractual arrangements involving executives and middle managers. In particular, the Group fine-tuned certain rationalisation processes related to important incentives such as supplementary health insurance, insurance coverage and supplementary pension schemes. Work continued on promoting and implementing **social services** aimed at all Group employees, which focus on offering especially advantageous benefit packages, including with regard to financial and commercial matters.
The Group's increasingly well-established international presence has led to closer scrutiny of integration processes concerning employment-related organisational, regulatory and contractual matters. In particular, programmes were launched aimed at standardising current international pension schemes (especially in the UK) and a close look was taken at the processes of intra-Group mobility at the supra-national level. The Group also continued to implement **shared services** dedicated to providing support for human resources activities that benefit all companies, especially those in the United Kingdom, thereby allowing us to optimise performance, reduce operational costs and offer high-profile, standard services for all the businesses involved.

Finally, specific initiatives were undertaken at the Group level aimed at reorganising the management of legal disputes by identifying specific common tools as well as sharing the most significant problems for the Group companies.

Finmeccanica Masters in International Business Engineering

The Masters integrates and enriches the Group's Training and Knowledge Management System. It is designed to train young high-potential graduates from across the world, and prepare them to face complex, international organisational contexts in the following areas: Programme/Project Management, Sales & Marketing, Business Improvement, Business Development, Risk Management. The Masters programme entails around 1,600 study hours over eight months (including lab hours and soft skill training).

The study period will be followed by a four-month long internship at a Group company in Italy or abroad.

Finmeccanica and the Group companies will provide Masters students with a study grant that covers all enrolment and attendance fees, in addition to providing accommodation near the course premises (Via Piemonte, 60, Rome).

Learning is monitored continually throughout the course. Final course results depend on passing exams and defending a final project. Subsequently, Finmeccanica will offer students the opportunity to work at a Group company in complex, international, organisational contexts, on hi-tech projects and activities.

The Masters was submitted to the Finmeccanica Board of Directors, which approved the course at its meeting on 11 May 2006. Andrea Del Chicca has been entrusted with implementing the new initiative through Finmeccanica Human Resources. He will be supervised by a special ***Strategic Steering Committee***, chaired by P. F. Guarguaglini.

One of the strong points of the Masters is the organic involvement of Group managers, lecturers from prestigious partner universities (Scuola Superiorie S. Anna in Pisa; Cefriel – Politecnico di Milano; Columbia University in New York; and the ISUFI – Università di Lecce) and respected lecturers from leading international academic bodies.

The "pilot" edition was officially inaugurated on 15 November 2006. The International Business Engineer is an innovative professional figure, the result of interdisciplinary training (business and technology) that is highly employable by international hi-tech firms.

Talented graduates were selected from over 3,500 applications from around the world. Once they have completed the eight-month long course and have successfully passed their exams, they shall be sent to work for the Group.

The selection process resulted in 29 top-notch admittees, some of whom were already employee by Finmeccanica, with the technological, managerial and business skills necessary to operate in complex international environments.

The profound international transformation of the Group is witnessed, in this strategic initiative, by the participation of young people from 16 different countries, including the UK, the US, China, India, Mexico, Malaysia, Thailand and Poland.

The average age of the participants is 25 years, with a grade point average of 108/110.

The Masters offers students the opportunity to acquire knowledge and develop skills and attitudes aimed at strengthening a strong knowledge base concerning the business segments in which the Group operates, and learning about the business management tools and methods used by the Group.

During the first three months of the course, students attended more than 400 hours of lessons, harmonising their basic preparation in the initial crash course, completing the preparation and sitting three exams from the Program Management modules (Basic Financial Management, Advanced Metrics of Business Performance and The Network Process and Project Based Firm), offered in concert with Cefriel – Politecnico di Milano.

In January 2007, the students attended lessons and sat the exams for the Strategic Business Management and Topics in International Economics modules, developed in cooperation with Columbia University, and began the Technology Management module, in cooperation with Scuola Superiore S.Anna. Students also worked on the Laboratory module (divided into Business Process Engineering and Enabling Collaborative Community), offered in concert with Isufi – Università di Lecce, for which they took their first intermediate-level tests.

During the entire initial study phase, in addition to attending classes taught by lecturers from the partner universities, students were also to meet

with many top managers of the Group Parent and the Group companies, providing lecturing and interviewing opportunities that gave the Masters a pragmatic managerial approach centred around Finmeccanica's experiences.

In order to ensure the personal, and as well professional, development of the participants, students also attended several days of training in "soft skills" – that will continue throughout the course of the programme – aimed at improving interpersonal skills and organisational conduct. On these days, students were also given the opportunity to visit Telespazio's "Piero Fanti" Space Centre in Fucino, Abruzzo. This is the first of several visits to Group companies. Also in the vein of personal development, a Basic Italian course was offered, involving the active participation of foreign students to facilitate their insertion into the Group's cultural and relational system.

8. Finmeccanica: Security Policy Statement (SPS)

"Information provided pursuant to Legislative Decree No. 196 of 30 June 2003 (Protection of personal data)"

Pursuant to Section 26 of the Technical Regulations on minimum date security measures, which constitutes Annex B to Legislative Decree no. 196 of 30 June 2003 ("Personal Data Protection Code"), the Security Policy Statement on the handling of personal information was prepared by the deadline of 31 March 2006, updating the SPS drawn up in December 2005.

The Security Policy Statement contains the information referred to in Section 19 of the Technical Regulations and describes the security measures adopted by the Company with the aim of minimising the risk of even accidental destruction or loss of personal data, unauthorized access, unauthorized handling of information or use for any purpose other than that for which it was gathered.

The updating of the statement did not involve significant changes with respect to the previous update carried out in December 2005, for the following reasons:
(i) the Company's data protection strategy has not changed;
(ii) the short time that had passed since the previous update;
(iii) the absence of significant changes in the organisational structure of the Company.

Information security management system

Finmeccanica S.p.A. received certification of its Information Security Management System in accordance with Standard ISO/IEC 27001:2005[1] for the "Management and supply of corporate electronic mail service".
The certification project was carried out from September 2005 through May 2006 with the assistance of the ICT Mecfin Group and the participation of the corporate departments involved.
The validity of the certificate, issued by DNV (Det Norske Veritas), is conditional upon an annual inspection and a complete review of the system every three years.

9. Stock option and stock grant plans

On 23 May 2006, the Ordinary Shareholders' Meeting approved the renewal for a period of 18 months of the authorisation of the purchase of treasury stock, previously approved by the Meeting on 1 June 2005, to be used as part of a Stock Grant Incentive Plan for the 2005-2007 period for strategic employees and key employees of the Group, under which shares were granted without cost subject to verification of the attainment of objectives set out in the Rules of the Plan.

On 21 April 2005, the Board of Directors examined and approved the general outline of the Plan to be submitted to the Shareholders' Meeting.
The Plan provided for granting the participants the right to receive shares of the Company without cost subject to verification of the attainment of objectives set by the Remuneration Committee, which was given the task of managing the Plan based upon general criteria set by the Board of Directors.

The Shareholders' Meeting of 1 June 2005 had authorised, pursuant to Art. 2357 of the Italian Civil Code, the purchase in one or more instalments and for a period of 18 months from the date of resolution of a maximum of 7,500,000 (seven million five hundred thousand) ordinary shares (150,000,000 prior to the reverse split) of Finmeccanica - Società per azioni for a minimum price of €4.40 per ordinary share, equal to its par value (€0.22 prior to the reverse split), and for a maximum price of €20.00 (€1.00 prior to the grouping) to service the new 2005-2007 Incentive Plan.

At its 20 September 2005 meeting, the Remuneration Committee examined the matter and drafted a proposal for the creation of a 2005-2007 Stock Incentive Plan that envisages that the Board of Directors shall delegate the adoption of Implementing Regulations and the share allotment, based upon a proposal from top management, to the Remuneration Committee.

At its 29 September 2005 meeting, the Board of Directors adopted a resolution formally creating the 2005-2007 Stock Incentive Plan (called the Performance Share Plan), and instructed the Remuneration Committee to approve the Implementing Regulations.

The Remuneration Committee, at its 28 November 2005 meeting, approved the regulations for the 2005-2007 Performance Share Plan and the right to receive shares of the Company without cost for 574 beneficiaries, for a total of 5,611,531 shares, based upon the proposal set out by the Chairman and the Chief Executive Officer. Due to certain slight changes in the scope of the participants, the number of beneficiaries was reduced to 573 while, following certain adjustments to the individual grants, the total value of the rights granted fell to 5,577,961 shares. This update was approved by the Remuneration Committee in managing the Plan.

The number of shares granted is calculated (according to the usual market practices for such a transaction) on the basis of the individual beneficiary's annual gross remuneration (AGR), which depends upon both the position held in the company and on the assessment made during the annual Management Review. For this purpose, the unit value of the share is taken to be €15.03, which is the average price of the share from 1 January 2005 (the date on which the Plan came into effect) through 29 September 2005, the date on which the Board of Directors formally established the Plan.

Under the Plan, the granting of shares is conditional on achieving certain objectives set out in the Regulations. These objectives regard orders (while maintaining expected margins) for 40% of the shares and economic value added (EVA) for 60% of the shares. Shares would be granted as follows: 25% for achieving targets in each of 2005 and 2006 and 50% for 2007 targets. Under the Regulations, achievement of the latter could enable "recovery" of share rights that had not been allocated in previous years.

The Remuneration Committee provided that, following the conclusion of each accounting period (2005, 2006 and 2007) and the approval of the relative individual and consolidated financial statements by the Board of Directors of Finmeccanica S.p.A. – based upon the representations and the data provided by the Company's departments that are duly certified in accordance with Group Procedures – an assessment be made of the degree to which the assigned performance objectives have been reached and a calculation be made of the number of shares to be allocated to each person, and that notice of such be provided to the participants.

At its 11 May 2006 meeting, the Committee conducted a review to verify whether the performance targets had been achieved at the Group and company level on the basis of the draft consolidated and statutory financial statements for 2005, and calculated the number of shares to be granted to each of the beneficiaries for 2005. Upon completion of the review, the Committee approved the award of a total of 1,075,901 shares (equal to about 76% of the total attributable to 2005). The purchase of the shares to serve the Plan was completed on 2 June 2006.

At the same meeting, the Committee also authorized, following the placement of more than

[1] ISO 27001:2005 sets out the guidelines and related controls that companies must follow in implementing an ISMS (Information Security Management System), essentially to achieve the objective of protecting corporate information and data.

50% of Ansaldo STS on the stock market, the revocation of the share rights awarded to 41 beneficiaries for a total of 318,265 shares. As from 2006, these beneficiaries will participate in a long-term incentive plan established by Ansaldo STS after its listing. The Committee also approved the adjustment of the performance targets to match the new values in the business plans of the companies affected by changes in their scope of operations or other major discontinuities, and the consequent adjustment at the consolidated level.

On 28 August 2006, Finmeccanica S.p.A. sent written notice to each of the beneficiaries of the shares to be granted based upon the results achieved in 2005.

Based on the findings of the 2006 Management Review, on 17 October, the Chairman and Chief Executive Officer presented a proposal to the Remuneration Committee for the inclusion of 78 new managers as Plan participants, granting them to right to receive up to a total of 366,840 Finmeccanica S.p.A. shares at no cost. On 17 October 2006, the Remuneration Committee approved the proposal of the Chairman and Chief Executive Officer.

As a result of the all the changes to the scope of the participants and the granting of shares subject to the achievement of the 2005 performance objectives, the total amount of shares to be granted to the 604 Plan participants, should the 2006 and 2007 performance objectives be fully achieved, is 4,562,310.

On 1 December 2006, effective delivery was made of the shares awarded for 2005. Of the 1,075,901 total shares available, 642,115 shares were transferred into individual deposit securities indicated by the beneficiaries, while the remaining 433,786 shares were withheld to cover tax and social security obligations arising under the Plan.

Previously, on 16 May 2003, the Ordinary and Extraordinary Shareholders' Meeting resolved to approve a Long-Term Incentive Plan (Stock Option Plan) for the key resources of Finmeccanica S.p.A. and its subsidiaries, which provided for the granting of subscription and purchase options for ordinary shares of Finmeccanica - Società per azioni, subject to the attainment of specific objectives.

When the Plan was created, up to 7,500,000 (150,000,000 prior to the reverse split) shares were allocated that could be made available by issuing new shares and/or by purchasing treasury shares, leaving the Board of Directors with the power to choose one or the other instrument in light of how the stock is performing at the time the grant is made and on its performance outlook.

The options granted could be exercised through 31 December 2009, a period in line with the most common standard business practices.

There were 271 Plan beneficiaries including almost all the Group's executives or directors.

Each option granted the right to purchase/subscribe a Finmeccanica share at a price not less than the "normal value" to ensure that the Plan is tax efficient. That value was set at €14.00 (€0.70 prior to the reverse split).

The Plan, following the Shareholders' resolution, was established by the Board of Directors on 12 November 2003 and was entrusted to the management of the Remuneration Committee.

As contained in the Plan Regulations, the Remuneration Committee took steps to verify whether the performance objectives had been attained, based upon the draft individual and consolidated 2004 financial statements approved by the Board of Directors, and calculated the number of options effectively exercisable for each participant.

Upon completion of the verification process, it was discovered that the objectives had been reached, thus permitting the Group to release for the period 60% of the options originally granted, for a total of 3,993,175 (79,863,500 prior to the reverse split) exercisable options, at the fixed price of €14.00 each.

On 21 April 2005, the Board of Directors resolved a paid capital increase of a nominal maximum of €16,432,108.00 through the issuance of a maximum number of 3,734,570 shares (74,691,400 prior to the reverse split), to be offered for subscription at €14.00 (€0.70 prior to the reverse split) each (with allocation of the difference to the share premium reserve) to the executives of Finmeccanica - Società per azioni and its subsidiaries, as established by the Remuneration Committee on 4 April 2005.

For the remaining 258,605 options (5,172,100 prior to the reverse split) granted to persons not employed by the Company, the Shareholders' Meeting of 1 June 2005 had extended for a further 18 months the authorization to purchase/sell the corresponding number of treasury shares, taking into consideration that the Company already holds 193,500 such shares (3,870,000 prior to the reverse split). In order to ensure that the Incentive Plan was adequately serviced, the Company had purchased 65,105 (1,302,100 prior to the reverse split) shares of treasury stock.

Under the Plan, of the 3,993,175 options granted, 3,072,429 ordinary Finmeccanica shares have effectively been subscribed, with a resulting capital increase of €13,518,687.60, while 91,790 options to purchase treasury stock have been exercised.

10. Corporate governance

The corporate governance system of the Company and its compliance generally and as to specific methods of implementation with the model set forth in the Corporate Governance Code, are periodically explained by the Board of Directors in a specific report which is published on the occasion of the Shareholders' Meeting held to approve the financial statements.
This section briefly explains the main changes made in relation to the Company's corporate governance in 2006.

1. Board of Auditors - On 23 May 2006, the Shareholders' Meeting appointed the new Board of Auditors of the Company, whose term of office runs until the financial statements for 2008 are approved.

The new Board of Auditors is composed of the following members:
Auditors: Giorgio Cumin, Francesco Forchielli, Luigi Gaspari, Silvano Montaldo and Antonio Tamborrino.
Alternates: Maurizio Dattilo and Piero Santoni.
The Shareholders' Meeting also appointed Luigi Gaspari as Chairman of the Board of Auditors pursuant to the new paragraph 2-bis of the Uniform Financial Services Code (Legislative Decree 58/98), as well as Article 28.3 of the Company Bylaws, under which the Chairman of the Board of Auditors is appointed by the Shareholders' Meeting from among auditors elected by minority Shareholders.

2. New corporate governance code for listed companies – In March 2006, the new edition of the Corporate Governance Code for Listed Companies prepared by the Corporate Governance Committee (sponsored by Borsa Italiana) was published. In the new edition, the principles of good corporate governance were redrafted and updated in the light of developments in "best practice" policies, taking into account the changed national, EU and international legislative framework. The Code recommends that the new standards and related application criteria be implemented by the end of 2006.

Therefore, on 17 October 2006, the Board of Directors decided to adapt the Company's corporate governance model to comply with the recommendations contained in the new Corporate Governance Code, authorising the Chairman and Chief Executive Officer to prepare a proposal on adjustments to be made to the regulations, procedures, and standards of conduct, and corporate documents addressing the issue of corporate governance in general, in consultation with the Internal Auditing Committee and the Board of Auditors.
The proposal on adjustments to be made was approved by the Board of Directors on 14 December 2006. The Company's fundamental governance rules were collected in a single document, which fully incorporates previous "Operating procedures for the Board of Directors".

A detailed and exhaustive report on the Company's compliance with the new Code will be presented in

the Annual Report on corporate governance, published on the occasion of the next Shareholders' Meeting to approve the financial statements.

3. With regard to the modifications made to the organisational structure and regulatory changes under Legislative Decree 231/01, concerning privileged information and market manipulation, as well as a result of the introduction of Law 262/2005 concerning "Provisions for the protection of savings and the regulation of financial markets" as modified and supplemented, **Finmeccanica** is currently implementing its updated Compliance Programme pursuant to Legislative Decree 231/01. This process is expected to be completed during the first half of 2007 with Board approval of the new document which also reflects the instructions contained in the soon-to-be-published updated Confindustria guidelines.

Almost all of the Supervisory Bodies in the Group subsidiaries are multi-party in form following the process of shifting away from the initial single-party structure.

As to the general process of implementing the requirements of Legislative Decree 231/01 within the Group, it should be noted that the Compliance Programme and the consequent implementing actions were approved by the Boards of Directors of the subsidiaries. In addition, the Group is in the process of updating it to reflect changes in the law and the organisation of the Group companies which is expected to be implemented in 2007.

In addition, Finmeccanica, aiming to comply with the rules set out in **Law 262/2005** which introduces the figure of the "**Manager responsible for drafting accounting and corporate documents**", has begun a special project to update in accordance with the new regulation which the Group is seizing upon as a further opportunity to continually improve its corporate governance. The project, begun during the fourth quarter of 2006, aims to verify the compliance and the management methods of administrative accounting procedures for preparing consolidated and statutory financial statements.
The responsible Manager will be appointed, subject to the required opinion of the control body, based on the methods provided in the Bylaws which must be amended by 30 June.

11. Outlook

In 2006, the strategic repositioning of the Finmeccanica Group was reinforced through selective dimensional expansion, increased internationalisation and the achievement of strategic autonomy, thanks to which consistent growth in terms of volumes of revenues and profitability was possible.

This policy will be reinforced by new objectives that Finmeccanica has assigned specifically to each Group company and which will permit the Group to achieve and strengthen its technological and industrial leadership, essential for competing with increasing international competition.

The new objectives for the companies may result in increased profitability, reduced industrial costs and structure, contained working capital and self-financed investments in products.

These objectives may be achieved through appropriate actions applicable to different areas.

The integration of recently acquired businesses continues, aimed at promoting the achievement of expected profitability levels. For all business segments, detailed, specific efficiency programmes will continue, including through the review of current purchasing, manufacturing and logistics processes.

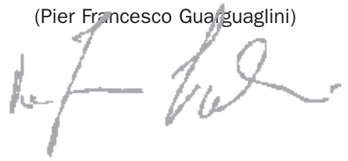
To reinforce the achievement of these objectives, the contribution of the Group's human resources involved will be vital, including through the development of a broad, flexible, incentive policy tied to the achievement of specific performance and financial objectives.

Before moving onto the growth forecasts for the Group, it is important to remember that the size of the orders backlog, defined based on its workability, is such as to guarantee 89% coverage of expected production for the next year.

Based on the foregoing, in 2007 we expect overall growth in Group revenues of between 5% and 10% with an increase in EBIT of between 8% and 14% over 2005.

We also expect Group Free Operating Cash Flow (FOCF) to remain substantially the same, given the significant investments in the development and sale of products, necessary to sustain Group growth, that will focus especially on Aeronautics, Helicopters and Defence Electronics.

For the Board of Directors
The Chairman and Chief Excecutive Officer
(Pier Francesco Guarguaglini)



Accounting statements and notes to the consolidated report at 31 December 2006

12. Income statement

€millions	Notes	For the twelve months ended 31 December 2006	2005
Revenue	32	11,179	10,101
Revenue from related parties	31	1,293	851
Changes in inventories of work in progress, semi-finished and finished goods		(24)	517
Other operating revenue	33	487	488
Other operating revenue from related parties	31	7	5
Costs for goods	34	(4,788)	(4,133)
Costs for services	34	(3,543)	(3,177)
Costs (net of recoveries) from related parties	31	(118)	(51)
Personnel costs	35	(3,391)	(3,042)
Depreciation, amortisation and impairment	36	(505)	(365)
Other operating costs	33	(433)	(514)
(-) Capitalisation of internal construction costs	37	714	55
		878	735
Financial income	38	1,191	432
Financial income from related parties	31	3	3
Financial expense	38	(779)	(546)
Financial expense from related parties	31	(16)	(13)
Effect of accounting for equity investments with equity method	39	(5)	(25)
Profit before taxes and the effect of discontinued operations		**1,272**	**586**
Income taxes	40	(243)	(200)
(Loss) Profit associated with discontinued operations	41	(9)	10
Net profit		**1,020**	**396**
. Group		988	373
. Minority interests		32	23
Earnings per share	42		
Basic		2.333	0.883
Diluted		2.323	0.877
Earnings per share net of discontinued operations	42		
Basic		2.353	0.861
Diluted		2.344	0.854

13. Balance sheet

€millions	Notes	31 December 2006	31 December 2005
Non-current assets			
Intangible assets	8	5,317	3,596
Property, plant and equipment	9	2,660	2,506
Investment properties	10	2	2
Equity investments	11	140	138
Financial assets at fair value	13	857	906
Non-current receivables from related parties	14	16	12
Receivables	15	426	110
Deferred tax assets	39	470	397
Other assets	15	9	4
		9,897	**7,671**
Current assets			
Inventories	16	3,095	5,511
Contract work in progress	17	2,823	2,538
Receivables from related parties	14	438	378
Trade receivables	18	3,479	3,284
Financial assets at fair value	19	21	20
Tax receivables	20	469	364
Financial receivables	18	452	442
Other assets	21	594	488
Cash and cash equivalents	22	2,003	1,061
		13,374	**14,086**
Non-current assets held for sale	**41**	**110**	**120**
Total assets		**23,381**	**21,877**
Shareholders' equity			
Share capital	23	1,858	1,858
Other reserves	23	3,418	2,586
Group shareholders' equity		**5,276**	**4,444**
Shareholders' equity of minority interests	**23**	**81**	**154**
Total shareholders' equity		**5,357**	**4,598**
Non-current liabilities			
Borrowings	24	1,979	1,975
Severance pay and other employee liabilities	26	1,238	1,114
Provisions for risks and charges	25	365	423
Deferred tax assets	40	340	101
Other liabilities	27	1,332	380
		5,254	**3,993**
Current liabilities			
Advances from customers	17	5,529	4,389
Trade payables to related parties	14	594	440
Trade payables	28	3,486	3,371
Borrowings	24	881	294
Tax payables	20	322	268
Provisions for risks and charges	25	571	523
Other liabilities	27	1,304	3,909
		12,687	**13,194**
Liabilities directly correlated with assets held for sale	**41**	**83**	**92**
Total liabilities		**18,024**	**17,279**
Total liabilities and shareholders' equity		**23,381**	**21,877**

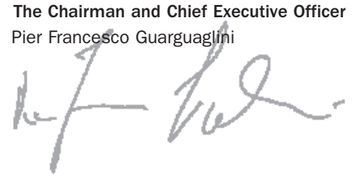
14. Cash flow statement

€millions	Notes	For the twelve months ended 31 December 2006	2005
Cash flow from operating activities			
Gross cash flow from operating activities	*43*	1,565	1,413
Changes in working capital	*43*	347	204
Changes in other operating assets and liabilities	*43*	(222)	(376)
Financial charges paid		(160)	(101)
Income taxes paid		(212)	(185)
Cash flow used for operating activities		**1,318**	**955**
Cash flow from investing activities			
Acquisitions of companies, net of cash acquired	*11*	(181)	(769)
Investments in property, plant and equipment and intangible assets		(873)	(436)
Disposals of property, plant and equipment and intangible assets		94	51
IPO Ansaldo STS	*5*	458	-
Avio transaction	*5*	303	-
Other investing activities		(63)	(51)
Cash flow generated from (used in) investing activities		**(262)**	**(1,205)**
Cash flow from financing activities			
Issues of debenture loans	*24*	-	494
Repayments of debenture loans	*24*	-	(927)
Net change in other financial payables		102	(207)
Dividends paid to shareholders of the Group Parent	*23*	(211)	(110)
Dividends paid to minority shareholders	*23*	(3)	(1)
Cash flow used for financing activities		**(112)**	**(751)**
Net increase (decrease) in cash and cash equivalents		944	(1,001)
Translation differences		(2)	7
Cash and cash equivalents at 1 January		1,061	2,055
Cash and cash equivalents at 31 December 2006	*22*	**2,003**	**1,061**

15. Statement of changes in shareholders' equity

€millions	Share capital	Retained earnings and consolidation reserve	Other reserves	Group shareholders' equity	Minority interests	Total shareholders' equity
Shareholders' equity at 31 December 2004	**1,856**	**1,798**	**(27)**	**3,627**	**22**	**3,649**
Adoption of IAS 32: treasury shares	(1)			(1)		(1)
Adoption of IAS 32 and IAS 39: other effects		109	418	527		527
Adoption of IFRS 2		(5)	5	-		-
	(1)	**104**	**423**	**526**	**-**	**526**
Change in the fair value of assets available for sale and transfers to the income statement			46	46		46
Change in the fair value of cash-flow hedge instruments and transfers to the income statement			(56)	(56)		(56)
Repurchase of treasury shares (net)	(1)			(1)		(1)
Allocations for stock grant plans			13	13		13
Translation differences			13	13	(1)	12
Dividends		(110)		(110)	(1)	(111)
Share capital increase for exercise of stock options	4	9	(1)	12	1	13
Change in the scope of the consolidation area and other minor changes		(1)	2	1	110	111
Net profit at 31 December 2005		373		373	23	396
Shareholders' equity at 31 December 2005	**1,858**	**2,173**	**413**	**4,444**	**154**	**4,598**
Change in the fair value of assets available for sale and transfers to the income statement			(66)	(66)		(66)
Change in the fair value of cash flow hedge instruments and transfers to the income statement			102	102		102
Repurchase of treasury shares (net)	(8)	(4)	(13)	(25)		(25)
Allocations for stock grant plans			18	18	(1)	17
Modification of accounting treatment of UK employee pension plans		(53)		(53)		(53)
Translation differences			33	33	(4)	29
Dividends		(211)		(211)	(3)	(214)
Share capital increase for exercise of stock options	8	19	(2)	25	4	29
Change in the scope of the consolidation area and other minor changes		16		16	(101)	(85)
Revaluation reserve		5		5		5
Net profit at 31 December 2006		988		988	32	1,020
Shareholders' equity at 31 December 2006	**1,858**	**2,933**	**485**	**5,276**	**81**	**5,357**
Note	*23*	*23*	*23*	*23*	*23*	

FOR THE BOARD OF DIRECTORS
The Chairman and Chief Executive Officer
Pier Francesco Guarguaglini



16. Notes to the consolidated financial statements at 31 December 2006

I. General information

The Finmeccanica Group is a major Italian high-technology organisation. Finmeccanica S.p.A. (the Group Parent), the holding company responsible for guiding and controlling industrial and strategic operations, coordinates its operating subsidiaries (the Finmeccanica Group or, simply, the Group), which are especially concentrated in the fields of Aeronautics, Helicopters, Space, Defence, Energy and Transportation.

Finmeccanica is a company limited by shares based in Rome (Italy), at Piazza Monte Grappa, 4, and is listed on the Milan stock market (S&P/MIB).

II. Basis of preparation and accounting standards used

In application of EC Regulation 1606/2002 of 19 July 2002, the consolidated financial statements of the Finmeccanica Group at 31 December 2006 were prepared in accordance with the international accounting standards (IFRSs) endorsed by the European Commission, supplemented by the relevant interpretations (Standing Interpretations Committee - SIC and International Financial Reporting Interpretations Committee - IFRIC) issued by the International Accounting Standard Board (IASB). The 2006 consolidated financial statements were prepared in accordance with international accounting standards (IAS/IFRS) issued by the International Accounting Standard Board (IASB), as endorsed at the date of presentation of these financial statements. Specifically, the standards used are those that have been endorsed by the European Union and which are contained in the following EU regulations: nos. 1725/2003, 707/2004, 2236/2004, 2237/2004, 2238/2004, 2086/2004, 211/2005, 1751/2005, 1864/2005, 1910/2005, 2106/2005, 108/2006, 708/2006 and 1329/2006.
The entire legislative framework was implemented by CONSOB which, by resolution 14990 of 14 April 2005, required that companies whose shares are admitted to trading in an EU-regulated market prepare their consolidated financial statements in accordance with IFRSs (instead of the individual local GAAPs) from the financial year beginning 1 January 2005.

In accordance with Legislative Decree 38 of 28 February 2005, the Group Parent Finmeccanica S.p.A. adopted IFRS as from 1 January 2006.

In certain respects, at the date of the preparation of these notes, the official bodies had not yet completed their adaptation and interpretations. As a result, there may be further modifications or amendments to these standards and interpretations that could require or permit the Finmeccanica Group to modify the accounting, measurement and classification standards adopted in preparing these consolidated financial statements.

The general principle used in preparing these consolidated financial statements is the cost method, except for the recognition of derivative instruments and some financial assets, which must or – to the extent of financial assets – can be recognised at fair value under IAS 39.

Among the options permitted by IAS 1, the Group has chosen to present its balance sheet by separating current and non-current items and its income statement by the nature of the items. Instead, the cash flow statement was prepared using the indirect method.

All figures are shown in millions of euros unless otherwise indicated.

Preparation of the consolidated financial statements required management to make certain estimates. The main areas affected by estimates or assumptions of particular importance or that have significant effects on the balances shown are described in Note 4.
The financial statements, prepared in accordance with IFRS, have been subject to a review by PricewaterhouseCoopers S.p.A.

III. Accounting standards adopted

III.1 Standards and consolidation area

The consolidated financial statements for the year ended 31 December 2006 include the statements of the companies/entities included in the scope of consolidation ('consolidated entities'), which have been prepared in accordance with the IFRSs adopted by Finmeccanica Group. Below is a list of the consolidated entities and the respective shares held either directly or indirectly by the Group.

List of companies consolidated on a line-by-line basis

Company Name	Registered Office	% owned by the Group		% contribution to the Group
		Directly	Indirectly	
ADVANCED TECHNOLOGIES S.R.L.	Pianezza (Turin)		100	100
AGUSTA AEROSPACE CORP. USA	Wilmington, Delaware (USA)		100	100
AGUSTA AEROSPACE SERVICES A.A.S. S.A.	Grace Hollogne (Belgium)		98	98
AGUSTA HOLDING BV	Amsterdam (the Netherlands)		100	100
AGUSTA SPA	Cascina Costa (Varese)		100	100
AGUSTA US INC.	Wilmington, Delaware (USA)		100	100
AGUSTAWESTLAND BELL LLC	Wilmington, Delaware (USA)		51	51
AGUSTAWESTLAND DO BRASIL LTDA	Sao Paulo (Brazil)		100	100
AGUSTAWESTLAND INTERNATIONAL LTD	Farnborough (UK)		100	100
AGUSTAWESTLAND HOLDINGS LTD	Yeovil Somerset (UK)		100	100
AGUSTAWESTLAND INC.	Wilmington, Delaware (USA)		100	100
AGUSTAWESTLAND NORTH AMERICA INC.	Wilmington, Delaware (USA)		100	100
AGUSTAWESTLAND N.V.	Amsterdam (the Netherlands)	100		100
AGUSTAWESTLAND PROPERTIES LTD	Yeovil Somerset (UK)		100	100
ALENIA AERMACCHI S.P.A.	Venegono Superiore (Varese)		99.998	99.998
ALENIA AERONAUTICA S.P.A.	Pomigliano (Naples)	100		100
ALENIA AERONAVALI S.P.A.	Tessera (Venice)		100	100
ALENIA COMPOSITE S.P.A.	Grottaglie (Taranto)		97	97
ALENIA NORTH AMERICA INC.	New Castle, Delaware (USA)		88.409	88.409
ALENIA S.I.A. S.P.A.	Turin		100	100
AMTEC S.P.A.	Piancastagnaio (Siena)		100	100
ANSALDO ENERGIA S.P.A.	Genoa	100		100
ANSALDO FUEL CELLS S.P.A.	Genoa		78.43	78.43
ANSALDO INDUSTRIA S.P.A. (IN LIQ.)	Genoa		100	100
ANSALDO NUCLEARE S.P.A.	Genoa		100	100
ANSALDO RICERCHE S.P.A.	Genoa		100	100
ANSALDO SEGNALAM. FERROVIARIO S.P.A.	Tito (Potenza)		100	100
ANSALDO SIGNAL ESPANA S.A.	Madrid (Spain)		100	40
ANSALDO SIGNAL FINLAND O.Y.	Helsingfors (Finland)		100	40
ANSALDO SIGNAL N.V.	Amsterdam (the Netherlands)		100	40
ANSALDO SIGNAL SWEDEN AB	Spanga (Sweden)		100	40
ANSALDO SIGNAL UK LTD	London (UK)		100	40
ANSALDO SIGNAL IRELAND LTD	Tralee (Ireland)		100	40
ANSALDO STS S.P.A.	Genoa	40		40
ANSALDO TRASPORTI - SIST. FERROV. S.P.A.	Naples		100	40
ANSALDOBREDA INC.	New York (USA)		100	100
ANSALDOBREDA S.P.A.	Naples	100		100
ASIA POWER PROJECTS PRIVATE LTD	Bangalore (India)		100	100
AUTOMATISMES CONTROLES ET ETUDES ELECTRONIQUES ACELEC S.A.	Les Ulis (France)		99.999	39.9996
BEIJING CS SIGNAL CONTR. SYST. CO. LTD	Beijing (China)		80	32
BREDAMENARINIBUS S.P.A.	Bologna	100		100
CSEE TRANSPORT HONG KONG LTD	Hong Kong (China)		100	40
CSEE TRANSPORT S.A.	Les Ulis (France)		99.999	40
CONSULTANCY AND PROJECTS GROUP S.R.L. (IN LIQ.)	Rome		100	96.923
DATAMAT SOLUZIONI PER LE IMPRESE S.R.L. (IN LIQ.)	Rome		100	96.923
DATAMAT S.P.A.	Rome	92.809	4.2445(*)	96.923
DATAMAT (SUISSE) S.A. (IN LIQ.)	Lugano (Switzerland)		100	96.923
DATASPAZIO-TELESPAZIO e DATAMAT PER L'INGEGNERIA DEI SISTEMI S.P.A.	Rome		100	82.261

List of companies consolidated on a line-by-line basis *(cont'd)*

Company Name	Registered Office	% owned by the Group		% contribution to the Group
		Directly	Indirectly	
DAVIES INDUSTRIAL COMMUNICATIONS LTD	Coventry (UK)		100	100
ELECTRON ITALIA S.R.L.	Rome		80	80
ELSACOM N.V.	Amsterdam (the Netherlands)	64.6	35.4	100
ELSACOM S.P.A.	Rome		100	100
ELSAG S.P.A.	Genoa	100		100
ELSAG BANKLAB S.P.A.	Genoa		100	100
ELSAG DOMINO S.P.A.	Genoa		100	100
ENERGY SERVICE GROUP LTD	Wurenlingen (Switzerland)		100	100
E-SECURITY S.R.L.	Montesilvano (Pescara)		80	80
FATA AUTOMATION S.P.A. (IN LIQ.)	Pianezza (Turin)		100	100
FATA DTS S.P.A.	Pianezza (Turin)		100	100
FATA ENGINEERING S.P.A.	Pianezza (Turin)		100	100
FATA GROUP S.P.A. (IN LIQ.)	Pianezza (Turin)		100	100
FATA HANDLING S.P.A. (IN LIQ.)	San Marco Evangelista (Caserta)		100	100
FATA HUNTER INC.	Riverside (USA)		100	100
FATA S.P.A.	Pianezza (Turin)	100		100
FATA LOGISTIC SYSTEMS S.P.A.	Pianezza (Turin)		100	100
FINMECCANICA FINANCE S.A.	Luxembourg	73.6395	26.3578	99.9973
GA IMMOBILIARE S.P.A. (..)	Rome	100		100
GALILEO AVIONICA S.P.A. (**)	Campi Bisenzio (Florence)		100	100
ITALDATA INGEGNERIA DELL'IDEA S.P.A.	Rome		51	51
KEYCAB S.P.A.	Rome		100	96.923
LARIMART S.P.A.	Rome		60	60
MECFIN - MECCANICA FINANZIARIA S.P.A. (...)	Rome	100		100
MECFINT (JERSEY) LTD	Luxembourg		99.997	99.997
METASISTEMI S.P.A.	Rome		100	96.923
NET SERVICE S.R.L.	Bologna		70	67.846
OTE MOBILE TECHNOLOGIES LIMITED	Warwickshire (UK)		100	100
OTE S.P.A.	Florence		100	100
OTO MELARA IBERICA S.A.	Valencia (Spain)		100	100
OTO MELARA S.P.A.	La Spezia	100		100
PROD-EL - PRODOTTI ELETTRONICI S.P.A.	Milan		100	100
QUADRICS LTD	Bristol (UK)		100	100
SAGEM ITALIA S.R.L.	Genoa		100	100
SAN GIORGIO S.A.	Parigi (France)	99.999		99.999
SECURTEAM S.R.L.	Rome		100	100
SEICOS S.P.A.	Rome	100		100
SELENIA MARINE CO. LTD (IN LIQ.)	Coventry (UK)		99.99996	99.99996
SELENIA MOBILE S.P.A.	Chieti Scalo (Chieti)		100	100
SELEX COMM. DO BRASIL LTDA	Rio de Janeiro (Brazil)		100	100
SELEX COMMUNICATIONS GMBH	Backnang (Germany)		100	100
SELEX COMMUNICATIONS HOLDINGS LTD	Chelmsford (UK)		100	100
SELEX COMMUNICATIONS INC.	Mountain View (USA)		100	100
SELEX COMMUNICATIONS INTERN. LTD	Coventry (UK)		100	100
SELEX COMMUNICATIONS LTD	Coventry (UK)		100	100
SELEX COMM. ROMANIA S.R.L.	Bucharest (Romania)		99.976	99.976
SELEX COMMUNICATIONS S.P.A.	Genoa	100		100
SELEX KOMINIKASYON AS	Golbasi (Turkey)		99.999	99.999

List of companies consolidated on a line-by-line basis *(cont'd)*

Company Name	Registered Office	% owned by the Group		% contribution to the Group
		Directly	Indirectly	
SELEX COMMUNICATIONS SECURE SYSTEMS LTD	Coventry (UK)		100	100
SELEX SENSORS AND AIRBORNE SYSTEMS S.P.A. (**)	Campi Bisenzio (Florence)	75		100
SELEX SENSORS AND AIRBORNE SYSTEMS LTD (**)	Essex (UK)		100	100
SELEX SERVICE MANAGEMENT S.P.A.	Rome	100		100
SELEX SISTEMI INTEGRATI GMBH	Neuss (Germany)		100	100
SELEX SISTEMI INTEGRATI INC.	Delaware (USA)		100	100
SELEX SISTEMI INTEGRATI LTD	Portsmouth Hampshire (UK)		100	100
SELEX SISTEMI INTEGRATI S.P.A.	Rome	100		100
SC ELETTRA COMMUNICATIONS S.A.	Ploiesti (Romania)		50.5	50.4997
SIRIO PANEL S.P.A.	Montevarchi (Arezzo)		75	75
SISTEMI E TELEMATICA S.P.A.	Genoa		92.793	92.793
SO.GE.PA. SOC. GEN. DI PARTECIPAZIONI S.P.A.	Genoa	100		100
SPACE SOFTWARE ITALIA S.P.A.	Taranto		100	100
TECNOSIS S.P.A.	Genoa		100	100
TELESPAZIO LUXEMBOURG S.A. (....)	Luxembourg	99.967		100
THE DEE HOWARD CO.	Sant'Antonio, Texas (USA)		100	88.409
THOMASSEN TURBINE SYSTEMS BV	Rheden (the Netherlands)		100	100
TRANSCONTROL CORPORATION	Wilmington, Delaware (USA)		100	40
TRIMPROBE S.P.A.	Rome	100		100
UNION SWITCH & SIGNAL (MALAYSIA) SDN BHD	Kuala Lumpur (Malaysia)		100	40
UNION SWITCH & SIGNAL INC. (USA)	Dover, Delaware (USA)		100	40
UNION SWITCH & SIGNAL INC. (CAN)	Burlington, Ontario (Canada)		100	40
UNION SWITCH & SIGNAL INT. CO.	Wilmington, Delaware (USA)		100	40
UNION SWITCH & SIGNAL INT. PROJECTS CO.	Dover, Delaware (USA)		100	40
UNION SWITCH & SIGNAL PRIVATE LTD	Bangalore (India)		100	40
UNION SWITCH & SIGNAL PTY LTD	Sydney (Australia)		100	40
WESTLAND HELICOPTERS INC.	Wilmington, Delaware (USA)		100	100
WESTLAND HELICOPTERS LTD	Yeovil, Somerset (UK)		100	100
WESTLAND INDUSTRIES LTD	Yeovil, Somerset (UK)		100	100
WESTLAND SUPPORT SERVICES LTD	Yeovil, Somerset (UK)		100	100
WESTLAND TRANSMISSIONS LTD	Yeovil, Somerset (UK)		100	100
WHITEHEAD ALENIA SIST. SUBACQUEI S.P.A.	Genoa	100		100

(*) Ownership of treasury shares
(**) See Section VIII-Intangible assets
(..) Finmeccanica Group Real Estate S.p.A. from 1 January 2007
(...) Finmeccanica Group Services S.p.A. from 1 January 2007
(....) Aeromeccanica S.A. from 2007

List of companies consolidated using the proportionate method

Company Name	Registered Office	% owned by the Group		% contribution to the Group
		Directly	Indirectly	
ALCATEL ALENIA SPACE S.A.S.	Paris (France)	33		33
ALCATEL ALENIA SPACE FRANCE S.A.S.	Paris (France)		100	33
ALCATEL ALENIA SPACE ITALIA SPA	Rome		100	33
ALENIA SPAZIO NORTH AMERICA INC.	Wilmington (USA)		100	33
ALCATEL ALENIA SPACE ESPANA S.A.	Madrid (Spain)		100	33
ALCATEL ALENIA SPACE ETCA S.A.	Charleroi (Belgium)		100	33
ALCATEL ALENIA SPACE ANTWERP	Hoboken (Belgium)		100	33
FORMALEC	Paris (France)		100	33
MARILEC	Paris (France)		100	33
VANELEC	Paris (France)		100	33
TELESPAZIO HOLDING SRL	Rome	67		67
TELESPAZIO FRANCE S.A.S.	Toulouse (France)		100	67
TELESPAZIO DEUTSCHLAND GMBH	Gilching (Germany)		100	67
TELESPAZIO SPA	Rome		100	67
E-GEOS SPA	Matera		55	36.85
EURIMAGE SPA	Rome		51	34.17
TELESPAZIO BRASIL S.A.	Rio de Janeiro (Brazil)		98.534	66.018
TELESPAZIO NORTH AMERICA INC.	Doover, Delaware (USA)		100	67
TELESPAZIO HUNGARY SAT. TELEC. LTD	Budapest (Hungary)		100	67
RARTEL S.A.	Bucharest (Romania)		61.061	40.91
TELESPAZIO ARGENTINA S.A.	Buenos Aires (Argentina)		100	66.950
MARS SRL	Naples		100	67
GAF AG	Munich (Germany)		100	67
EUROMAP SATELLITENDATEN-VERTRIEB MBH	Neustrelitz (Germany)		100	67
AMSH BV	Amsterdam (the Netherlands)	50		50
MBDA S.A.S.	Paris (France)		50	25
MBDA ITALIA SPA	Rome		100	25
MBDA UK LTD	Stevenage (UK)		100	25
MBDA FRANCE S.A.S.	Paris (France)		100	25
MATRA ELECTRONIQUE S.A.	Paris (France)		100	25
ALKAN S.A.	Paris (France)		100	25
MBDA INCORPORATED	Wilmington, Delaware (USA)		100	25
MBDA TREASURE COMPANY LTD	Jersey (UK)		100	25
MBDA SERVICES S.A.	Paris (France)		99.76	24.94
MARCONI OVERSEAS LTD	Londra (UK)		100	25
LFK-LENKFLUGKORPERSYSTEME GMBH	Unterschleibheim (Germany)		100	25
AVIATION TRAINING INTERNATIONAL LIMITED	Dorset (UK)		50	50
CONSORZIO ATR-GIE e S.P.E.	Toulouse (France)		50	50

List of companies consolidated using the equity method

Company Name	Registered Office	% owned by the Group		% contribution to the Group
		Directly	Indirectly	
ABU DHABI SYSTEMS INTEGRATION LLC	Abu Dhabi (United Arab Emirates)		43.043	43.043
ADVANCED AIR TRAFFIC SYSTEMS SDN BHD	Darul Ehsan (Malaysia)		40	40
ADVANCED LOGISTICS TECHNOLOGY ENGINEERING CENTER S.P.A.	Turin		51	16.83
ALENIA HELLAS S.A.	Kolonaki (Athens) (Greece)		100	100
ALENIA NORTH AMERICA-CANADA CO	Halifax (Canada)		100	88.409
ALIFANA DUE S.C.R.L.	Naples		53.34	21.336
ALIFANA SCRL	Naples		65.85	26.34
ANSALDO ARGENTINA S.A.	Buenos Aires (Argentina)		99.98	99.98
ANSALDO DO BRASIL E.E. LTDA	San Paolo (Brazil)		99.999	99.999
ANSALDO ELECTRIC DRIVES S.P.A.	Genoa		100	100
ANSALDO - E.M.I.T. S.C.R.L.	Genoa		50	50
ANSALDO ENERGY INC.	Wilmington, Delaware (USA)		100	100
ANSALDO INVEST DENMARK AS (IN LIQ.)	Gentofte (Denmark)		100	100
ANSALDO TRASMISSIONE E DISTRIBUZIONE S.P.A.	Genoa		30	30
ANSERV S.R.L.	Bucharest (Romania)		100	100
AUTOMATION INTEGRATED SOLUTIONS S.P.A.	Pianezza (Turin)		40	40
AVIONS DE TRANSPORT REGIONAL IRELAND LIMITED	Dublin (Ireland)		50	50
AVIONICS SENSORS US INC. (**)	Wilmington, Delaware (USA)		100	100
BELL AGUSTA AEROSPACE COMPANY LLC	Wilmington, Delaware (USA)		45	45
BRITISH HELICOPTERS LTD	Yeovil, Somerset (UK)		100	100
CARDPRIZE TWO LIMITED (**)	Basildon, Essex (UK)		100	100
CLOSED JOINT STOCK COMPANY MAREMS	Moscow (Russia)		49.001	49.001
COMLENIA SENDIRIAN BERHAD	Selangor Darul Ehsan (Malaysia)		30	30
CONSORZIO PER IL GIURISTA D'IMPRESA S.C.R.L.	Genoa		22.7	22.7
CONSORZIO START S.P.A.	Rome		40	40
DOGMATIX LEASING LIMITED	Mauritius		100	50
ECOSEN S.A.	Caracas (Venezuela)		48	19.2
ELETTRONICA S.P.A.	Rome	31.333		31.333
ELSACOM BULGARIA AD	Sofia (Bulgaria)		90	89.997
ELSACOM HUNGARIA KFT	Budapest (Hungary)		100	99.999
ELSACOM SLOVAKIA SRO	Bratislava (Slovakia)		100	99.999
ELSACOM-UKRAINE JOINT STOCK COMPANY	Kiev (Ucraine)		49	49
ELSAG EASTERN EUROPE S.R.L.	Bucharest (Romania)		75	75
ELSAG GEST S.P.A.	Genoa		30	30
ELSAG INC.	Washington D.C. (USA)		100	100
ENCOM CONSTRUCOES E MONTAGENS LTDA	Sao Paolo (Brazil)		95.555	95.555
ENERGEKO GAS ITALIA S.R.L.	Brindisi		22.631	22.631
EURISS N.V.	Leiden (the Netherlands)		25	8,25
EUROFIGHTER AIRCRAFT MANAGEMENT GMBH	Hallbergmoos (Germany)		21	21
EUROFIGHTER JAGDFLUGZEUG GMBH	Hallbergmoos (Germany)		21	21
EUROFIGHTER INTERN. LTD	London (UK)		21	21
EUROFIGHTER SIMUL. SYST. GMBH	Unterhaching (Germany)		24	18
EUROMIDS S.A.S.	Paris (France)		25	25
EUROPEA MICROFUSIONI AEROSPAZIALI S.P.A.	Morra De Sanctis (Avellino)	49		49
EUROPEAN CO. FOR MOBILE COMM. SERV. BV (IN LIQ.)	Amstelveen (the Netherlands)		100	100
EURO PATROL AIRCRAFT GMBH	Munich (Germany)		50	50
EUROSYSNAV S.A.S.	Paris (France)	50		50
FATA AUTOMATION GMBH (IN LIQ.)	Frankfurt (Germany)		100	100
FATA AUTOMATION SRO (IN LIQ.)	Kosmonosy (Czech Republic)		100	100
FATA CONTRACTING LTD	Moscow (Russia)		100	100
FATA ENGINEERING S.A. (IN LIQ.)	Fribourg (Switzerland)		100	100
FATA HUNTER INDIA PVT LTD	New Dehli (India)		100	100
FATA POLAND LTD	Bielsko Biala (Poland)		100	100
FINMECCANICA INC.	Dover, Delaware (USA)	100		100
FINMECCANICA UK LTD	London (UK)	100		100

List of companies consolidated using the equity method *(cont'd)*

Company Name	Registered Office	% owned by the Group		% contribution to the Group
		Directly	Indirectly	
GALILEO INDUSTRIES GMBH (.)	Ottobrunn (Germany)	18.94	18.94	25.19
GALILEO INDUSTRIES S.A.	Brussels (Belgium)	18.94	18.94	25.19
GALILEO VACUUM SYSTEMS SPA	Prato		24,9	24,9
GIEINTER AG	Lugano (Switzerland)		100	100
GLOBAL AERONAUTICA LLC	Delaware (USA)		50	44.2045
GLOBAL MILITARY AIRCRAFT SYSTEMS LLC	Greenville (USA)		50	44.2045
GROUPEMENT IMMOBILIER AERONAUTIQUE G.I.A. S.A.	Blagnac (France)		20	20
IAMCO SCRL	Mestre (Venice)		20	20
ICARUS SCPA	Turin		49	49
IGS SPA (IN LIQ.)	Rome	100		100
IMMOBILIARE CASCINA SRL	Gallarate (Varese)		100	100
IMMOBILIARE FONTEVERDE SRL	Rome		60	48
INTERNATIONAL LAND SYSTEMS INC.	Wilmington, Delaware (USA)		28.37	19
IRIDIUM ITALIA SPA (IN LIQ.)	Rome		35	35
I.M. INTERMETRO SPA	Rome		33.333	23.338
I.T.I.S.A. S.A. (IN LIQ.)	Nanterre (France)		100	100
IVECO FIAT - OTO MELARA SCRL	Rome		50	50
JIANGXI CHANGE AGUSTA HELICOPTER CO. LTD	Zone Jiangxi Province (China)		40	40
LIBYAN ITALIAN ADVANCED TECHNOLOGY CO	Tripoli (Libya)	25	25	50
LMATTS LLC	Georgia (USA)		50	44.21
MACCHI HUREL DUBOIS S.A.S.	Meudon La Foret (France)		50	49.99
MEDESSAT S.A.S.	Tolosa (France)		28.801	19.296
METRO 5 SPA	Milan		31.9	17.14
MUSI NET ENGINEERING SPA	Turin		49	49
NAHUELSAT S.A.	Buenos Aires (Argentina)	33.332		33.33
NGL PRIME SPA	Turin	30		30
N.H. INDUSTRIES SARL	Aix-en-Provence (France)		32	32
NICCO COMMUNICATIONS S.A.S.	Colombes (France)		50	50
NNS - SOC. DE SERV. POUR REACTEUR RAPIDE S.N.C.	Lione (France)		40	40
ORIZZONTE - SISTEMI NAVALI SPA	Genoa	49		49
OTE M	Moscow (Russia)		100	100
OTO MELARA NORTH AMERICA INC.	Washington D.C. (USA)		100	100
PEGASO SCRL	Rome		46.87	18.748
POLARIS SRL	Genoa		50	50
PT DAYALISTRIK PRATAMA (IN LIQ.)	Jakarta (Indonesia)		45	45
QUADRICS INC.	New Castle, Delaware (USA)		100	100
REMINGTON ELSAG LAW ENFORCEMENT SYST.	Madison (USA)		50	50
ROXEL S.A.S.	Le Plessis Robinson (France)		50	12.5
SAPHIRE INTERNAT. ATC ENGINEERING CO. LTD	Beijing (China)		65	65
SELEX SENSORS AND AIRBORNE SYSTEMS ELECTRO OPTICS (OVERSEAS) LTD (**)	Basildon Essex (UK)		100	100
SELEX SENSORS AND AIRBORNE SYSTEMS INFRARED LTD (**)	Basildon Essex (UK)		100	100
SELEX SISTEMI INTEGRATI DE VENEZUELA S.A.	Caracas (Venezuela)		100	100
SEVERNYJ AVTOBUZ Z.A.O.	San Pietroburgo (Russia)		35	35
SISTEMI DINAMICI SPA	San Piero a Grado (Pisa)		40	40
SOGELI - SOCIETÀ DI GESTIONE DI LIQ. SPA	Rome		100	100
SOSTAR GMBH	Immerstad (Germany)		28.2	21.15
TELBIOS SPA	Milan		31.034	20.793
TELESPAZIO NETHERLAND BV	Enschede (the Netherlands)		100	67
THOMASSEN SERVICE AUSTRALIA PTY LTD	Canning Vale (Australia)		100	100
THOMASSEN SERVICE GULF LLC	Abu Dhabi (United Arab Emirates)		48.667	48.667
TRADE FATA BV	Rotterdam (the Netherlands)		100	100
WESTLAND INDUSTRIAL PRODUCTS LTD	Yeovil, Somerset (UK)		100	100
WITG L.P. INC.	Dover, Delaware (USA)		24	21.22
WITG L.P. LTD	Dover, Delaware (USA)		20	17.68
ZAO ARTETRA	Moscow (Russia)		51	51

(.) European Satellite Navigation Industries GmbH dal 2007
(**) See Section VIII-Intangible assets

List of companies valued at fair value

Company Name	Registered Office	% owned by the Group		% contribution to the Group
		Directly	Indirectly	
BCV INVESTMENTS S.C.A.	Luxembourg		15	15
BCV MANAGEMENT S.A.	Luxembourg		14,999	14,999
STMICROELECTRONICS HOLDING N.V.	Amsterdam (the Netherlands)	20		20

List of subsidiaries and associates valued at cost

Company Name	Registered Office	% owned by the Group		% contribution to the Group
		Directly	Indirectly	
ALENIA IMPROVEMENT S.P.A.	Pomigliano D'Aarco (Naples)		100	100
CCRT SISTEMI SPA (IN BANKRUPTCY)	Milan		30,34	30,34
FOSCAN SRL (IN BANKRUPTCY)	Anagni (Frosinone)		20	20
IND. AER. E MECC. R. PIAGGIO SPA (IN EXTR. ADMIN.)	Genoa	30,982		30,982
SAITECH SPA (IN BANKRUPTCY)	Passignano (Perugia)		40	40
SCUOLA ICT S.R.L.	L'Aquila	20		20
UNION SWITCH & SIGNAL (CHILE) LTDA	Santiago (Chile)		68	27,2
U.V.T. SPA (IN BANKRUPTCY)	San Giorgio Jonico (Taranto)		50,613	50,613
U.V.T. ARGENTINA S.A.	Buenos Aires (Argentina)		60	30,368

Subsidiaries and entities controlled jointly

In particular, the entities over which Finmeccanica exercises a controlling power, either by directly or indirectly holding a majority of shares with voting rights or by exercising a dominant influence through the power to govern the financial and operating policies of an entity and obtain the related benefits regardless of the nature of the shareholding, have been consolidated on a line-by-line basis.

Not consolidated on a line-by-line basis are those entities which, because of the dynamics of their operations (e.g. consortiums without shares and controlling interests in equity consortiums which, by charging costs to their members, do not have their own financial results and the financial statements of which do not, net of intercompany assets and liabilities, have material balances) or their current status (e.g. companies that are no longer operational, have no assets or personnel, or for which the liquidation process appears to be essentially concluded), would be immaterial to the Group's situation in both quantitative and qualitative terms. These holdings have been consolidated using the equity method.

Participating interests in entities (including special-purpose entities) over which control is exercised jointly with other parties are consolidated proportionally (so as to incorporate only the value of the assets, liabilities, costs and income proportional to the percentage held without, therefore, including the holdings of the other parties).

All controlled entities are consolidated at the date on which control was acquired by the Group. The entities are removed from the consolidated financial statements at the date on which the Group relinquishes control.

Business combinations are recognised using the purchase method, whereby the acquirer purchases the equity and recognises all assets and liabilities, even if merely potential, of the acquired company. The cost of the transaction includes the fair value at the date of purchase of the assets sold, the liabilities assumed, the capital instruments issued, and all other incidental charges. Any difference between the cost of the transaction and the fair value at the date of purchase of the assets and liabilities is allocated to goodwill. In the event the process of allocating the purchase price should result in a negative difference, this difference is recorded as an expense immediately at the purchase date.
In the case of purchase of controlling stakes other than 100% stakes, goodwill is recognised only to the extent of the portion attributable to the Group Parent.

Amounts resulting from transactions with consolidated entities have been eliminated, particularly where related to receivables and payables outstanding at the end of the period, as well as interest and other income and expenses recorded on the income statements of these enterprises. Also eliminated are the net profits or losses posted between the consolidated entities along with their related tax adjustments.

The consolidated entities all close their financial years on 31 December. The Group consolidated financial statements have been prepared based on the ending balances at 31 December.

Owner equity investments

Investments in entities over which significant influence is exercised, which generally corresponds to a holding of between 20% and 50%, are accounted for either using the equity method or at fair value. In the case of the equity method, the value of the investment is in line with shareholders' equity adjusted, when necessary, to reflect the application of IFRSs, and includes the recognition of goodwill (net of impairments) calculated at the time of purchase, and to account for the adjustments required by the standards governing the preparation of consolidated financial statements. Unrealised gains and losses on transactions between the Group and its associates are eliminated to the extent of the Group's interest in the associates.
Any value losses in excess of book value are recorded in the provision for risks on equity investments if there is an obligation to cover these losses.

The fair value of equity investments, in the event this method applies, is calculated based on the bid price of the last trading day of the month for which

the IFRS consolidated financial statements were prepared (in this case 29 December 2006).

III.2 Segment information

The Group considers the organisation by industry to be 'primary', as company risks and benefits are influenced significantly by differences in the products and services provided, with the organisation by geographic area being 'secondary', as company risks and benefits are also significantly influenced by operating in different countries or different geographic areas.

III.3 Currency translation

Identification of the functional currency

The balances of the financial statements of each Group entity are presented in the currency of the primary economy in which each enterprise operates (the functional currency). The consolidated financial statements for the Finmeccanica Group have been prepared in euros, which is the functional currency of the Group Parent.

Translation of transactions denominated in a foreign currency

Items expressed in a currency other than the functional currency, whether monetary (cash and cash equivalents, receivables or payables due in pre-set or measurable amounts, etc.) or non-monetary (advances to suppliers of goods and services, goodwill, intangible assets, etc.), are initially recognised at the exchange rate prevailing at the date on which the transaction takes place. Subsequently, the monetary items are translated into the functional currency based on the exchange rate at the reporting date, and any differences resulting from this conversion are recognised in the income statement. Non-monetary items continue to be carried at the exchange rate on the date of the transaction, except in situations where there is a persistent unfavourable trend in the exchange rate concerned. If this is the case, exchange differences are recognised in the income statement.

Translation of financial statements expressed in a currency other than the functional currency

The rules for translating financial statements expressed in a foreign currency into the functional currency (except where the currency is that of a hyper-inflationary economy, a situation not applicable to the Group), are as follows:

- the assets and liabilities presented, even if solely for comparative purposes, are translated at the end-of-period exchange rate;
- costs and revenues, charges and income presented, even if solely for comparative purposes, are translated at the average exchange rate for the period in question, or at the exchange rate on the date of the transaction in the event this is significantly different from the average rate;
- the "translation reserve" includes both the exchange rate differences generated by the translation of balances at a rate different from that at the close of the period and those that are generated by the translation of opening balances of shareholders' equity at a rate different from that at the close of the period.

Goodwill and adjustments to fair value related to the acquisition of a foreign entity are treated as assets and liabilities of the foreign entity and translated at the end-of-period.

III.4 Intangible assets

Intangible assets are non-monetary items without physical form, but which can be clearly identified and generate future economic benefits for the company. They are carried at purchase and/or production cost, including directly related expenses allocated to them when preparing the asset for operations and net of accumulated amortisation (with the exception of intangibles with an indefinite useful life) and any permanent impairments of value. Amortisation begins when the asset is available for use and is recognised systematically over its remaining useful life. In the period in which the intangible asset is recognised for the first time, the amortisation rate applied takes into account the period of actual use of the asset.

Development costs

This account includes costs related to the application of the results of research or other knowledge in a plan or a project for the production of materials, devices, processes, systems or services that are new or significantly advanced, prior to the start of commercial production or use, for which the generation of future economic benefits can be demonstrated. These costs are amortised over the entire period in which the future earnings are expected to be realised for the project itself. If such costs fall within the scope of costs defined by Group standards as "non-recurring costs", they are recognised in a special item within intangible assets (Note 4.1).
Research costs, on the other hand, are expensed in the period in which they are incurred.

Industrial patent and intellectual property rights

Patents and intellectual property rights are carried at acquisition cost net of amortisation and accumulated impairment losses. Amortisation begins in the period in which the rights acquired are available for use and is calculated based on the shorter of the period of expected use and that of ownership of the rights.

Concessions, licenses and trademarks

This category includes: concessions, i.e. government measures that grant private parties the right to exclusive use of public assets or to manage public services under regulated conditions; licences that grant the right to use patents or other intangible assets for a determinate or determinable period of time; trademarks that establish the origin of the products of a given company; and licences for the know-how or software owned by others. The costs, including the direct and indirect costs incurred to obtain such rights, can be capitalised after receiving title to the rights themselves and are amortised systematically over the shorter of the period of expected use and that of ownership of the rights.

Goodwill

Goodwill recognised as an intangible asset is associated with business combinations and represents the difference between the cost incurred to acquire a company or division and the sum of the values assigned, based on current values at the time of the acquisition, to the individual assets and liabilities of the given company or division. As it does not have a definite useful life, goodwill is not amortised but is subject to impairment tests conducted at least once a year, unless market and operational factors identified by the Group indicate that an impairment test is also necessary in the preparation of interim financial statements. In conducting an impairment test, goodwill is allocated to the individual cash-generating units (CGUs), i.e. the smallest financially independent business units through which the Group operates in its various market segments.
Goodwill related to the acquisition of consolidated companies is recognised under intangible assets. Goodwill related to unconsolidated associated companies or subsidiaries is included in the value of investments.

III.5 Property, plant and equipment

Property, plant and equipment is measured at purchase or production cost net of accumulated depreciation and any impairment losses. The cost includes all direct costs incurred to prepare the assets for use, as well as any charges for dismantlement and disposal that will be incurred to return the site to its original condition.
Charges incurred for routine and/or cyclical maintenance and repairs are expensed in full in the period in which they are incurred. Costs related to the expansion, modernisation or improvement of owned or leased structural assets are only capitalised to the extent that such costs meet the requirements for being classified separately as an asset or part of an asset. Any public capital grants related to property, plant and equipment are recognised as a direct deduction from the asset to which they refer.
The value of an asset is adjusted by systematic depreciation calculated based on the residual useful life of the asset itself. In the period in which the asset is recognised for the first time, the depreciation rate applied takes into account the period of actual use of the asset. The estimated useful lives adopted by the Group for the various asset classes are as follows:

	Years
Land	indefinite useful life
Buildings	20-33
Plants and machinery	5-10
Equipment	3-5
Other assets	5-8

In the event the asset to be depreciated is composed of distinct elements with useful lives that are significantly different from those of the other constituent parts, each individual part that

makes up the asset is depreciated separately, in application of the component approach to depreciation.

This item also includes equipment intended for specific programmes (tooling), although it is depreciated, as with other non-recurring costs (see Note 4.1), on the basis of units manufactured in relation to those expected to be produced.

The gains and losses from the sale of assets or groups of assets are calculated by comparing the sales price with the related net book value.

III.6 Investment properties

Those investments that can generate cash flows, regardless of the company business, are carried under "investment properties"; they are valued at purchase or construction cost plus any related charges, net of accumulated depreciation and impairment, if any.

III.7 Impairment of intangible assets and property, plant and equipment

Assets with indefinite lives are not depreciated or amortised, but are rather subject to impairment tests at least once a year to ascertain the recoverability of their book value.
For assets that are depreciated or amortised, an assessment is made to determine whether there is any indication of a loss in value. If so, the recoverable value of the asset is estimated, with any excess being recognised in the income statement.
If the reasons for such write-downs should cease to obtain, the asset's book value is restored within the limits of its net book value; the write-back is also taken to the income statement. Under no circumstances, however, is the value of goodwill that has been written down restored to its previous level.

III.8 Equity investments

The Group classifies its equity investments as follows:

- "subsidiaries" in which the owner of the interest has the power to determine the financial and operating decisions and to receive the related benefits;
- "associated companies" in which the owner of the interest exercises significant influence (which is assumed to exist when owner can exercise at least 20% of the votes in the Ordinary Shareholders' Meeting). This also includes companies subject to joint control (joint ventures);
- "parent companies", when the company held holds shares in its own parent;
- "other companies" that do not fall under any of the categories above.

Equity investments due to be sold and those purchased for the sole purpose of being sold within 12 months are classified separately under "assets held for sale".

Subsidiaries (including those subject to joint control), associates and other companies, with the exception of those that are held for sale, are recognised at the cost of purchase or start-up posted in the separate accounts of the companies of the Group that have been prepared for consolidation purposes. The cost value is maintained in subsequent financial statements except in the event of a loss of value, or any write-back, following a change in its economic use or capital transactions. Equity investments held for sale are carried at the lower of cost and fair value net of sales costs.

III.9 Inventories

Inventories are recorded at the lower of cost and net realisable value. The Group used the weighted average cost method. The net realisable value is the sales price in the course of normal operations net of estimated costs to finish the goods and those needed to make the sale. Any write-downs made with regard to any risk of obsolescence are eliminated in future periods if the reason for the write-down should cease to obtain.
The Group classifies inventories as follows:

- raw materials, supplies and consumables;
- work in progress and semi-finished goods;
- finished products;
- goods.

Work in progress is recognised at production cost using the weighted average cost, excluding financial charges and general overheads.

III.10 Contract work in progress

Work in progress is recognised on the basis of progress (or percentage of completion), whereby costs, revenues and margins are recognised based on the progress of production. The state of completion is determined on the basis of the ratio between costs incurred at the measurement date and the total expected costs for the programme. The valuation reflects the best estimate of the schedules prepared at the reporting date. The assumptions upon which the valuations are made are periodically updated. Any impact on profit or loss are recognised in the period in which the updates are made.
In the event the completion of a contract is expected to result in a loss at the gross margin level, the loss is recognised in its entirety in the period in which it becomes reasonably foreseeable.
Contract work in progress is recorded net of any write-downs, as well as pre-payments and advances related to the contract being performed. This analysis is carried out contract by contract: in the event of positive differences (where the value of work in progress is greater than total pre-payments), the difference is recorded as an asset; negative differences, on the other hand, are recorded as a liability under "due to customers for contract work". If it has not been collected at the date of preparation of the annual or interim accounts, the amount recorded among advance payments will have a directly contra-item in trade receivables.
Contracts with payments in a currency other than the functional currency (the euro for the Group) are measured by converting the portion of payments due, calculated using the percentage-of-completion method, at the exchange rate prevailing at the close of the period in question. However, the Group's policy for exchange-rate risk calls for all contracts in which cash inflows and outflows are significantly exposed to exchange rate fluctuations to be hedged specifically. In such cases, the recognition methods described in Note 4.3 below are applied.

III.11 Receivables and financial assets

The Group classifies its financial assets into the following categories:

- financial assets at fair value through profit or loss;
- loans and receivables;
- held-to-maturity financial assets;
- available-for-sale financial assets.

Management classifies assets at the time they are first recognised.

Financial assets at fair value through profit or loss

This category includes financial assets acquired for the purpose of short-term trading transactions, or designated for this use by management, as well as derivatives, which are discussed in the next section. The fair value of these instruments is determined with reference to their end-of-period bid price. For unlisted instruments, the fair value is calculated using commonly adopted valuation techniques. Changes in the fair value of instruments in this category are recognised immediately in the income statement.
The classification of assets as current or non-current reflects management expectations regarding their trading. Current assets include those that are planned to be sold within 12 months or those designated as held for trading purposes.

Loans and receivables

This category includes non-derivative financial assets with fixed or determinable payments that are not quoted on an active market. They are measured at their amortised cost using the effective interest method. Should objective evidence of impairment emerge, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in profit or loss – is removed from equity and recognised in the income statement. If the reasons for the write-down should cease to obtain, the value of the asset is restored up to the amortised cost value it would have if no impairment had been recognised. Loans and receivables are posted under current assets except for the portion falling due beyond 12 months, which is carried under non-current assets.

Financial assets held to maturity

These are non-derivative assets with fixed maturities that the Group has the intention and ability to hold to maturity. Those maturing within 12 months are carried as current assets. Should objective evidence of impairment emerge, the

cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in profit or loss – is removed from equity and recognised in the income statement. If the reasons for the write-down should cease to obtain in future periods, the value of the asset is restored up to the amortised cost value it would have if no impairment had been recognised.

Financial assets available for sale

This category encompasses non-derivative financial assets specifically designated as available for sale or not classified in any of the previous items. They are recognised at fair value, which is calculated with reference to their market price at the reporting date or using financial valuation techniques and models. Changes in value are recognised in a specific equity reserve ("Reserve for assets available for sale"). The reserve is taken to the income statement only when the financial asset is effectively sold or, in cases of a loss of value, when it becomes evident that the impairment in value already recognised in equity is unrecoverable. Classification as current or non-current depends on the intentions of management and the effective marketability of the security itself. Assets that are expected to be sold within 12 months are carried under current assets. Should objective evidence of impairment emerge, the value of the asset is reduced to the value obtained by discounting the expected cash flows from the asset; reductions in value previously recognised in equity are reversed to profit or loss. If the reasons for the write-down should cease to obtain, the value of the asset is restored.

III.12 Derivatives

Derivatives are still regarded as assets held for trading and stated at fair value through profit and loss unless they are deemed eligible for hedge accounting and effective in offsetting the risk in respect of underlying assets, liabilities or commitments undertaken by the Group.
In particular, the Group uses derivatives as part of its hedging strategies to offset the risk of changes in the fair value of assets or liabilities on its balance sheet or the risk associated with contractual commitments (fair value hedges) and the risk of changes in expected cash flows in contractually defined or highly probable operations (cash flow hedges). For details regarding the methodology for recognising hedges of the exchange rate risk on long-term contracts, see Note 4.3.

The effectiveness of hedges is documented both at the start of the operation and periodically thereafter (at least every time an annual or interim report is published) and measured by comparing changes in the fair value of the hedging instrument against changes in the hedged item ('dollar offset ratio'). For more complex instruments, the measurement involves statistical analysis based on the variation of the risk.

Fair value hedge

Changes in the value of derivatives that have been designated and qualify as fair value hedges are recognised in profit or loss, similarly to the treatment of changes in the fair value of the hedged assets or liabilities that are attributable to the risk that has been offset with the hedge.

Cash flow hedge

Changes in the fair value of derivatives that have been designated and qualify as cash flow hedges are recognised – with reference to the 'effective' component of the hedge only – in a specific equity reserve ("cash flow hedge reserve"), which is subsequently recognised in profit or loss when the underlying transaction affects profit or loss. Changes in fair value attributable to the non-effective component are immediately recognised in profit or loss for the period. If the derivative is sold, or ceases to function as an effective hedge against the risk for which it was originated, or the occurrence of the underlying operation ceases to be highly probable, the relevant portion of the cash flow hedge reserve is immediately recognised in the income statement.

Determining fair value

The fair value of instruments quoted on public markets is determined with reference to the bid price for the instrument in question at the reference date. The fair value of unquoted instruments is determined with financial valuation techniques. Specifically, the fair value of interest rate swaps is measured by discounting the expected cash flows, while the fair value of foreign exchange forwards is determined on the basis of the market exchange rate at the reference date and the rate differentials among the currencies involved.

III.13 Cash and cash equivalents

The item includes cash, deposits with banks or other institutions providing current account services, post office accounts and other cash equivalents, as well as investments maturing in less than three months from the date of acquisition. Cash and cash equivalents are recognised at their fair value.

III.14 Shareholders' equity

Share capital

Share capital consists of the capital subscribed and paid up by the Group Parent. Costs directly associated with the issue of shares are recognised as a decrease in share capital when they are directly attributable to capital operations.

Treasury shares

Treasury stock is recognised as a decrease in Group shareholders' equity. The costs incurred in the issue of new shares by the Group Parent are recognised as decreases in shareholders' equity, net of any deferred tax effect. Gains or losses realised in the acquisition, sale, issue or cancellation of treasury stock are recognised directly in shareholders' equity.

Profits (losses) carried forward

These include net profits or losses for the period and for previous years that are not distributed or allocated to reserves (for profits) or covered (for losses). The item also includes transfers from other equity reserves when the restrictions on their release cease to apply, as well as the effects of changes in accounting policies and significant errors.

Other reserves

They include the fair value reserve relating to items accounted for using the fair value method recognised in equity and the cash flow hedge reserve in respect of the effective portion of such hedges.

III.15 Payables and other liabilities

Payables and other liabilities are initially recognised at fair value net of transaction costs. They are subsequently valued at their amortised cost using the effective interest rate method (see Note 3.22). Payables and other liabilities are defined as current liabilities unless the Group has the contractual right to settle its debts at least 12 months after the reporting date.

III.16 Deferred tax assets and liabilities

Deferred tax assets and liabilities are calculated based on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. Deferred tax assets and liabilities are calculated by applying the tax rate in force at the time the temporary differences will be reversed. Deferred tax assets are recognised to the extent that it is probable the company will post taxable income at least equal to the temporary differences in the financial periods in which such assets will be reversed.

III.17 Employee benefits

Post-employment benefits plans

Group companies use several types of pension and supplementary benefit plans, which can be classified as follows:

- defined contribution plans in which the company pays fixed amounts to a distinct entity (e.g. a fund) but has no legal or constructive obligation to make further payments if the fund does not have sufficient assets to pay the benefits accrued by employees during their period of employment with the company. The company recognises the contributions to the plan only when employees rendered their services to the company specifically in exchange for these contributions;
- defined benefit plans in which the company undertakes to provide agreed benefits for current and former employees and incur the actuarial and investment risks associated with the plan. The cost of the plan is therefore not determined by the amount of the contributions payable in the financial period but, rather, is redetermined with reference to demographic and statistical assumptions and wage trends. The methodology used is the projected unit credit method. The *"trattamento di fine rapporto"*, a staff severance pay mechanism peculiar to Italy, belongs to this category.

In compliance with IAS 19, the Finmeccanica Group uses the so-called "corridor" approach in recognising actuarial losses and gains relating to defined benefit plans. This method makes it possible to dilute the effects of changes in the valuation parameters over a number of financial years. Consequently, net actuarial losses and gains at the end of the prior period that exceed the greater of 10% of the present value of the obligation and 10% of the fair value of the benefit plan assets divided by the remaining working life of employees are recognised in each period.

Other long-term benefits and post-employment benefits

Group companies grant employees with other benefits (such as seniority bonuses after a given period of service with the Company) that, in some cases, continue to be provided after retirement (for example, medical care). These receive the same accounting treatment as defined benefit plans, using the projected unit credit method. However, the corridor approach cannot be used for 'other long-term benefits'. Consequently, net actuarial gains and losses are recognised both immediately and in full as they occur.

Benefits payable for the termination of employment and incentive plans

Termination benefits are recognised as liabilities and expenses when the enterprise is demonstrably committed to terminating the employment of an employee or group of employees before the normal retirement date or to providing termination benefits as a result of an offer made in order to encourage voluntary redundancy. The benefits payable to employees for the termination of employment do not bring any future economic benefit to the enterprise and are therefore recognised immediately as expenses.

Equity compensation benefits

The Group uses stock option plans as part of its compensation of senior management. In these cases, the theoretical benefit attributable to the recipients is charged to the income statement in the financial periods for which the plan is operative with a contra-item in an equity reserve. The benefit is quantified by measuring the fair value of the assigned instrument using financial valuation techniques that take account of market conditions and, at the date of each annual or interim report, an updated estimate of the number of instruments expected to be distributed.

III.18 Provision for risks and charges

Provisions for risks and charges cover certain or probable losses and charges whose timing or amount was uncertain at the reporting date.
The provision is recognised only when a current obligation (legal or constructive) exists as a result of past events and it is probable that an outflow of economic resources will be required to settle the obligation. The amount reflects the best current estimate of the cost of fulfilling the obligation. The interest rate used to determine the present value of the liability reflects current market rates and includes the additional effects relating to the specific risk associated with each liability.
Risks for which the emergence of a liability is merely a possibility are reported in the section in the notes on commitments and risks and no provision is recognised.

III.19 Leasing

Group entities as lessees in a finance lease

At the date on which a lease is first recognised, the lessee records a non-current asset and a financial liability at the lower of the fair value of the asset and the present value of the minimum lease payments at the date of the inception of the lease, using the implicit interest rate in the lease or the incremental borrowing rate. Subsequently, an amount equal to the depreciation expense for the asset and the finance charge separated from principal component of the lease payment made in the period is recognised in the income statement.

Group entities as lessors in a finance lease

At the date on which a lease is first recognised, the value of the leased asset is eliminated from the balance sheet and a receivable equal to the net investment in the lease is recognised. The net investment is the sum of the minimum payments plus the residual unguaranteed value discounted at the interest rate implicit in the lease contract. Subsequently, financial income is recognised in the income statement for the duration of the contract in an amount providing a constant periodic rate of return on the lessor's net investment.
The unsecured residual value is reviewed periodically for possible impairment.

Operating leases

Receipts and payments in respect of contracts qualifying as operating leases are recognised in the income statement over the duration of the contract.

III.20 Revenue

Revenues generated by an operation are recognised at the fair value of the amount received and receivable, inclusive of volume discounts and reductions. Revenues also include changes in work in progress, the accounting policies for which were described in Note 3.10 above.
Revenues generated from the sale of goods are recognised when the enterprise has transferred to the buyer substantially all of the significant risks and rewards of ownership of the goods, which, in many cases, will coincide with the transfer of title or possession to the buyer; and when the value of the revenues can be reliably determined.
Revenues from services are recognised on a percentage-of-completion method when they can be reliably estimated.

III.21 Government grants

Once formal authorisation for their assignment has been issued, grants are recognised on an accruals basis in direct correlation with the costs incurred. Specifically, set-up grants are taken to the income statement in direct relation to the depreciation of the relevant goods or projects, and are recognised as a direct reduction in the value of the depreciation expense.

III.22 Financial income and expense

Interest is recognised on an accruals basis using the effective interest rate method, i.e. the interest rate that results in the financial equivalence of all inflows and outflows (including any premiums, discounts, commissions, etc.) that make up a given operation.
Financial expense is never capitalised.

III.23 Dividends

Dividends are recognised as soon as shareholders obtain the right to receive payment, which is normally when the Shareholders' Meeting approves the distribution of dividends.
Dividends distributed to Finmeccanica shareholders are recognised as liabilities for the period in which their distribution is approved by the Shareholders' Meeting.

III.24 Emission rights

In expectation of specific rules governing emission rights, the Group recognises only income and expense items and assets and liabilities arising from the sale and/or purchase of emission rights to cover deficits for the sale of any surpluses among the shares assigned and the effective emissions produced. Specifically, they are recognised in a special provision for risk if the estimated emissions are higher than the allocated share and if it is believed that the deficit has to be covered by acquiring rights in the marketplace.

III.25 Transactions with related parties

Transactions with related parties are carried out at arm's length.

III.26 Costs

Costs are recorded in compliance with the inherence principle and the matching principle.

III.27 Seasonality of the core business

Cash flows relating to operations

The businesses in which the Group is primarily active are characterized by a high concentration of cash flows from customers in the closing months of the year. This pattern affects both the interim cash flow statements and the volatility of the debt situation of the Group over each interim period, which shows a marked improvement in the final months of the calendar year.

III.28 New IFRSs and IFRIC interpretations

Over the last months of 2006 the IASB and the International Financial Reporting Interpretations Committee (IFRIC) published new standards and interpretations. Although at the date of preparation of this report the standards and interpretations are not compulsory or have not been endorsed by the European Commission, the Group has considered their effects and reported their potential impact on its balance sheet and income statement, as follows:

IFRS – IFRIC interpretation		Effects for the Group
IFRS 6 Amendment	Exploration for and evaluation of mineral assets	N/A
IAS 19 Amendment	Employee benefits	The Group expects to apply these changes from 1 January 2007
IAS 39 Amendments	Financial instruments	Not significant
IFRS 4 Amendment	Insurance contracts	N/A
IFRS 7	Disclosures and changes to IAS 1 - Presentation of financial statements	The application of this standard implies disclosures on financial instruments and capital
IFRIC 4	Determining a lease contract	Not significant
IFRIC 5	Rights from interests and Environmental Rehabilitation Funds	N/A
SIC 12 Amendment	Special purpose entities	Not significant
IFRIC 6	Liabilities arising from participating in a specific market - Waste electrical and electronic equipment	N/A
IFRIC 7	Applying the Restatement Approach under IAS 29 – Financial reporting in hyperinflationary economies	Not significant
IFRIC 8	Scope of IFRS 2	N/A
IFRIC 9	Reassessment of embedded derivatives	The Group expects to apply these changes from 1 January 2007

IV. Significant issues

IV.1 Non-recurring costs

The Group classifies costs incurred for design activities, prototype development and customisation to the technical and operating specifications of clearly identified of potential customers – if financed by Law 808/1985, which governs state interventions to promote the competitiveness of companies operating in the Aeronautics and Defence industries – are classified separately by the Group among intangible assets. These costs are presented net of incentives received or to be received under Law 808/1985 for programmes qualifying as important for national security or similar purposes. For these programmes, the Law 808/1985 incentives are recognised as a decrease in capitalised costs, while the royalties due to the distributing agency are recognised in the accounts upon verification of satisfaction of the requirements of the applicable law (sale of products incorporating technology eligible for legal subsidies).
As to “other programmes”, non-recurring costs are recognised under the item “Non-recurring costs”, while financing received is recognised among “other liabilities” at the nominal value, with a distinction being made between the current and non-current portions based on the expected date of repayment. In both cases, non-recurring costs are suspended between intangible assets and amortisation on the basis of units manufactured in relation to those expected to be produced. These costs are subject to impairment tests performed at least annually until development is completed, and thereafter if the outlook of the obtaining of contracts changes due to the absence of or delay in expected orders. The test is performed on the basis of the project sale plans, generally over 5 years, in consideration of the especially long life-cycle of the products being developed.

IV.2 Financing for GIE-ATR aircraft

In order to enhance its competitive position, in certain cases GIE-ATR facilitates access to financing by its customers by providing specific guarantees to third parties (an approach taken by its direct competitors), an activity that in the past was also conducted through special purpose entities.
Where, due to the effect of the guarantees provided or the content of other contractual provisions, it is felt that substantially all risks and benefits attaching to aircraft sale contracts have not transferred to customers, the sale is not recognised as such in the accounts. Rather, the entire operation is recognised as a lease, postponing the recognition of profits until such time as the risks no longer obtain by way of recognition under deferred income and carrying the aircraft among the Group’s assets, undergoing normal depreciation. If, however, the operation is structured in a manner in which substantially all risks and benefits are transferred to the customer, it is booked as a loan or a finance lease, with the sale being recognised upon delivery and the financial component being recognised under financial income on an accruals basis. If contracts envisage a buy-back clause or a residual value guarantee, the operation is recognised as a sale only if the present value of the guarantees can be considered immaterial with respect to the overall value of the transaction; otherwise, the aircraft is carried under the Group’s assets and depreciated. All likely risks associated with operations carried out by GIE-ATR are measured on the basis of a prudent valuation conducted by management and are either deducted directly from the carrying value of the asset or are recognised under provisions for risks and charges.

IV.3 Hedging long-term contracts against foreign exchange risk

In order to hedge exposure to changes in flows of receipts and payments associated with long-term construction contracts denominated in currencies other than the functional currency, the Group enters into specific hedges for the expected individual cash flows in respect of the contracts. The hedges are entered into at the moment the commercial contracts are finalised, except where the award of the contracts is felt to be highly likely as a result of existing framework contracts. Exchange-rate risk is normally hedged with plain vanilla instruments (forward contracts); in some cases, however, in order to protect the Group against the persistent adverse trend in the US dollar, we have entered into more highly structured operations that, while substantively hedging the positions, do not qualify for hedge accounting under IAS 39. In these cases, as in all cases where hedges prove to be ineffective, changes in the fair value of such instruments are taken immediately to the income statement as financial items, while the underlying is valued as if it were exposed to exchange rate variations. The effects of this recognition policy are reported in Note 38. Hedges in the former case are carried as cash flow hedges, considering as ineffective the part relating to the premium or discount in the case of forwards or the time value in the case of options, which is recognised under financial items.

IV.4 Recognition of the equity investment in STMicroelectronics N.V. (STM)

The equity investment indirectly held in STM was designated as available for sale. Accordingly, the carrying value is adjusted at each balance-sheet or interim balance-sheet date to market value (bid price), recognising the differential with respect to the carrying value determined in accordance with previous GAAP, as well as subsequent changes in fair value, in a specific equity reserve (“reserve for assets available for sale”), which will be reversed to profit or loss only if and when the equity investment is sold.
The effects of this recognition policy are reported in Note 13.

IV.5 Provisions for risks and estimates of final costs of long-term contracts

The Group operates in sectors and with contractual arrangements that are especially complex. They are recognised on a percentage-of-completion basis. Margins recognised in the income statement are a function of both the state of progress on contracts and the margins that are expected to be recognised for the completed contract. Accordingly, correct recognition of work in progress and margins on contracts that have not yet been completed requires management to make a careful estimate of the final costs and expected increases as well as delays, extra costs and penalties that could reduce the expected margin. In order to enhance support for this activity, the Group has adopted contract management and risk analysis tools designed to identify, monitor and quantify the risks associated with such contracts.

The amounts posted in the financial statements and in the interim reports represent management's best estimate at the reporting date using said procedures.
In addition, the Group's operations regard sectors and markets where many disputes are settled only after a considerable period of time, especially in cases where the customer is a government entity, making it necessary for management to estimate the outcome of such disputes. The main potential loss situations classified as 'probable' or 'possible' (no provision is recognised for the latter) are reported in Note 25.

IV.6 Disclosure on employee severance pay (Finance Act of 2007 and enabling acts)

Starting from 1 January 2007, the Finance Act and the related enabling acts introduced changes concerning the rules governing employee severance pay, including giving the employee the choice of electing where the benefit will accrue. Specifically, the employee may direct new funds allocated as severance pay towards pre-selected pension schemes or may elect that the funds remain with the company (in this case, the company will make severance pay contributions into a treasury account set up with INPS, the national social security institute). Currently, given the uncertainty as to the interpretation of the recently-issued rules, the different possible interpretations of the qualification of the accruing severance pay in accordance with IAS 19, the consequent changes in the actuarial calculations relating to accrued severance pay, as well as the impossibility of estimating choices of employees as to the destination of the accruing fund (for which the individual employee has time until 30 June), making any assumption about changes to the actuarial calculation of severance pay accrued at 31 December 2006 would be premature.

V. Significant non recurring events or transactions

As illustrated in the Report on Operations, significant events relate, especially:

- to finalising the project for listing **Ansaldo STS S.p.A.** on the Italian Stock Exchange. Ansaldo STS S.p.A. is the head of a Group which includes system and railway signalling in the Transportation segment. On 24 March 2006 52.17% (52,174,000 shares) of the company's share capital was placed with institutional and retail investors, and the price was set at €7.80 per share. 29 March 2006 was the first listing day. In the following days, the banks guiding the placing consortium exercised the greenshoe option to purchase 7,826,000 shares (7.83% of the share capital) at a price of €7.80 per share, bringing total shares placed to 60%. The shares are listed in the STAR segment of Borsa Italiana's automated stock exchange.
Placing 52.17% of the share capital of Ansaldo STS at a price of €7.80 each brought total revenue of €mil. 398 less commissions. The sale of an additional 7.83% of the share capital in April brought net revenue of €mil. 60. The overall gain was €mil. 404 excluding taxes. Below is a summary of the transaction:

€millions	
Revenue from IPO	458
Gain	416
Tax expense	(12)

At present the company is consolidated on a line-by-line basis and 60% of net income and equity is attributable to minority interests;
- the sale of the AvioGroup S.p.A. On 6 August 2006 Finmeccanica signed agreements to resize its stake in **AvioGroup S.p.A.** (formerly Aero Invest 1 S.p.A.), which is the holding company of the Avio Group including Avio S.p.A., a company operating in the development and production of large engines and important aeronautics and space components.
Under the agreements, finalised on 14 December 2006, Finmeccanica sold, together with Carlyle (which holds about 70%), its roughly 30% of AvioGroup to the British Cinven investment funds for a gross sum of around €mil. 432.
Aeromeccanica S.A. (which, at 31 December 2006, was named Telespazio Luxembourg S.A.), a subsidiary of Finmeccanica, simultaneously bought back a 15% stake in the Avio Group for about €mil. 130. The difference between the amount received upon the sale and that reinvested in the Avio Group contributed, excluding transaction costs, to the improvement in the Group's net financial position. The new shareholders' agreements between Aeromeccanica S.A. and Cinven regarding the management of the Avio Group provide for the same corporate governance rights and shareholder relations as before between Finmeccanica and Carlyle.

€millions	
Revenue	302
Gain	291
Tax expense	(11)

Finmeccanica also purchased from Avio S.p.A. for about €mil. 6 an option to acquire the company's Space division.

VI. Effects of changes in the accounting standards adopted

VI.1 Non-recurring costs

Non-recurring costs were, up until 31 December 2005, classified by the Group among inventories, in part to take into account the fact that these costs are generally eligible for the incentives envisaged under Law 808/85 (regarding the implementation of interventions for the development and competitiveness growth of companies in the Aeronautics and Defence industries). In 2006, the regulations implementing Law 808/85 underwent profound changes. Specifically, within the scope of programmes eligible for intervention under Law 808/85, special rules were carved out for those involving national security. For these programmes, the obligations on the part of the entities receiving the incentives of the interventions translate into royalties to be paid to the distributing agency based on sales made. Similar treatment is expected for programmes of European interest. Generally, the obligation to repay the amount without interest stands for the other programmes.
As a result of these changes to the law and especially the specific methods for performing the obligations of the entities receiving the incentives of the interventions associated with each category of programmes, the payables pursuant to Law 808/85 recognised in the Group's financial statements at 31 December 2005 were reallocated in the balance sheet. Payables for "civil" programmes were classified among other current and non-current liabilities, based on the assumed date of repayment, while interventions relating to national security programmes or those of European interest were taken against the correlating non-recurring costs, recognised among intangible assets.
In order to permit an easier comparison of the balance sheets presented, the effects of these different methods of accounting presentation are summarised on the next page.

Effects of changes in the accounting standards adopted

	31 December 2005	Effects of 2006 regulatory changes	31 December 2005 after 2006 changes
Intangible assets	3,596	770	4,366
Property, plant and equipment	2,506	(39)	2,467
Other non-current assets	1,569	332	1,901
Total non-current assets	7,671	1,063	8,734
Inventories	5,511	(2,736)	2,775
Other current assets	8,575	-	8,575
Total current assets	14,086	(2,736)	11,350
Non-current assets held for sale	120	-	120
Total assets	**21,877**	**(1,673)**	**20,204**
Shareholders' equity	4,598	-	4,598
Payables pursuant to Law 808/85	-	650	650
Other non-current liabilities	3,993	384	4,377
Total non-current liabilities	3,993	1,034	5,027
Payables pursuant to Law 808/85	2,767	(2,767)	-
Other current liabilities	10,427	60	10,487
Total current liabilities	13,194	(2,707)	10,487
Liabilities directly linked with assets held for sale	92	-	92
Total liabilities	**17,279**	**(1,673)**	**15,606**
Total liabilities and shareholders' equity	**21,877**	**(1,673)**	**20,204**

The primary changes were:
- the reclassification of non-recurring costs among intangible assets, due to the overall redefinition of the accounting treatment of these items and in adherence with the practices developed following the introduction of the IFRSs;
- the reclassification of payables pursuant to Law 808/85 recognised in the financial statements of the Group at 31 December 2005. Payables for "civil" programmes were classified among other current or non-current liabilities, based on the assumed date of repayment, while interventions relating to national security programmes were taken against the correlating non-recurring costs, recognised among intangible assets. In the event where interventions exceeded capitalised costs, the difference was classified among other liabilities;
- the recognition of non-current receivables from the Ministry of Economic Development with regard to the current value of interventions pursuant to Law 808/85 relating to national security projects where receipt of payment is deferred;
- the recognition of payments for royalties relating to sales already made but not yet paid to the distributing agency;
- the increase in non-current assets and liabilities. In the past, these items where entirely classified within working capital.

In order to provide a better comparison of the income statement and the statement of cash flows for 2006, it should be noted that:
- the capitalisation of non-recurring costs were recognised in the 2006 income statement as a reduction of costs. In the past, this value was treated as a separate component of revenue, within the value of production;
- the cash flows relating to these expenses were recognised among investments in the 2006 statement of cash flows. In the past, these figures where treated as "change in other operating assets and liabilities", within the cash flow generated by operating assets.

VI.2 Participation of the MBDA joint venture in the BAE Systems pension funds

The British employees of the MBDA joint venture, consolidated proportionally at 25% by the Group, participate in pension plans in the UK, in which the primary employer is BAE Systems Plc.
Under IAS 19, these funds are treated as "pension plans in which more than one employer participates". Although under the shareholders' agreement, MBDA's contribution to the fund is capped through 2007, with any difference to be made up by BAE, IAS 19 provides that any plan deficit is to be allocated evenly among companies that participate in the plan even if not in the capacity of sponsor. Starting from 1 January 2005, as a result of the transition to IFRS, BAE revealed a deficit in its plans calculated under IAS 19. However, the information provided was not deemed sufficient by the Group to permit it to properly allocate a share of the deficit to its assets held in MBDA and, as a result, the participation in the fund was accounted for using the rules provided for defined-contribution plans by recognising the contribution paid in the income statement without any recognition of the actuarial deficit attributable to the fund. In 2006, greater information concerning the methods for determining the total deficit and possible allocations to individual entities that participate in the plan was obtained. Therefore, the Group estimated its share of the deficit for MBDA at €mil. 75. The change in the accounting presentation method of the participation of MBDA in BAE's pension fund was recognised in accordance with IAS 8 ("Accounting policies, changes in estimates and errors"), with a contra-item in initial shareholders' equity at 1 January 2006.
With regard to this liability, tax advances of €mil. 22, with a net decrease in shareholders' equity of €mil. 53, were recognised.

VII. Segment information

Primary frame of reference

The Group operates in a variety of industry segments: Helicopters, Defence Electronics, Aeronautics, Space, Defence Systems, Energy, Transportation and Other activities.

For a more detailed analysis of the main programmes, outlooks and operating indicators for each segment, see the Report on Operations. The results for each segment at 31 December 2006, as compared with those of the same period of the previous year, are as follows:

	31 December 2006									
	Helicopters	Defence Electronics	Aeronautics	Space	Defence Systems	Energy	Transport-ation	Other activities	Eliminations	Total
Revenue from external customers	2,697	3,175	1,066	758	961	976	1,350	196	-	11,179
Revenue from other segments	30	572	842	6	166	2	18	33	(376)	1,293
Operating result	290	300	203	44	91	63	15	(128)	-	878
Financial income and expense - net										399
Share of result of associates	1		(4)		(2)					(5)
Tax expense										(243)
Profit (Loss) from discontinued operations										(9)
Profit (Loss) for the period										1,020
Group share of net result										988
Minority share										32
Investments	89	150	554	16	51	15	22	17	-	914

	31 December 2005									
	Helicopters	Defence Electronics	Aeronautics	Space	Defence Systems	Energy	Transport-ation	Other activities	Eliminations	Total
Revenue from external customers	2,403	2,522	1,316	726	996	761	1,226	151	-	10,101
Revenue from other segments	10	642	473	9	147	3	-	24	(457)	851
Operating result	272	269	166	26	112	39	(48)	(101)	-	735
Financial income and expense - net										(124)
Share of result of associates	-	1	(3)	(1)	(1)	-	-	(21)	-	(25)
Tax expense										(200)
Profit (Loss) from discontinued operations										(10)
Profit (Loss) for the period										396
Group share of net result										373
Minority share										23
Investments	142	1,020	165	41	45	14	26	12	-	1,465

The assets and liabilities attributable to the segments at 31 December 2006 and 31 December 2005 are as follows:

	31 December 2006									
	Helicopters	Defence Electronics	Aeronautics	Space	Defence Systems	Energy	Transport-ation	Other activities	Eliminations	Total
Assets	5,142	6,398	4,551	1,090	2,289	1,108	1,837	4,303	(3,447)	23,271
Liabilities	3,086	3,732	4,257	639	1,666	1,056	1,729	5,572	(3,796)	17,941

	31 December 2005									
	Helicopters	Defence Electronics	Aeronautics	Space	Defence Systems	Energy	Transport-ation	Other activities	Eliminations	Total
Assets	5,283	5,394	4,510	967	2,093	941	1,920	3.798	(3,149)	21,757
Liabilities	3,383	3,392	4,281	594	1,430	909	1,845	4,667	(3,314)	17,187

Secondary frame of reference

Group revenue can also be broken down geographically as follows (based on the customer's home country):

	31 December 2006	31 December 2005
Europe	9,241	8,514
North America	1,408	943
Other	1,823	1,495
	12,472	**10,952**

Assets are geographically distributed as follows:

	31 December 2006	31 December 2005
Europe	22,819	21,167
North America	351	539
Other	101	51
	23,271	**21,757**

Capital expenditure is distributed as follows (based on the location in which it is made):

	31 December 2006	31 December 2005
Europe	893	1,454
North America	18	9
Other	3	2
	914	**1,465**

VIII. Intangible assets

	Goodwill	Development costs	Non-recurring costs	Patents & similar rights	Concessions, licences and trademarks	Other	Total
1 January 2005							
Cost	2,424	54		82	128	291	2,979
Depreciation, amortisation and impairment	(361)	(44)		(63)	(110)	(176)	(754)
Carrying amount	**2,063**	**10**	**-**	**19**	**18**	**115**	**2,225**
Investments (*)	952	4		6	104	40	1,106
Sales	(1)	-		(2)	-	(1)	(4)
Depreciation and amortisation	-	(8)		(8)	(15)	(29)	(60)
Increases for business combinations	287	17		1	7	2	314
Other changes	21	1		(7)	(1)	1	15
31 December 2005 broken down as follows							
Cost	3,516	84		63	187	311	4,161
Depreciation, amortisation and impairment	(194)	(60)		(54)	(74)	(183)	(565)
Carrying amount	**3,322**	**24**	**-**	**9**	**113**	**128**	**3,596**
Adjustments (**)	(358)	174	596	-	-	578	990
Investments	-	118	156	4	21	49	348
Depreciation and amortisation		(34)	(59)	(5)	(19)	(55)	(172)
Increases for business combinations	156	2	-	-	-	29	187
Other changes	358	-	-	(1)	1	10	368
31 December 2006 broken down as follows:	3,478	284	693	7	116	739	5,317
Cost	3,672	385	826	65	209	970	6,127
Depreciation, amortisation and impairment	(194)	(101)	(133)	(58)	(93)	(231)	(810)
Carrying amount	**3,478**	**284**	**693**	**7**	**116**	**739**	**5,317**
(*) of which capitalisation of internal construction costs	-	2	-	-	-	12	14
(**) of which capitalisation of internal construction costs	-	118	441	1	2	16	578

Goodwill rose by €mil. 156, due to:

- the recognition of the relevant goodwill deriving from the possible exercise of the put and call options over 25% of the Selex Sensors and Airborne Systems Group, now held by BAE Systems (€mil. 326). Based on these agreements, the companies involved have been fully consolidated on a line-by-line basis and minority interests have not been calculated, provided that the legal portion held by the Finmeccanica Group amounts to 75%, and GBPmil. 269 (€mil. 401 at the exchange rate prevailing at 31 December 2006, see Note 24) has been recorded as a financial liability at 31 December 2006. The put option can be exercised by BAE Systems during a fixed time period (from May 2007 through August 2007), and the call option can be currently exercised by Finmeccanica. The aforesaid amount is contractually subject to price adjustments upon the occurrence of certain events. The Group has begun the process of early exercise of the call option;
- the operation to purchase shares held by minority shareholders in Datamat S.p.A. (€mil. 64), Tecnosis S.p.A. (€mil. 2) and GAF AG (€mil. 1), discussed at greater length in Note 12;
- the acquisition by the MBDA joint venture of the remaining 81.25% of the LFK Group (€mil. 43) (Note 12);
- the acquisition (Note 12) of 100% of Thomassen Turbine Systems B.V. (€mil. 4) and 55% of Energy Service Group Ltd (€mil. 1) in the Energy segment, and the reclassification of the share of goodwill in this company relating to the share previously held (€mil. 2);
- the establishing of the price adjustment provided for in the articles of incorporation of the joint venture in the Space segment (€mil. 41);
- the completion of the purchase price allocation process for the operations described in Note 12, which led to a decrease in goodwill of €mil. 360 and recognition of other intangible assets (€mil. 578) and deferred tax liabilities (€mil. 218) (Note 40);
- exchange differences amounting to €mil. 31, entirely due to assets held in the United Kingdom.

The recognised amount of goodwill is allocated to the individual cash-generating units (CGUs) concerned, which generally coincide with the Group's individual legal entities as per Group practice.

A summary of goodwill by segment is as follows:

	31 December 2006	31 December 2005
Helicopters	1,314	1,435
Defence Electronics	1,368	1,180
Aeronautics	60	60
Space	315	276
Defence Systems	376	333
Energy	7	-
Transportation	38	38
Other activities	-	-
	3,478	**3,322**

Goodwill is subject to impairment tests to determine any losses in value. This is done by individual CGU by comparing the carrying amount with the greater of the value in use of the CGU and amount recoverable by sale. In particular, the value in use is measured by discounting the cash flows of the three-year plans approved by management and projected beyond the explicit time horizon covered by the plan using growth rates of no greater than those forecast for the market in which the given CGU operates. The WACCs used fell within the 9.1% to 9.8% range.
"Development costs" and "non-recurring costs" (€mil. 977 at 31 December 2006) increased due to the reclassification (€mil. 174 and €mil. 596, respectively) of costs previously classified by the

Group among inventories (Note 16). The highest values related to aeronautics (€mil. 526) and helicopter (€mil. 164) programmes and the Defence Electronics segment (€mil. 192).

"Concessions, licences and trademarks" include €mil. 77 in expenses related to the acquisition made by the BAAC joint venture amounting to US$mil. 95 for all of the production and marketing rights for the AW139 helicopter.

"Other" include €mil. 590 of the residual value of the intangible assets identified in the course of corporate aggregation operations, in accordance with IFRS 3. Of this, €mil. 128 related to internally-developed technological knowledge and software, €mil. 46 to trademarks, €mil. 403 to activities related to the backlog of acquired companies, and their commercial positioning and to acquired programs, and €mil. 13 to licenses.

IX. Property, plant and equipment

	Land and buildings	Plant and machinery	Equipment	Other	Total
1 January 2005					
Cost	1,341	1,233	715	1,074	4,363
Depreciation, amortisation and impairment	(287)	(842)	(439)	(495)	(2,063)
Carrying amount	**1,054**	**391**	**276**	**579**	**2,300**
Investments (*)	61	117	78	103	359
Sales	(2)	(1)	(3)	(3)	(9)
Depreciation and amortisation	(47)	(108)	(61)	(73)	(289)
Increases for business combinations	25	100	20	42	187
Other changes	(46)	(27)	4	27	(42)
31 December 2005 broken down as follows:					
Cost	1,410	1,492	851	1,225	4,978
Depreciation, amortisation and impairment	(365)	(1,020)	(537)	(550)	(2,472)
Carrying amount	**1,045**	**472**	**314**	**675**	**2,506**
Investments (**)	56	87	73	350	566
Sales	(36)	(4)	(1)	(19)	(60)
Depreciation and amortisation	(45)	(112)	(71)	(82)	(310)
Increases for business combinations	5	1	-	5	11
Other changes	(6)	9	(1)	(55)	(53)
31 December 2006 broken down as follows:	1,019	453	314	874	2,660
Cost	1,426	1,549	897	1,466	5,338
Depreciation, amortisation and impairment	(407)	(1,096)	(583)	(592)	(2,678)
Carrying amount	**1,019**	**453**	**314**	**874**	**2,660**
(*) of which capitalisation of internal construction costs	-	17	12	12	41
(**) of which capitalisation of internal construction costs	-	-	10	103	113

Property, plant and equipment includes assets held under finance leases of €mil. 31 (€mil. 45 at 31 December 2005), which is composed of land and buildings of €mil. 25 (€mil. 35 at 31 December 2005) and plant, machinery, equipment and other assets of €mil. 6 (€mil. 10 at 31 December 2005).

"Other non-current assets" include a total of €mil. 16 (€mil. 28 at 31 December 2005) for helicopters owned by the AgustaWestland Group and a total of €mil. 214 (€mil. 271 at 31 December 2005) for aircraft owned by the GIE-ATR Group, as well as for aircraft that did not meet the requirements, in terms of the substantial transfer of the risks of ownership (see Note 4.2), to recognize the sale, despite the fact that sales contracts have been concluded with external customers.
The item also includes the value of assets under construction totalling €mil. 507 (€mil. 223 at 31 December 2005).

The most significant investments amounted to €mil. 346 for Aeronautics (mainly for the start-up of the B787 programme), €mil. 78 for the Defence Electronics segment, €mil. 62 for Helicopters and €mil. 25 for Defence Systems.

X. Investment properties

Investment properties, amounting to €mil. 2 (€mil. 2 at 31 December 2005), entirely regarded land and buildings.

XI. Equity investments

	31 December 2006	31 December 2005
Opening balance	138	197
Acquisitions/subscriptions and capital increases	44	21
Revaluations/impairment	6	(25)
Dividends received	(3)	(1)
Sales	(37)	(10)
Other changes	(8)	(44)
Closing balance	**140**	**138**

Increases specifically included the increase in the share capital of Oto Melara North America Inc. (€mil. 4) in the Defence segment, the incorporation of Metro C S.p.A. (€mil. 21) and Metro 5 S.p.A. (€mil. 8) in the Transportation segment, the formation of the Libyan Italian Advanced Technology Company joint venture (€mil. 2) in the Helicopters segment and the increase in the share capital of Finmeccanica Inc. (€mil. 3) in the Other activities segment.

Revaluations regarded Elettronica S.p.A. (€mil. 3), Vitrociset S.p.A. (€mil. 2), Roxel S.A.S. (€mil. 2), Eurofighter Jagdflugzeug GmbH (€mil. 2) and Eurosysnav S.A.S. (€mil. 1). Impairment regarded mainly Oto Melara North America Inc. (€mil. 4). Dividends received specifically regarded Elettronica S.p.A. and Eurosysnav S.A.S.

List of unconsolidated equity investments at 31 December 2006 (millions of euros)

	Ownership %	€mil.	Assets currency/mil.	Liabilities currency/mil.	Currency
Orizzonte-Sistemi Navali S.p.A.	49%	10	242	221	
Elettronica S.p.A. (*)	31.333%	11	758	730	
Metro 5 S.p.A. (..)	31.9%	8	14	8	
Icarus S.C.p.A.	49%	5	23	12	
Europea Microfusioni Aerospaziali S.p.A. (*)	49%	5	37	28	
Eurofighter Jagdflugzeug GmbH (*)	21%	4	1,338	1,321	
Eurosysnav S.A.S. (*)	50%	4	311	304	
Finmeccanica Inc.	100%	3	5	1	USD
Consorzio Cris (*)	81%	2	11	9	
Jiangxi Changhe Agusta Helicopters Co. Ltd	40%	2	n.a.	n.a.	
Musinet Engineering S.p.A. (*)	49%	2	8	4	
Libyan Italian Advanced Technology Company (...)	50%	2	n.av.	n.av.	
Metro C S.p.A.	14%	21			
Indra Espacio S.A.	16.17%	6			
Vitrociset S.p.A.	10%	6			
Roxel S.A.S.	12.5%	5			
Innovazione e Progetti S.C.p.A.	15%	5			
Panavia Aircraft GmbH	15%	3			
Digitalglobe Inc.	2.078%	3			
Ferromovil 9000 S.L.	10%	2			
Sofresa S.A.	2.995%	2			
Cesi-Centro Elettrotecnico Sperimentale Italiano G. Motta S.p.A.	9.36%	2			
Investments in companies and consortiums with value lower than €mil. 2		27			
Total equity investments		**140**			

(..) incorporated on 5 June 2006
(...) incorporated on 18 May 2006
(*) financial statements 2005
n.av.: not available
n.a.: not applicable

XII. Business combinations

The following summarises the business combinations that took place in previous financial years. With regard to 2006, Group net cash outlays totalled €mil. 181 (€mil. 769 in 2005) of which €mil. 116 related to transactions with minority shareholders on companies already consolidated.

LFK

On 1 March 2006 the MBDA joint venture, owned by the Group at 25% and consolidated using the proportionate method, acquired the remaining 81.25% of the LFK Group, the main manufacturer of missile systems in Germany.
The fair value attributed to the assets and liabilities acquired (pertaining to Finmeccanica) is as follows:

	Value prior to acquisitions	Fair value adjustment	Value recognised upon acquisition
Cash and cash equivalents	59	-	59
Property, plant and equipment	8	1	9
Intangible assets	-	29	29
Receivables	27	-	27
Inventories and works in progress	30	-	30
Other assets	1	-	1
Pension-plan liabilities	(26)	-	(26)
Payables	(60)	(1)	(61)
Provision for risks	(37)	-	(37)
Deferred taxes	-	(5)	(5)
Net assets acquired	2	24	26
Negative third party interests	1		1
Net assets belonging to the Group	3		27
81.25% acquired	**2**		**22**
Price paid	64		64
Acquisition costs	1		1
Total cost of acquisition	**65**		**65**
Goodwill resulting from the acquisition	63		43
Cash acquired			59
Net cash outlay			6

Thomassen Turbine Systems and Energy Service Group

In 2006, Ansaldo Energia S.p.A. acquired 100% of Thomassen Turbine Systems (TTS) a Dutch company specialising in services for gas turbines, for €mil. 12, and the remaining 55% of the Swiss firm Energy Service Group (ESG) which provides on-site plant maintenance and repairs, for €mil. 2.
The fair value attributed to the assets and liabilities acquired is as follows:

	TTS	ESG
Cash and cash equivalents	1	1
Property, plant and equipment	2	-
Intangible assets	2	-
Other non-current assets	5	-
Receivables	4	2
Inventories and work in progress	7	-
Payables	(11)	(1)
Provision for risks	(2)	-
Deferred taxes	-	-
Net assets acquired	8	2
Share acquired	100%	55%
Share of net assets acquired	**8**	**1**
Price paid	12	2
Acquisition costs	-	-
Total cost of acquisition	**12**	**2**
Goodwill resulting from the acquisition	4	1
Cash acquired	1	1
Net cash outlay	11	1

Alcatel adjustment

In September 2006, Finmeccanica paid €mil. 47 to Alcatel as the price adjustment contractually agreed upon formation of the joint ventures in the Space segment.

Transactions with minority shareholders

In 2006, the Group entered into significant transactions with minority shareholders. In this regard, it should be noted that IFRS 3 applies solely to transactions that involve the acquisition of control by the acquiring entity over the assets of the acquired company. Therefore, acquisitions of additional shares after control has already been achieved are not specifically governed by the IFRSs. Under the current doctrine, these transactions may be recognised as equity transactions (with the difference between the acquisition cost and the carrying value of the minority stakes acquired being directly attributed to the Group's shareholders' equity) or, in accordance with the standard of the parent company (which treats minority shareholders as third parties), allocating the difference between the acquisition cost and the carrying value of the minority stakes acquired to goodwill.

Consistent with its approach to the sale of shares that do not lead to the loss of control (Ansaldo STS IPO), the Group treats such transactions using the "parent company approach", which presently complies with the current version of IAS 27, recognising the difference as goodwill.
The details of these transactions are as follows:

- Datamat. In 2005, Finmeccanica, as a result of exceeding the 30% statutory threshold provided by Legislative Decree 58/1998, launched a mandatory public offering on the 12,284,840 ordinary Datamat S.p.A. shares for a unit price of €9.65 per share. At the conclusion of the mandatory public offering, the Group acquired, as of 4 January 2006, an additional 9,178,274 ordinary shares, for a total value of €mil. 89. The Group later acquired further shares on the open market, thus exceeding the 90% necessary to launch the residual offering, at a price per share set by CONSOB (the Italian Securities Regulator) of €9.911 per share. In the end, the Group's total stake came to 98.6% for a total additional outlay of €mil. 20. Following this process, the Datamat S.p.A. shares were withdrawn from the MTAX market effective as from 9 January 2007. Finmeccanica now plans to exercise the right to purchase the remaining Datamat shares in a squeeze-out operation pursuant to Article 111 of the Finance Act;
- Tecnosis. At the beginning of 2006, the Group, through Elsag S.p.A. purchased a minority stake (30%) in Tecnosis S.p.A. for €mil. 2;
- GAF. On 21 December 2006 Telespazio S.p.A. (a joint venture in which the Group holds 67% and which is consolidated proportionally) purchased the remaining 24.92% of the German company GAF AG for €mil. 3.

The total effects of these acquisitions on the performance and financial position of the Group are as follows:

	Datamat	Tecnosis	GAF (67%)	Total
Cash paid	109	2	2	113
Acquisition costs	3	-	-	3
Cash outlays	112	2	2	116
Third party assets acquired	48	-	1	49
Goodwill resulting from acquisition	**64**	**2**	**1**	**67**

Transactions related to financial year 2005

In 2005, the following transactions were completed:

- Eurosystems. On 29 April 2005, the final agreement was signed with BAE Systems Plc (BAE) for the overall reorganisation of Group activities in the Defence Electronics segment. As a result of this transaction:
  - Finmeccanica has acquired a 75% interest in the new company Selex Sensors and Airborne Systems S.p.A. (Selex S&AS) (the remaining 25% is owned by BAE Systems), to which it transferred its entire stake in Galileo Avionica S.p.A. Selex Sensors and Airborne Systems S.p.A., in turn, acquired the entire capital in the new company BAE Avionics Ltd (now Selex Sensors and Airborne Systems Ltd, or SS&AS), which received the BAE businesses specified in the agreement. The agreements also call for a call option in favour of Finmeccanica and a put option exercisable by BAE upon expiration (24 months) on the remaining 25%. The impact of these options on the Group's balance sheet and income statement are described in Notes 8 and 24;
  - Finmeccanica acquired the BAE businesses in the field of military communications (or "comms");
  - the Italian operations transferred by the Group in 1998 to the joint venture with BAE AMS N.V. have once again become wholly owned by the Group, while the UK component is once again under the full control of BAE. The new scope of Selex Sistemi Integrati S.p.A. (formerly AMS S.p.A.) has been redefined with the acquisition from BAE of its businesses in the area of Air Traffic Management and Air Traffic Control in Germany, the UK, and the US.
- Joint Ventures in the Space segment. On 1 July 2005 the alliance between Finmeccanica and Alcatel for the management of their respective activities in the Space sector was finalised. The agreements envisaged the creation of two joint ventures: Alcatel Alenia Space S.A.S. – in which Alcatel holds 67% and Finmeccanica 33% – operating in the design, development and production of space and satellite systems, and Telespazio Holding S.r.l. – owned by Finmeccanica (67%) and Alcatel (33%) – operating in the sector of services for satellite solutions. For the transaction Finmeccanica posted a net financial outlay of €mil. 109. Both joint ventures are consolidated in these financial statements using the proportionate consolidation method, according to the percentage held by the Group. Consequently, the result for 2005 includes the effects of the full consolidation of the Telespazio Group and of Alenia Spazio at 30 June 2005, and the effects of the proportionate consolidation of Alcatel

Alenia Space S.A.S. and Telespazio Holding S.r.l. (33% and 67% respectively) for the second half of 2005 and for 2006.

- Datamat. On 4 October 2005 the Group purchased 52.7% of the share capital of Datamat S.p.A., a company listed on the Electronic Stock Exchange (Techstar segment) organised and managed by Borsa Italiana and operating in the Defence Electronics business at a set price of €mil. 151.
  Therefore, the 2005 income statement includes the effects of the full consolidation of Datamat starting as of that date.

The effect of these transactions on the Group's cash and cash equivalents, net of the companies' cash at the moment they were included in the scope of consolidation, is as follows:

	Eurosystems	Space Joint Venture	Datamat	Total
Cash paid	(718)	(124)	(151)	(993)
Counterparty adjustment	190	15	-	205
	(528)	(109)	(151)	(788)
Transaction costs	(14)	-	-	(14)
Cash of acquired companies	12	5	16	33
Net effect	**(530)**	**(104)**	**(135)**	**(769)**

XIII. Financial assets at fair value

	31 December 2006		31 December 2005	
	Assets available for sale	Assets at fair value through profit or loss	Assets available for sale	Assets at fair value through profit or loss
Investment in STM	840	-	906	-
Other securities	17	-	-	-
	857	**-**	**906**	**-**

These fully relate to the indirectly-owned interest in STMicroelectronics (STM), amounting to 6.6% at 31 December 2006. Below are changes for the period in this item:

31 December 2005	906
Purchases for the year	
Sales for the year	
Fair value adjustment at 31 December 2006	(66)
31 December 2006	840

The decrease for the year was offset by a specific equity reserve named "reserve for assets available for sale" (€mil. 372 at 31 December 2006 net of the translation reserve which was negative in the amount of €mil. 14 relating to prior years).

The strategy for hedging the STM instrument is designed to limit the negative effects of a partial depreciation of the security.
The Group likewise is exposed in the event the coverage limits are exceeded (Notes 29 and 44).

XIV. Equity transactions with related parties

In general, commercial relations with related parties are carried out at arm's length, as is settlement of the interest-bearing receivables and payables when not governed by specific contractual conditions. Below are the amounts:

Receivables at 31 December 2006	Non-current financial receivables	Other non-current receivables	Current financial receivables	Trade receivables	Other current receivables	Total
Subsidiaries						
Ansaldo Invest Denmark A/S (in liq.)			3			3
Alifana Due S.c.r.l.				3		3
Finmeccanica UK Ltd			2			2
Ansaldo Argentina S.A.				1		1
Finmeccanica Inc.			1			1
IGS S.p.A. (in liq.)			1			1
Alenia Improvement S.p.A.				1		1
Ansaldo Do Brasil Equipamentos Eletromecanicos Ltda					1	1
Ansaldo Electric Drives S.p.A.			1			1
Other companies with unit amount lower than €mil. 1				1		1
Associates						
Eurofighter Jagdflugzeug GmbH				79		79
Iveco Fiat/Oto Melara S.c.a.r.l.				58		58
NH Industries S.a.r.l.				14		14
Eurosysnav S.A.S.				11		11
Galileo Vacuum Systems S.p.A.			9	1		10
Orizzonte - Sistemi Navali S.p.A.				9		9
Macchi Hurel Dubois S.A.S.				8		8
Ansaldo Trasmissione e Distribuzione S.p.A.	5			1		6
Elettronica S.p.A.				5		5
Remington Elsag Law Enforcement Systems LLC				4		4
Euromids S.A.S.				4		4
I.M. Intermetro S.p.A.				3		3
Consorzio Start S.p.A.				2		2
Eurofighter Simulation Systems GmbH				2		2
Comlenia Sendirian Berhard				2		2

Receivables at 31 December 2006	Non-current financial receivables	Other non-current receivables	Current financial receivables	Trade receivables	Other current receivables	Total
Nicco Communications S.A.S.				1		1
Eurofighter Aircraft Management GmbH				1		1
Advanced Air Traffic Systems Sdn Bhd				1		1
Industrie Aeronautiche Rinaldo Piaggio S.p.A. (in extr. admin.)				1		1
Thomassen Service Gulf LLC				1		1
Other companies with unit amount lower than €mil. 1				2		2
Joint ventures (*)						
GIE-ATR					33	33
MBDA S.A.S.				45		45
Alcatel Alenia Space S.A.S.			2	23		25
Aviation Training International Ltd	11		1			12
Telespazio S.p.A.				1	1	2
Consortiums (**)						
Saturno				35		35
Trevi - Treno Veloce Italiano				24		24
CMS Italia				14		14
C.I.S. DEG				6		6
Filobus Vesuvio				3		3
Telaer				2		2
CREO - Centro Ricerche Elettroniche			2			2
Thamus			2			2
S3Log				2		2
SESM - Soluzioni Evolute per la Sistemistica e i Modelli			2			2
Ferroviario Vesuviano				2		2
Ferroviario S. Giorgio Volla				2		2
Contact				1		1
Sistemi Navali Selenia-Elsag				1		1
Total	**16**	**-**	**26**	**377**	**35**	**454**

Payables at 31 December 2006	Non-current financial payables	Other non-current payables	Current financial payables	Trade payables	Other current payables	Total
Subsidiaries						
Alifana Due S.c.r.l.				5		5
Oto Melara North America Inc.				1	2	3
Finmeccanica UK Ltd				2		2
Finmeccanica Inc.				1		1
Alenia Hellas S.A.				1		1
Alifana S.c.r.l.				1		1
Selex Sensors and Airborne Systems Electro Optics (overseas) Ltd				1		1
Other companies with unit amount lower than €mil. 1			1			1
Subsidiaries						
Eurofighter Jagdflugzeug GmbH			78	9		87
Eurosysnav S.A.S.			20			20
Ansaldo Trasmissione & Distribuzione S.p.A.			10		1	11
Iveco Fiat/Oto Melara S.c.a.r.l.					9	9
Metro 5 S.p.A.					6	6
Pegaso S.c.r.l.				4		4
Advanced Air Traffic Systems Sdn Bhd				3		3
Orizzonte - Sistemi Navali S.p.A.					1	1
Europea Microfusioni Aerospaziali S.p.A.			1			1
Libyan Italian Advanced Technology Company			1			1
Bell Agusta Aerospace Company LLC				1		1
Eurofighter International Ltd			1			1
Other companies with unit amount lower than €mil. 1				1		1
Joint ventures (*)						
MBDA S.A.S.			358	15		373
Telespazio S.p.A.			28			28
GIE-ATR				4		4
Alcatel Alenia Space S.A.S.				4		4
Consortiums (**)						
CMS Italia				14		14
C.I.S. DEG				3		3
S3Log				2		2
Trevi - Treno Veloce Italiano				1		1
Sistemi Navali Selenia - Elsag			1			1
RES - Raggruppamento Europeo per la Sicurezza			1			1
Telaer				1		1
Thamus				1		1
Total	**-**	**-**	**500**	**75**	**19**	**594**

Receivables at 31 December 2005	Non-current financial receivables	Other non-current receivables	Current financial receivables	Trade receivables	Other current receivables	Total
Subsidiaries						
Alifana Due S.c.r.l.				6		6
CLC S.r.l (in liq.)					3	3
Finmeccanica UK Ltd			3			3
Ansaldo Invest Denmark A/S					3	3
Ansaldo Argentina S.A.				1	1	2
IGS S.p.A. (in liq.)			2			2
Gieinter A.G.			1			1
Finmeccanica Inc.			1			1
Ansaldo Do Brasil Equipamentos Eletromecanicos Ltda					1	1
Other companies with unit amount lower than €mil. 1			2	2		4
Associates						
Eurofighter Jagdflugzeug GmbH				89		89
Bell Agusta Aerospace Company LLC				32		32
Iveco Fiat/Oto Melara S.c.r.l.				32		32
Macchi Hurel Dubois S.A.S.				17		17
Eurofighter Simulation System GmbH				4		4
Euromids S.A.S.				3		3
Eurosysnav S.A.S.				3		3
Sostar GmbH				3		3
Iniziative Industriali Milano S.r.l. (in liq.)					2	2
Nicco Communications S.A.S.				2		2
Comlenia Sendirian Berhad				2		2
Intermetro S.p.A.				2		2
Remington Elsag Law Enforcement Systems LLC				1		1
Advanced Air Traffic Systems Sdn Bhd				1		1
Other companies with unit amount lower than €mil. 1				5		5
Joint ventures (*)						
MBDA S.A.S. (Group)			1	41		42
GIE-ATR					34	34
Alcatel Alenia Space S.A.S.				19		19
Aviation Training International Ltd	12		1			13
Telespazio S.p.A.				3		3
Consortiums (**)						
Trevi - Treno Veloce Italiano				34		34
C.I.S. DEG				7		7
Thamus			3			3
CREO - Centro Ricerche Elettroniche			2			2
SESM - Soluzioni Evolute per la Sistemistica e i Modelli			2			2
Spike				2		2
Telaer				1		1
Contact				1		1
Sistemi Navali Selenia - Elsag				1		1
CMS Italia				1		1
Other companies with unit amount lower than €mil. 1				1		1
Total	**12**	**-**	**18**	**316**	**44**	**390**

Payables at 31 December 2005	Non-current financial payables	Other non-current payables	Current financial payables	Trade payables	Other current payables	Total
Subsidiaries						
Alifana Due S.c.r.l.				3		3
CLC S.r.l (in liq.)			2			2
Selex Sensors and Airborne Systems Infrared Ltd				1		1
Finmeccanica UK Ltd				1		1
Selex Sensors and Airborne Systems Electro Optics (overseas) Ltd				1		1
Oto Melara North America Inc.				1		1
Finmeccanica Inc.				1		1
Other companies with unit amount lower than €mil. 1				2		2
Associates						
Eurofighter Jagdflugzeug GmbH				11		11
Iveco Fiat/Oto Melara S.c.r.l.					7	7
Pegaso S.c.r.l.				4		4
Other companies with unit amount lower than €mil. 1			1	2		3
Joint ventures (*)						
MBDA S.A.S. (Group)			349	16		365
Telespazio S.p.A.			19		1	20
Alcatel Alenia Space S.A.S.				6		6
GIE-ATR				5		5
Consortiums (**)						
Thamus				2		2
CIC			1			1
SESM - Soluzioni Evolute per la Sistemistica e i Modelli				1		1
CMS Italia				1		1
Other companies with unit amount lower than €mil. 1				2		2
Total	-	-	**372**	**60**	**8**	**440**

(*) Amounts refer to the portion not eliminated for consolidation
(**) Consortiums over which the Group exercises considerable influence or which are subject to joint control

XV. Receivables and other non-current assets

	31 December 2006	31 December 2005
Third-party financing	1	3
Security deposits	16	15
Receivables for finance leases	20	19
Deferred receivables Law 808/85	314	-
Other	75	73
Non-current receivables	**426**	**110**
Financial accrued income - non-current	6	3
Other accrued income - non-current	1	1
Other non-current assets	2	-
Other non-current assets	**9**	**4**

"Receivables for finance leases" relate to transactions qualifying as finance leases made by GIE-ATR where the Group is the lessor: in this case, the aircraft being the subject-matter of the lease contract is removed from assets and replaced by a receivable, and the relevant financial income is recognised progressively over the term of the contract at the effective interest rate applicable to the lease contract.

The item "Deferred receivables Law 808/85" includes the receivables from the Ministry of Economic Development relating to the current value of the interventions pursuant to Law 808/85 in national security and similar projects for which collections were deferred. The portion for which collection is expected within 12 months (€mil. 38) is classified among other current assets (Note 21).

The item "Other" also includes tax receivables for the prepayment of withholdings for personal income tax (IRPEF) on the severance benefits for Italian companies (€mil. 17 compared to €mil. 25 at 31 December 2005).

XVI. Inventories

	31 December 2006	31 December 2005
Raw materials, supplies and consumables	1,543	1,297
Work in progress and semi-finished goods	800	3,527
Finished goods and merchandise	134	168
Advances to suppliers	618	519
	3,095	**5,511**

The decrease in "work in progress and semi-finished goods" is attributable, in the amount of €mil. 2,736 to the reclassification of non-recurring costs to intangible assets, which were classified among inventories up through December 2005 (Note 6.1).

XVII. Contract work in progress and advances received

	31 December 2006	31 December 2005
Contract work in progress (gross)	6,184	5,728
Advances from customers	(3,361)	(3,190)
Contract work in progress (net)	**2,823**	**2,538**
Advances from customers (gross)	12,996	11,146
Contract work in progress	(7,467)	(6,757)
Advances from customers (net)	**5,529**	**4,389**

"Contract work in progress" is recognised as an asset if the gross value of a given contract is greater than the advances received from the customer or as a liability if the advances received are greater than the related contract work in progress. In the event the advances have not been received at the balance sheet date, the corresponding value is recognised among trade receivables.

XVIII. Trade and financial receivables

	31 December 2006		31 December 2005	
	Trade	Financial	Trade	Financial
Receivables	3,659	453	3,512	444
Impairments	(180)	(1)	(228)	(2)
	3,479	**452**	**3,284**	**442**

Other trade receivables at 31 December 2006 include €mil. 10 (€mil. 39 at 31 December 2005) related to receivables sold as part of non-recourse factoring transactions that do not qualify for derecognition under IAS 39. It should be noted (see also Note 24) that these assets are not available to the Group, given that they have been transferred fully and with no possibility of repurchase by third parties.
Financial receivables from other partners of the joint ventures relate in large part (€mil. 358) to the deposit of cash and cash equivalents of the MBDA Group with the other participants in the joint venture (BAE Systems plc and EADS N.V.), acquired on a pro rata basis (25%) through the proportional consolidation of the Group.

XIX. Current financial assets at fair value

These assets are as follows:

	31 December 2006		31 December 2005	
	Assets available for sale	Assets at fair value through profit or loss	Assets available for sale	Assets at fair value through profit or loss
Bonds	9	-	10	-
Other securities	12	-	10	-
	21	**-**	**20**	**-**

Bonds mainly relate to Government securities issued by the Italian Government and maturing during 2007. Other securities relate to Group Parent liquidity being invested almost exclusively in units of a fund established under the laws of Italy.

XX. Tax receivables and payables

	31 December 2006		31 December 2005	
	Receivables	Payables	Receivables	Payables
Direct taxes	370	139	262	80
Other taxes	99	183	102	188
	469	**322**	**364**	**268**

"Tax receivables" includes receivables of the Group Parent totalling €mil. 280 (€mil. 157 at 31 December 2005) related to IRPEG/I.Re.S. (income) taxes in the amount of €mil. 151, interest on tax credits of €mil. 89, VAT credits in the amount of €mil. 24 and other receivables (IRAP, ILOR) in the amount of €mil. 16. Specifically, the tax receivables of the Group Parent increased by €mil. 106 due to the re-recognition of tax credits, which were derecognised in past years following the non-recourse sale to a bank. The bank, in recovering the credits, has raised objections which has led to a foreseeable delay in collections, as a result of which the Company and the bank involved began a process of renegotiating certain contract clauses to ascertain any non-compliance with the requirements of IAS 39 concerning derecognition. Therefore, a financial payable has been recognised in the same amount as these tax credits (Note 24).

"Tax payables" includes payables of the Group Parent totalling €mil. 17 (€mil. 41 at 31 December 2005), of which €mil. 12 relates to stamp taxes on the share capital increase and €mil. 5 for IRPEF and other taxes.

XXI. Other current assets

	31 December 2006	31 December 2005
Accrued income - current portion	80	101
Equity investments	-	-
Derivatives (Note 29)	147	59
Receivables for contributions	83	69
Receivables from employees and social security	33	32
Deferred receivables Law 808/85 (Note 15)	38	-
Other assets	213	227
	594	**488**

Other assets include receivables from the Camozzi Group of €mil. 14 (€mil. 14 at 31 December 2005), the receivable for a fixed deposit account for €mil. 40 established in favour of the Ministry of Economic Development by a Group company (€mil. zero at 31 December 2005), sundry advances of €mil. 21 (€mil. 22 at 31 December 2005) and receivables for default interest of the Group Parent for €mil. 28.

XXII. Cash and cash equivalents

	31 December 2006	31 December 2005
Cash	5	3
Bank deposits	1,998	1,058
	2,003	**1,061**

The Group does not include overdraft facilities, since it is not systematically used as a form of financing.

XXIII. Shareholders' equity

Shareholders' equity at 31 December 2006 is equal to €mil. 5,357 (€mil. 4,598 at 31 December 2005), a net increase of €mil. 759.

Share capital	Number of ordinary shares	Par value €mil.	Treasury share €mil.	Total €mil.
Outstanding shares	422,845,466	1,860	-	1,860
Treasury shares	(258,605)	-	(2)	(2)
31 December 2005	422,586,861	1,860	(2)	1,858
Shares subscribed during the period	1,748,690	8	-	8
Repurchase of treasury shares, less shares sold	(373,096)	-	(8)	(8)
31 December 2006 broken down as follows:	423,962,455	1,868	(10)	1,858
Outstanding shares	424,594,156	1,868	-	1,868
Treasury shares	(631,701)	-	(10)	(10)
	423,962,455	**1,868**	**(10)**	**1,858**

The Group Parent's share capital fully subscribed and paid-up is divided into 424,594,156 ordinary shares with a par value of €4.40 each, including 631,701 treasury shares.

During 2006 the share capital increased by €mil. 8 for the issue of 1,748,690 new shares resulting from the exercise of subscription rights as resolved by the Board of Directors as part of the stock option plan 2002-2004.
Moreover, 1,075,901 ordinary shares were purchased on the market, for a total amount of €mil. 19, in order to support the stock grant plan 2005-2007, and 60,690 options were exercised for the purchase of treasury shares of Finmeccanica from persons not related to Finmeccanica through an employment contract as part of the former stock option plan, and 642,115 shares were awarded under the stock grant plan for a total payment of €mil. 11.
As a result, treasury shares amounted to 631,701, of which 197,915 were used in the above said stock option plan and 433,786 in the stock grant plan.

At 31 December 2006, the Ministry of Finance held some 33.767% of the shares.

Retained earnings and consolidation reserve

	31 December 2006	31 December 2005
Start of period	2,173	1,902
Dividends paid	(211)	(110)
Surplus on share capital increases	17	9
Reclassified from reserve for stock-option plans	2	1
Awarding of stock grants	(4)	-
Change in accounting treatment of UK employee pension plans	(53)	-
Revaluation reserve	5	-
Other changes	16	(2)
Net profit for the period	988	373
End of period	2,933	2,173

Other reserves

	Reserve for assets available for sale	Cash flow hedge reserve	Translation reserve	Reserve for stock-option and stock-grant plans	Total
31 December 2005	438	(44)	2	17	413
Stock option/grant plans:					
- services rendered				18	18
- issue of new shares				(15)	(15)
Fair value adjustments	(66)	116			50
Recognition in the income statement		(14)			(14)
Translation differences			33		33
31 December 2006	372	58	35	20	485

Reserve for assets available for sale
This reserve includes changes in the value of the indirect investment in STMicroelectronics N.V. (Note 13), which is designated as an asset available for sale, and in the other assets included in this category.

Cash flow hedge reserve
This reserve includes the fair value of derivatives used by the Group to hedge its exposure to currency or interest rate risk net of the effect of deferred taxes until the moment in which the underlying position is recognised in the income statement. When this condition is met, the reserve is recognised in the income statement to offset the economic effects of the hedged transaction.

Translation reserve
This reserve is used to recognise the exchange rate differences resulting from the translation of the financial statements of consolidated companies. The most significant amounts were the result of the consolidation of the UK component of the AgustaWestland (€mil. 6), Selex Communications (€mil. 6), Selex S&AS Ltd (€mil. 10) and Ansaldo Signal (€mil. 2) Groups.

Reserve for stock-option and stock-grant plans
This reserve is the equity contra-item of the value of the activities performed by employees and non-employees, remunerated through the assignment of options on the shares of the Group Parent Finmeccanica S.p.A. stock as part of the previous stock option plan for 2002-2004 or through the

free assignment of shares as part of the stock grant plan 2005-2007.
With regard to the stock option plan 2002-2004, following achievement of the conditions specified in the plan, a total of 3,993,175 (79,863,500 before combining them) options have been assigned and are currently exercisable by their recipients through 31 December 2009. The strike price is set at €14 per share with a par value of the shares to be subscribed of €4.40, with the difference allocated to the share premium reserve. With the increase in the share capital authorised by the Board of Directors within the limits set by the shareholders on 16 May 2003, at 31 December 2006 a total of 2,699,665 ordinary shares have been subscribed, for an increase in capital of €mil. 12. At 31 December 2006 treasury shares used in the stock option plan amounted to 197,915, following the exercise of 60,690 call options for treasury shares from persons not related to Finmeccanica through an employment contract.
With regard to the stock grant plan, this was approved by the Board of Directors on 29 September 2005 and its beneficiaries are 574 key resources among executives, directors and self-employed workers with top-level roles in Finmeccanica S.p.A. or its subsidiaries. Under the plan, each of the beneficiaries is entitled to receive Finmeccanica S.p.A.'s ordinary shares for each of the years 2005, 2006 and 2007, on annual assignment and deferred delivery of shares, subject to the achievement of the performance goals defined internally.
The shares to be assigned following the assignment and subject to the achievement of the goals will be made available through a share capital increase resolved by the Company pursuant to Article 2349 of the Italian Civil Code or through shares already issued and included in the Group portfolio, to be purchased upon prior authorisation resolved by the Shareholders' Meeting on 1 June 2005. In 2006 1,075,901 treasury shares were purchased and used in the plan and on 1 December 2006 642,115 shares were delivered to the beneficiaries of the 2005 assignment.
The fair value of the 2006 grant shares to be assigned in 2007 was set at €15.90 per share, on the basis of the market value of the share at the date the plan structure and the key parameters were defined; the valorisation of the rights that are estimated to be assigned has increased the reserve by €mil. 18 during the period; this reserve also includes contributions of €mil. 2, for a total cost of €mil. 20 for 2006 (Note 35).

Shareholders' equity of minority interests

	31 December 2006	31 December 2005
Start of period	2,173	1,902
Dividends paid	(3)	(1)
Change in scope of consolidation and other minority shareholders	(101)	110
Share capital increases	4	1
Translation differences	(4)	(1)
Fair value adjustments	-	-
Other changes	(1)	-
Net profit for the year	32	23
End of period	81	154

The net change in the scope of consolidation is essentially due to transactions involving the Datamat Group and the Ansaldo STS Group and operations in the Defence Electronics segment which were the subject-matter of agreements made in 2005 with BAE Systems Plc.

XXIV. Borrowings

	31 December 2006			31 December 2005		
	Current	Non-current	Total	Current	Non-current	Total
Bonds	78	1,670	1,748	64	1,659	1,723
Bank borrowings	81	195	276	126	220	346
Finance leases	5	20	25	8	28	36
Payable for non-recourse factoring	116	-	116	39	-	39
Other borrowings	601	94	695	57	68	125
	881	**1,979**	**2,860**	**294**	**1,975**	**2,269**

Bonds

	31 December 2004	IAS 32 and 39	Increases	Interest	Repayments	Other changes	31 December 2005
Exchangeable bonds	501	(102)	-	18	(2)	-	415
Bonds - 1997	7	-	-	-	-	(1)	6
Bonds - 2002	297	(7)	-	11	(9)	-	292
Bonds - 2003	500	(4)	-	30	(29)	-	497
Bonds - 2005	-	-	494	19	-	-	513
	1,305	**(113)**	**494**	**78**	**(40)**	**(1)**	**1,723**

	31 December 2005	Interest	Repayments	Other changes	31 December 2006
Exchangeable bonds	415	19	(2)		432
Bonds - 1997	6	-	-		6
Bonds - 2002	292	12	(5)		299
Bonds - 2003	497	29	(29)		497
Bonds - 2005	513	25	(24)		514
	1,723	**85**	**(60)**		**1,748**

Below are the salient features of these bonds:
- Exchangeable bonds: the bond, with a total nominal value of €mil. 501, was issued by Finmeccanica Finance S.A. during financial year 2003 with a maturity date of 8 August 2010 and offers investors the option to exchange the bond for STMicroelectronics N.V. shares at a price of €25.07 per share.
With a nominal yield of 0.375% annually, the bond was measured at an effective interest rate

of 4.36%, which is the rate at which it would have been issued had it not had the exchange option. This component, separated from the value of the bond, was measured at fair value and recognised through profit and loss (see Notes 29 and 38 for more information). On 1 June 2005, the Group entered into a transaction to hedge the income volatility caused by the recognition of the embedded option by purchasing an offsetting option sold to investors with the same underlying position and the same basic parameters. The economic effects of this transaction are nil (see Note 38). For the handling of the STM shares linked to the conversion (20,000,000) see Note 13.

- Bonds - 1997: this bond, issued by Finmeccanica Finance S.A. in 1997 with a maturity date of 16 January 2007, pays an annual coupon of 3.30% and has a total nominal value of JPY 900 million (€mil 6).
- Bonds - 2002: this bond, issued by Finmeccanica Finance S.A. in 2002 with a maturity date of 30 December 2008 has a total nominal value of €mil. 297, returns a variable yield based on the Euribor rate with spread of 90 b.p.s., mitigated by a "cap & floor" mechanism.
- Bonds - 2003: this bond was issued in 2003 by Finmeccanica Finance S.A. with a maturity date of 12 December 2018 and has a total nominal value of €mil. 500. With an annual coupon of 5.75%, the effective interest rate is 5.93%.
- Bonds - 2005: this bond was issued in 2005 by Finmeccanica S.p.A. with a maturity date of 24 March 2025 and has a total nominal value of €mil. 500. With an annual coupon of 4.875%, the effective interest rate is 4.96%.

Changes for the period in borrowings are:

	31 December 2004	IAS 32 and 39	Increases (*)	Repayments (*)	Change in scope of consolidation	Other changes	31 December 2005
Convertible bonds	931	(4)	26	(953)	-	-	-
Bonds	1,305	(113)	572	(40)	-	(1)	1,723
Bank borrowings	402	-	4	(96)	31	5	346
Finance leases	36	-	1	(4)	-	3	36
Payable for non-recourse factoring	-	526	132	(619)	-	-	39
Other borrowings	193	(4)	5	(71)	5	(3)	125
	2,867	**405**	**740**	**(1,783)**	**36**	**4**	**2,269**

	31 December 2005	Increases (*)	Repayments (*)	Change in scope of consolidation	Other changes	31 December 2006
Bonds	1,723	85	(60)	-	-	1,748
Bank borrowings	346	25	(93)	-	(2)	276
Finance leases	36	-	(11)	-	-	25
Payable for non-recourse factoring	39	-	(29)	-	106	116
Other borrowings	125	593	(26)	(1)	4	695
	2,269	**703**	**(219)**	**(1)**	**108**	**2,860**

(*) Net changes for current liabilities. The items also include changes resulting from the application of the effective interest rate method, which may not correspond with actual cash movements.

Bank borrowings
This item specifically includes borrowings by the joint ventures ATIL Ltd in the Helicopters segment (€mil. 96), and GIE-ATR in the Aeronautics segment (€mil. 14), borrowings related to companies being liquidated (€mil. 2) and subsidised loans posted by Selex Sistemi Integrati S.p.A. (€mil. 58). Of the non-current portion, €mil. 107 falls due in between 2 and 5 years, and €mil. 88 falls due in more than 5 years.

Finance leases
These obligations are related to property, plant and equipment and intangible assets held by the Group under finance lease contracts. Of these, €mil. 20 has an expiration of between 2 and 5 years.

Payable for non-recourse factoring
Although some assignments of receivables carried out by the Group in prior years are both legally and substantively assignments without recourse and their terms and conditions do not envisage repurchase or reversion clauses or guarantees that could require reimbursement of the amounts received, these are not eligible for derecognition. Accordingly, the accounting policy adopted calls for the trade receivable to remain among assets (even though the Group no longer has control over the asset), with the recognition of a corresponding financial liability. On the date the assignee receives payment from the assigned debtor, the receivable and the related financial liability are eliminated from the Group's assets and liabilities. In 2006, the item increased by €mil.106 due to the re-recognition of tax credits derecognised in past periods (Note 20).

Other borrowings
This item includes:

- the liability of €mil. 67 to the Ministry for Economic Development for medium and long-term financing granted under various Italian laws;
- the value of the put and call options with BAE Systems Plc for the sale in 2007 of the remaining 25% of Selex Sensors and Airborne Systems S.p.A. to Finmeccanica for €mil. 401;
- the amount of €mil. 114 arising from financial costs for advances made by customers, that a Group company will be required to pay during the next period, recognised as financial payables considering the particular contractual context from which they arise.

Of the non-current portion, €mil. 54 falls due in between 2 and 5 years, and €mil. 39 falls due in more than 5 years.

Below is the financial information required under CONSOB communication no. DEM/6064293 of 28 July 2006:

	31 December 2006	31 December 2005
Cash	5	3
Bank deposits	1,998	1,058
Securities held for trading	21	20
Liquidity	**2,024**	**1,081**
Current financial receivables	**478**	**460**
Current bank payables	81	126
Current portion of non-current borrowings	83	72
Other current borrowings	1,217	468
Current net debt	**1,381**	**666**
Current net debt (cash)	**(1,121)**	**(875)**
Non-current bank payables	195	220
Bonds issued	1,670	1,659
Other non-current payables	114	96
Non-current net debt	**1,979**	**1,975**
Net debt	**858**	**1,100**

XXV. Provisions for risks and charges and contingent liabilities

	Guarantees given	Restructuring	Penalties	Product guarantees	Other	Total
1 January 2005						
Current	10	135	27	22	320	514
Non-current	51	75	17	146	298	587
	61	**210**	**44**	**168**	**618**	**1,101**
Allocations	5	14	9	63	91	182
Uses	(13)	(138)	(9)	(16)	(60)	(236)
Reversal	(18)	(32)	(9)	(14)	(82)	(155)
Other changes	29	23	21	(10)	(9)	54
31 December 2005	**64**	**77**	**56**	**191**	**558**	**946**
Broken down as follows:						
Current	9	53	50	101	310	523
Non-current	55	24	6	90	248	423
	64	**77**	**56**	**191**	**558**	**946**
Allocations		9	14	52	150	225
Uses	(1)	(13)	(6)	(12)	(58)	(90)
Reversal	(11)	(22)	(16)	(29)	(93)	(171)
Other changes	(13)	(13)	4	29	19	26
31 December 2006	**39**	**38**	**52**	**231**	**576**	**936**
Broken down as follows:						
Current	-	28	43	132	368	571
Non-current	39	10	9	99	208	365
	39	**38**	**52**	**231**	**576**	**936**

"Other changes" include changes in the scope of consolidation.

These specifically include:

- the "provision for guarantees given" in the amount of €mil. 39 (€mil. 64 at 31 December 2005) related to business in the Aeronautics segment, for activities with foreign partners, as well as activities related to the Space segment;
- the "provision for conversion and restructuring" in the amount of €mil. 38 (€mil. 77 at 31 December 2005), established for expected charges resulting from the programme to restructure the various segments. The most significant uses for the period involved the Helicopter, Space and Other activities segments. The amounts recorded are related to the Space, Helicopter, Energy, Defence Electronics and Other activities segments;
- the "provision for penalties" in the amount of €mil. 52 (€mil. 56 at 31 December 2005). The amounts recorded are related to the Aeronautics, Space and Defence Systems segments;
- the "provision for product guarantees", in the amount of €mil. 231 (€mil. 191 at 31 December 2005) includes allocations related to commitments for products sold. The amounts recorded are related to the Helicopter, Energy, Defence Electronics and Defence Systems segments. The increase is also due to the acquisition of LFK GmbH by MBDA S.A.S.;
- the "other provisions" total €mil. 576 (€mil. 558 at 31 December 2005) and include:
  - the provision for risks on operations of the GIE-

ATR in the amount of €mil. 68 (€mil. 100 at 31 December 2005);
- the provision for risks and contractual charges in the amount of €mil. 93 (€mil. 123 at 31 December 2005) related, in particular, to business in the Helicopter, Defence Electronics, Transportation, Defence Systems and Other Activities segments;
- the provision for bad debts of €mil. 27 (€mil. 26 at 31 December 2005) includes accruals to cover losses exceeding the carrying amounts of investees;
- the provision for taxes in the amount of €mil. 43 (€mil. 27 al 31 December 2005);
- the provision for disputes with employees and former employees in the amount of €mil. 42 (€mil. 37 at 31 December 2005);
- the provision for risks on aeronautical business related to the C27J and AMX programmes in the amount of €mil. 38 (€mil. 26 at 31 December 2005);
- the provision for pending litigation in the amount of €mil. 110 (€mil. 121 at 31 December 2005);
- the provisions for risk on contract-related losses in the amount of €mil. 49 (€mil. 32 at 31 December 2005);
- other provisions in the amount of €mil. 106 (€mil. 66 at 31 December 2005).

With regard to the risk provisions, the Finmeccanica Group's operations regard industries and markets where many disputes are settled only after a considerable period of time, especially in cases where the customer is a government entity. Of course, in application of related accounting standards, provisions have been made for any obligations related to probable and quantifiable risks. Likewise, to the best of our knowledge, regarding other disputes against the Group, no specific allocation has been made since the Group reasonably believes that such disputes may be resolved satisfactorily and without any significant impact on the results.
The situations below are mentioned here for the purposes of full disclosure.

Of particular note:
- the dispute in which Finmeccanica has been asked to cover the contractual commitments assumed upon the sale of the former subsidiary Finmilano S.p.A. to Banca di Roma (now Capitalia) originating from the assessment ordered by the Rome Office of Direct Taxes of Finmilano S.p.A. regarding the disallowance of the tax deductibility of the capital loss originating in 1987 on the sale of a non-recourse "deferred" receivable at a price below the nominal value. In essence, the Italian Tax Authority felt that this sale was actually a financing transaction and that the loss, in the same manner as a finance cost, should not have been deducted in its entirety in 1987, but should have been recognised over subsequent years as implicit interest in the transaction.
After the Court of Cassation (the supreme court of appeal) – in allowing the appeal filed by the Tax Authority – had returned the parties to the court of first instance, the latter once again upheld the Company's complaint. This ruling was once again appealed to the Court of Cassation. It should be noted that substantial charges to be paid by Finmeccanica are not currently foreseeable. In agreement with the bank, it has been deemed that there is insufficient justification to accept the settlement of pending disputes pursuant to Article 16 of Law 289/2002, partly in light of the fact that the significant financial outlay that this would have required does not make sense from a cost-benefit point of view;
- the dispute resulting from the notice to settle the registry fee of about €mil. 10, which was received by Finmeccanica in July 2001 and due on the capital increase approved in 1998. Although the tax liability had already been recognised in the related financial year, the Company felt it was unnecessary to meet the tax demand because it was unjustified both in law and in fact. In fact, in addition to being received after the statutory deadline, the notice contained a request for a tax related to a tax base that was partially inconsistent with applicable laws. The Tax Commission for the Province of Rome upheld the Company's dispute in its ruling filed in December 2002. The ruling was appealed by the Company in relation to the failure to order the Tax Authority to reimburse costs. In the first half of 2004, the Tax Authority in turn filed a cross appeal of the same ruling, but only with regard to the decision that confirmed the termination of the office's assessment power in the matter. No objection was raised, however, with regard to the substance of the original ruling establishing the partial lack of justification of the amount requested by the revenue office. In a ruling filed in October 2004, the appeal court rejected the Company's primary appeal regarding the lack of reimbursement of costs, but at the same time declared that the cross appeal filed by the Tax Authority was inadmissible in that it was filed after the ordinary statutory deadlines. In particular, the Regional Tax Commission in Rome upheld the complaint filed by the Company regarding the fact that the Tax Authority had erroneously deemed the suspension of the procedural deadlines defined by Article 16 of Law 289/02 (facilitated settlement of pending disputes) to be applicable, given that the case did not fall within the scope of this law. The sentence of the court of second instance has been appealed to the Court of Cassation by the tax authorities.
- the dispute initiated by Telespazio S.p.A against the Agenzia delle Entrate, Rome District 4 challenging a tax assessment regarding direct income taxation (IIDD) for the year 2000, which contained a demand for a total of about €mil. 30 consisting of additional taxes, penalties and interest. The notice of assessment, served on 27 November 2006, relates to a tax audit completed in 2001 in which the Tax Authority challenged the deductibility of the loss regarding receivables from a foreign company taken by Telespazio S.p.A. within the context of a non-recourse sale carried out following many fruitless attempts to recover these receivables. Specifically, the Tax Authority, deeming the actions undertaken by the Company to forcibly collect the receivables and therefore the evidence of the foreign debtor's solvency or lack thereof to be insufficient, found that the requirements of certainty and precision under the law were not met to allow the loss to be fully deducted, regardless of the fact that the loss was conclusively realised by Telespazio S.p.A. within the context of the non-recourse sale of the receivables arguing that sale *per sé* guarantees certainty only of the legal loss of the receivable but not the financial loss. The case is currently pending before tax court of first instance and no provision has been made in the financial statements since, in the Company's opinion, it can prove that the transaction was accounted for properly;
- the dispute initiated by Telespazio S.p.A against the Agenzia delle Entrate, Rome District 4 challenging a tax assessment for the purposes of direct income taxation (IIDD) and regional business taxation (IRAP) for the year 2001 containing an adjustment of about €mil. 9.7 in taxable income at the time the tax statement was prepared. Considering that the adjustment, for IIDD purposes, results in a reduction by an amount equal to the final tax loss in 2001 and that this loss was fully used by the Company in 2006, the total amount owed to the Tax Authority would be about €mil. 7 plus additional taxes, penalties and interest. The notice of assessment, served on 27 November 2006, relates to a tax audit completed in 2003 in which the Tax Authority challenged Telespazio S.p.A.'s reserving tax treatment until the completion of the Astrolink contract. Specifically, in November 2001, the customer Astrolink at its discretion terminated a long-term contract triggering Telespazio's right to compensation under the contract equal to the costs (plus 20% and in any event "be agreed" with the customer) that Telespazio would incur as a result of the early termination. Since it was not possible in 2001 to determine and agree upon the total amount of these costs (and the corresponding compensation revenues), the Company prudentially allocated €mil 48.5 in the 2001 financial statements to a provision for risks and charges, as it deemed that amount to not be tax deductible. The auditors, starting, instead, with the assumption that Telespazio could have calculated the amount of compensation due from the counterparty as early as 2001 since the costs that it would have incurred as a result of the early termination of the contract were determinable, challenged the failure to account for revenues in the amount of €mil. 58.2 and also gave full tax effect to the amount of €mil. 48.5 in the provision for risks and charges which Telespazio, instead, treated as fully taxed. As a result, the Tax Authority determined that Telespazio had €mil. 9.7 more in taxable income

in 2001 for direct income taxation and regional business taxation purposes. The case is currently pending before tax court of first instance and no provision has been made in the financial statements since, in the Company's opinion, it can prove that the transaction was accounted for properly.
Beyond the merits, it should be pointed out that it is currently impossible to estimate the substantive costs to be borne by the Finmeccanica Group considering that the liability, if it should be found to exist, would be neutralised by the guaranteed issued by Telecom Italia within the scope of the contract selling its shares of Telespazio in November 2002;

- the dispute initiated by SO.GE.PA. S.p.A. against the Agenzia delle Entrate, Rome District 4 challenging a tax assessment for the purposes of direct income taxation (IIDD) and regional business taxation (IRAP) for the year 2001 containing a demand for a total of about €mil. 18 in additional taxes, penalties and interest.
The tax claim, served on 27 December 2006, traces back to a tax audit completed in 2004 against ALS S.p.A., a Finmeccanica Group company absorbed by So.Ge.Pa. in 2006, in which the tax inspectors – without including any formal comments – merely notified the tax office responsible for the assessment of possible violations in applying the regulations concerning the tax appraisal of work in progress inventories within the context of the long-term contract for the provision and launching of the Atlantic Bird1 satellite obtained in 2000. Specifically, the warning originates from the fact the company had, over the years, accounted for these inventories based on the percentage completed (calculated using the cost-to-cost method), thereby rendering the settlement and payments received over the medium-term upon the achievement of various milestones irrelevant since they are not, under the contract, final settlements and therefore recognising as revenues (and therefore taxable) the entire amount of the inventories only when ownership of the satellite was transferred in 2002 upon acceptance in orbit of the satellite by the customer as contractually agreed. By contrast, the tax inspectors asked the competent tax office to assess whether, in reality, under the contract, the various milestones could have been treated using the Work Status (WS) process, so as to include in the tax assessment of work-in-progress inventories the payments received based on the achievement of the WS objectives, regardless of the amounts recognised in the financial statements, on the assumption that the object of the contract could be divided into individual, "autonomous" lots for which each payment represents a final settlement of payments owed.
The tax officials, receiving the auditors' report and without carrying out any further analysis of the matter although it involves a rather complex contractual relationship, issued the notice of assessment against the company. The case is currently pending before tax court of first instance and no provision has been made in the financial statements since, in the Company's opinion, it can prove that the transaction was accounted for properly;

- the appeal, together with ENEL and other parties, filed with the Regional Administrative Court of Lombardy of the resolution of the Italian Electricity and Gas Authority regarding the method of calculating interest due on amounts to be paid, as compensation, in relation to the termination of the Italian national nuclear energy programme.
The amount of interest that would result from a different calculation method amounts to roughly €mil. 13. Previous rulings by the Lombardy Regional Administrative Court do not support the resolutions of the Authority. Accordingly, it is reasonable to expect a favourable outcome for Finmeccanica;
- on 6 July 2001, Finmeccanica and its subsidiary Alenia Spazio S.p.A. (formerly ALS S.p.A., now So.Ge.Pa. S.p.A.) received notice of a summons to appear before the Texas Federal Court to respond to a request for damages resulting from the alleged violation of agreements as part of the Gorizont programme, which is related to the events of 1998-1999 when Alenia Spazio operated as a division of Finmeccanica (on 9 July 2001, Alenia Spazio alone received a second summons to appear before the court for the same issue).
Based on an examination of the case files by US lawyers, the companies feel there are valid reasons to contest the substance of the demands of the plaintiffs. The pre-trial issue of the lack of jurisdiction of the Texas Court raised by Finmeccanica and ALS in both suits was favourable to the companies at all levels of hearings. Therefore, at present, both cases before the Texas Court can be considered closed;
- arbitration is under way to settle a dispute between Consorzio Trevi – of which the subsidiary AnsaldoBreda S.p.A. is a member with a 40% stake – and Trenitalia S.p.A. in relation to the application of penalties for the late delivery of ETR 500 trains. Consorzio Trevi has contested the penalties and has requested reimbursement of the significant additional costs incurred. The arbitration board arranged for the issues involved in the arbitration to be examined by an independent expert. The expert's report was filed on 10 January 2005 and is in favour of Consorzio Trevi. However, on 19 October 2005 the arbitration board arranged, upon request of Trenitalia, for a supplementation of the expert's report; this was filed on 31 January 2006. The findings of this supplemental report do not provide clear indications on the amount attributable to Trenitalia's delays. These indications had been clearly reported in the former report. For this reason, Consorzio Trevi, confirming its own reservations concerning the lawfulness of the supplemental report, requested to submit its own considerations on this matter. On 13 March 2006 the parties filed their final pleadings. The arbitration award is expected to be filed in May 2007;
- on 1 October 2003, the European Commission notified the Ministry of Foreign Affairs of the formal proceedings initiated for an investigation of the Italian State, pursuant to Article 11 of the EC Treaty, in relation to subsidies granted by the Italian Government to the companies Alenia Aeronautica S.p.A., Alenia Aermacchi S.p.A. (formerly Aermacchi S.p.A.), and Agusta S.p.A., based on Law 808/85, for six research and development projects. The Commission considers the subsidies to be state aid. The preliminary assessment of the Commission was that these subsidies were not notified to the Commission at the time, even though they were each in excess of the ECU 20 million threshold (1 ECU being equal to €1). On 22 January 2004, the decision to open proceedings was published in the EU Official Journal.
The Italian authorities submitted their own observations to the Commission on 30 January 2004.
In response to requests of third parties, the Commission requested further information from the Italian Government, which was provided in the latter part of May 2004. Further exchanges of requests and information between the Commission and the Italian Government continued in the second half of the year. With its letter of 22 June 2005 C(2005)1813, received by the Permanent Representation of Italy in the EU on 24 June, the European Commission informed the Italian Government of its decision to extend the scope of the current proceedings to an additional six projects of the aforementioned companies that had initially been excluded by the Commission itself. The Italian authorities submitted their reply to the Commission on 29 November 2005. On 19 December 2005 the Commission served on the Italian Government further considerations filed by an anonymous third party, and the Government replied accordingly on 24 February 2006. At the moment, this procedure deeply affects the application principles of Law 808/85.
Finmeccanica will follow the issue with special attention with the assistance of local counsel. At present, further information is being exchanged between the Italian Government and the Commission before the latter issues its final decision, which is expected in September 2007.
- in November 1997 in relation to a contract commissioned by Prepa, the Puerto Rican Electric Power Authority, the company Abengoa awarded to Ansaldo Energia a sub-supplier contract for expansion work on the San Juan, Puerto Rico power plant.
In connection with the contract between Abengoa and Prepa, American International Insurance Company of Puerto Rico (AIIP), a member of the AIG Group, issued a performance bond and a payment bond, each in the amount of US$mil. 125, in favour of Prepa which Ansaldo Energia, as a supplier, counter-guaranteed for US$mil. 36 each.
In 2000, Abengoa unilaterally terminated its

contract without informing Ansaldo Energia and filed suit against the customer in the Court of Puerto Rico seeking compensation for damages it allegedly suffered.
In 2001, Ansaldo Energia initiated arbitration proceedings in Paris seeking a finding that Abengoa breached the contract by terminating its agreement with Prepa without notifying Ansaldo Energia in advance. The arbitration finding, issued in March 2003, came out in favour of Ansaldo Energia.
In order to avoid any enforcement of the aforementioned guarantees, on 13 May 2005, Ansaldo Energia brought an action against Abengoa, AIG and AIP before the Court of Milan, requesting that its counter-guarantees be found void, or, in the alternative, that it be held harmless by Abengoa. AIIP asked that Ansaldo Energia be held jointly liable to hold harmless AIG in the event it loses the case.
In the opinion of its legal team, even if the court does not accept Ansaldo Energia's arguments and, if the counter-guarantees are enforceable, the company could, in any case, initiate an action against Abengoa, a company that is absolutely solvent, even based on the aforementioned arbitration award.

XXVI. Severance pay and other employee liabilities

	31 December 2006	31 December 2005
Severance obligations	778	778
Defined-benefit retirement plans	341	318
Share of joint venture pension obligation	75	-
Other employee obligations	44	18
	1,238	**1,114**

The statutory severance pay obligation is specific to Italy and calls for the payment of the entitlement accumulated by employees until the time they leave the company. This provision is calculated in accordance with Article 2120 of the Italian Civil Code by dividing the fixed components of an employee's compensation by 13.5.
With the defined-benefit plans, the Group assumes the obligation to ensure a specific retirement benefit level for employees participating in the plan, guaranteeing to make good any negative difference between value of plan assets and the agreed-upon benefit level.
Other employee obligations mainly relate to provisions of the MBDA joint venture (€mil. 37). The increase for the period (€mil. 26) primarily relates to the inclusion in the scope of consolidation of the defined-benefit plans of the LFK Group, which was acquired by the joint venture on 1 March 2006.

Liabilities relating to defined-benefit retirement plans include the share of the total defined-benefit retirement plans managed by BAE Plc (Note 6.2) allocable to the MBDA joint venture.

A detail of the defined-benefit retirement plans is as follows:

	31 December 2006	31 December 2005
GBP area	304	282
Euro area	37	36
	341	**318**

A breakdown of severance obligations and defined-benefit plans is as follows:

	Severance obligations		Defined-benefit plans	
	31 December 2006	31 December 2005	31 December 2006	31 December 2005
Present value of the obligations	846	851	1,126	1,025
Fair value of the plan's assets	-	-	(796)	(641)
Unrecognised actuarial gain (loss)	(68)	(73)	11	(66)
Carrying amount of the obligation	778	778	341	318

Unrecognised net actuarial gains mainly relate, with regard to defined-benefit plans, to the AgustaWestland Group (€mil. 7) and the Alcatel Alenia Space joint venture (€mil. 7), and are partly offset by the unrecognised actuarial losses of Selex Sensors and Airborne Systems Ltd (€mil. 3).

The considerable decrease in unrecognised actuarial losses on both types of defined-benefit plans is due to the considerable rise in rates used in calculating pension differences and to the increase in expected returns on the plan's assets.

Below are movements in defined-benefit plans:

	31 December 2006			
	Present value of the obligation	Present value of the asset	Unrecognised actuarial gain (loss)	Net liability defined-benefit plans
Opening balance	1,025	641	66	318
Costs of benefits paid	78	-	-	78
Interest expense	50	-	-	50
Expected return on plan assets	-	46	-	(46)
Actuarial losses (gains)	(54)	23	(77)	-
Decreases for sales	-	-	-	-
Increases from business combinations	-	-	-	-
Contributions paid	-	66	-	(66)
Contributions from other plan participants	20	20	-	-
Exchange rate differences	21	15	-	6
Benefits paid	(20)	(19)	-	(1)
Other changes	6	4	-	2
Closing balance	1,126	796	(11)	341

	31 December 2005			
	Present value of the obligation	Present value of the asset	Unrecognised actuarial gain (loss)	Net liability defined-benefit plans
Opening balance	709	474	22	213
Costs of benefits paid	51	-	-	51
Interest expense	42	-	-	42
Expected return on plan assets	-	35	-	(35)
Actuarial losses (gains)	117	73	44	-
Decreases for sales	-	-	-	-
Increases from business combinations	83	-	-	83
Contributions paid	-	55	-	(55)
Contributions from other plan participants	16	16	-	-
Exchange rate differences	19	13	-	6
Benefits paid	(22)	(22)	-	-
Other changes	10	(3)	-	13
Closing balance	1,025	641	66	318

Changes in severance obligations are shown below:

	31 December 2006			
	Present value of the obligation	Present value of the asset	Unrecognised actuarial loss	Net liability defined-benefit plans
Opening balance	851	-	73	778
Costs of benefits paid	64	-	-	64
Interest expense	25	-	-	25
Actuarial losses (gains)	(6)	-	(5)	(1)
Decreases for sales	(7)	-	-	(7)
Increases from business combinations	-	-	-	-
Benefits paid	(82)	-	-	(82)
Other changes	1	-	-	1
Closing balance	846	-	68	778

	31 December 2005			
	Present value of the obligation	Present value of the asset	Unrecognised actuarial loss	Net liability defined-benefit plans
Opening balance	806	-	55	751
Costs of benefits paid	66	-	-	66
Interest expense	21	-	-	21
Actuarial losses (gains)	19	-	18	1
Decreases for sales	(89)	-	-	(89)
Increases from business combinations	110	-	-	110
Benefits paid	(76)	-	-	(76)
Other changes	(6)	-	-	(6)
Closing balance	851	-	73	778

The amounts recognised in the income statement were calculated as follows:

	31 December 2006		31 December 2005	
	Severance obligations	Defined-benefit plans	Severance obligations	Defined-benefit plans
Costs of benefits paid	64	78	66	51
Interest expense	25	50	21	42
Expected return on plan assets	-	(46)	-	(35)
Actuarial gain (loss) recognised during the period	(1)	-	1	-
Total cost	**88**	**82**	**88**	**58**

No actuarial losses were recognised in the income statement in relation with defined-benefit plans, in compliance with the corridor approach, as the actuarial deficit is lower than such threshold.

The main actuarial assumptions are as follows:

	Severance obligations		Defined-benefit plans	
	31 December 2006	31 December 2005	31 December 2006	31 December 2005
Discount rate (annual)	3.40-4.10%	3.00-3.60%	4.50-5.20%	4.70-4.80%
Expected return on plan assets	-	-	4.50-8.0%	4.50-7.50%
Rate of salary increase	1.30-4.30%	2.00-5.20%	3.30-4.15%	3.90-4.00%
Rate of turnover	1.00-5.75%	0.90-4.50%	-	-

Assets of defined-benefit plans include:

	31 December 2006	31 December 2005
Shares	500	455
Real properties	116	92
Bonds	66	62
Cash or equivalents	6	6
Other	108	26
	796	**641**

Below is statistical information regarding the excess (deficit) of plans:

	31 December 2006		31 December 2005		31 December 2004	
	Severance obligations	Defined-benefit plans	Severance obligations	Defined-benefit plans	Severance obligations	Defined-benefit plans
Present value of obligations	846	1,126	851	1,025	806	709
Fair value of the plan's assets	-	(796)	-	(641)	-	(474)
Plan excess (deficit)	**846**	**330**	**851**	**384**	**806**	**235**

XXVII. Other current and non-current liabilities

	Non-current		Current	
	31 December 2006	31 December 2005	31 December 2006	31 December 2005
Employee obligations	54	49	337	299
Deferred income	207	178	100	93
Social security payable	6	6	201	182
Payable to Min. of Econ. Dev. Law 808/1985	564	-	58	2,767
Payable to Min. of Econ. Dev. for monopoly rights Law 808/1985	46	-	15	-
Other payables Law 808/1985	356	-	-	-
Derivatives (Note 29)	-	-	104	121
Other payables	99	147	489	447
	1,332	**380**	**1,304**	**3,909**

The payables to the Ministry of Economic Development (MED) include the payables for royalties accrued pursuant to Law 808/1985 for "national security" and similar projects, in addition to payables for disbursement received from the MED supporting development of non-national security and similar programmes eligible for the incentives under Law 808/85 (€mil. 622 at 31 December 2006). The payables are reimbursed on the basis of a scheduled repayment plan, without the incurrment of financial expense. These disbursements are included among other non-financial payables, by the virtue of their precise nature, especially considering the risk-sharing characteristics and correlation with development programmes which distinguish them.

The item "Other liabilities Law 808/1985" includes the difference between the interventions received or to be received pursuant to Law 808/1985, relating to programmes qualifying as "national security and similar", with regard to the share of the subsidised costs classified among non-recurring costs, as well as the differential between the monopoly rights charged for the above programmes and the effective payable accrued based on the established reimbursement ratio (Note 6.1). The amount is reduced as a result of the reclassifications described in Note 6.1.

Specifically, other payables include:

- the amount of €mil. 61 (of which €mil. 53 is carried as a non-current liability) due to Bell Helicopters due to the "BAAC reorganisation", which involved the acquisition of 100% of the construction and marketing rights for the helicopter AW139, previously owned by Bell Helicopter at 25%;
- the amount of €mil. 33 due to EADS N.V. from GIE-ATR (consortium owned by Alenia Aeronautica S.p.A. and EADS N.V.);
- the amount of €mil. 41 in respect of contractual penalties;
- the amount of €mil. 36 due to repurchase of a G222 aircraft;
- commissions due in the amount of €mil. 38;
- royalties due in the amount of €mil. 24.

XXVIII. Trade payables

Trade payables rose slightly, due to the increase in production volumes, from €mil. 3,371 at 31 December 2005 to €mil. 3,486 at 31 December 2006.

XXIX. Derivatives

The table below provides a detail of the asset and liability positions related to derivative instruments. The portion of changes recognised in the income statement is shown in Note 38.

	31 December 2006		31 December 2005	
	Assets	Liabilities	Assets	Liabilities
Forward forex instruments	115	69	25	69
Forex options	1	-	-	1
Interest rate swap	7	21	-	18
Options on STM	13	-	1	-
Exchangeable bond option	11	11	33	33
Other equity derivatives	-	3	-	-
	147	**104**	**59**	**121**

Forward forex instruments

The notional value of the forward transactions totalled €mil. 2,772 of which €mil. 1,986 is related to contracts to sell and €mil. 786 to contracts to buy, primarily US dollars.
The Group hedges its own contracts for purchases or sales denominated in a currency different from the functional currency using forward contracts of amounts, maturities, and key parameters that are similar to the underlying position. Under Group procedures, derivative instruments are purchased with the intent to hedge certain or highly probably commitments and, as such, are designated as hedging instruments at the time of purchase. The effectiveness of the hedge is tested at least at each interim or year-end reporting date using mathematical and statistical methods. In the event that, due to its nature or following such tests, a

derivative instrument held should be found to no longer be an effective hedge, the fair value of the instrument is immediately recognised through profit or loss. In the event the designation of the instrument as a hedge should continue to be supported by the tests of actual and future effectiveness, the cash-flow hedge accounting method of recognition is adopted (see Note 4.3). The positive change in the fair value of forward instruments is due to the considerable depreciation of the US dollar against the euro: the exchange rate increased from 1.1797 at 31 December 2005 to 1.3170 at 31 December 2006.

Interest rate swaps

At 31 December 2006, the Group held interest rate swaps totalling €mil. 830. A detail of the main instruments is as follows:

Description	Notional	Underlying position	
Fixed/floating/fixed swap	€mil. 500	Bonds - 2003	(a)
Fixed/floating/fixed swap	€mil. 200	Bonds - 2005	(b)
Floating/fixed swap	€mil. 130	Bonds - 2002	(c)
Interest rate options	€mil. 200	Bonds - 2005	(b)

(a) The transaction was carried out to benefit from low short-term interest rates without, however, exposing the Group to the risk of any subsequent increases. As such, the exposure was converted to a floating rate through 19 December 2005 and back to fixed (5.80% average) after that date.
The transaction was measured at fair value through profit or loss, thereby generating no economic effect during the period. At 31 December 2006, the fair value of the instrument was a negative €mil. 11.

(b) The transaction was carried out during 2005 in order to earn short-term benefits from low interest rates. The instruments purchased also include a number of interest rate options that enable the Group to protect a portion of the debt portfolio exposed to floating rates and to switch to floating for additional portions of the debt.
The transaction was measured at fair value through profit or loss, thereby generating a loss of €mil. 2. The fair value of these instruments was positive at 31 December 2006 in the amount of €mil. 5.

(c) The transaction makes it possible to limit exposure to future changes in the reference interest rate (6-month Euribor) and has been recognised as a cash-flow hedge. At 31 December 2006, the fair value of the instrument was €mil. 1.

This item also includes other minor transactions with a total negative fair value of €mil. 5 and a floating/fixed interest rate swap carried out by the helicopter-related joint venture ATIL, the fair value of which was a negative €mil. 4 at 31 December 2006, and recognised as a cash-flow hedge.
The transactions recognised as cash-flow hedges have resulted in a negative reserve at 31 December 2006 in the amount of €mil. 3 (€mil. 11 at 31 December 2005), whereas those that have been recognised at fair value through profit or loss have produced financial expense totalling €mil. 4.

Forex options

At 31 December 2006 forex options are held in the notional amount of €mil. 156, carried out by the Group Parent on behalf of its subsidiaries. Given their nature and the particularly restrictive requirements of IAS 39, these instruments do not qualify for hedge accounting. From 31 December 2004 to now almost all of these transactions have been closed. The fair value of the instruments included in the portfolio is positive in the amount of €mil. 1. During the period income of €mil. 2 and expense amounting to nil were recorded.

Options on STM

This item includes transactions to hedge a portion of the remaining portfolio of STM securities, which were valued at fair value through profit or loss. The changes during the period were as follows:

1 January 2006	New operations	Completed operations	Fair value delta	31 December 2006
1	4	(1)	9	13

Specifically, during 2006, transactions were made on an additional 15,000,000 shares for premiums paid of €mil. 4 which extend the hedge to 45,000,000 STM shares at 31 December 2006. During the period, on premiums paid of €mil. 4, income from the completion of hedging operations arose in the amount of €mil. 8. The fair value of such instruments is positive in the amount of €mil. 13 at 31 December 2006 (€mil. 1 at 31 December 2005), generating an income for the period of €mil. 9 including the €mil. 4 in premiums paid. The strategy for hedging the STM instrument is designed to limit the negative effects of a partial depreciation of the security. The Group likewise is exposed in the event the coverage limits are exceeded (Note 44).

Exchangeable bond options

This item includes the liability related to the call option embedded in the exchangeable bonds (Note 24). On 1 June 2005, the Group purchased a call option with the same key parameters in order to hedge future changes in the value of the option sold.

Other equity derivatives

Following the stock exchange placement of 60% of the shares of Ansaldo STS, Finmeccanica undertook the obligation to deliver, without compensation, shares to subscribers who held shares through 28 March 2007 (Notes 5 and 44). The fair value of this obligation at 31 December 2006 is valued at cost and amounts to € mil. 3.

XXX. Guarantees and other commitments

Leasing

The Group is party to a number of operating leases as both lessor and lessee primarily for the purposes of acquiring the use of plant and equipment. Below are the non-cancellable minimum future payments and collections relating to operating lease contracts:

	Operating leases - payable	Finance leases - receivable
Within 1 year	135	86
2 to 5 years	226	165
Beyond 5 years	70	38
	431	**289**

The amount of the purchase and sale commitments includes those relating to the satellite capacity business conducted by the Telespazio joint venture, as well as those relating to GIE-ATR's airplane leasing and sub-leasing operations. Specifically, the amount of the commitments to purchase satellite capacity came to about €mil. 215 (€mil. 263 at 31 December 2005) and is substantially covered by the customer orders backlog. The corresponding sales commitments amounted to €mil. 217 (€mil. 260 at 31 December 2005).

Guarantees

At 31 December 2006, the Group had the following outstanding guarantees:

	31 December 2006	31 December 2005
Guarantees in favour of Group companies	9,056	8,313
Guarantees in favour of third parties	3,914	3,939
Endorsements in favour of third parties	-	18
Other unsecured guarantees given to third parties	583	1,337
Unsecured guarantees given	**13,553**	**13,607**

At 31 December 2006 the amount of secured guarantees given for the obligations of others totalled €mil. 820 (€mil. 29 at 31 December 2005).

XXXI. Transactions with related parties

The following describes all transactions with related parties for 2006 and 2005.

31 December 2006	Revenues	Other operating revenues	Costs	Financial income	Financial expense
Subsidiaries					
Alifana Due S.c.r.l.			23		
Finmeccanica UK Ltd			6		
Finmeccanica Inc.			3		
Oto Melara North America Inc.			1		
Associates					
Eurofighter Jagdflugzeug GmbH	764				
Iveco Fiat Oto Melara S.c.r.l.	149		3		7
Eurosysnav S.A.S.	51				
N.H. Industries S.a.r.l.	26				
Macchi Hurel Dubois S.A.S.	25	1			
Euromids S.A.S.	11				
Orizzonte Sistemi Navali S.p.A.	14		2		
Eurofighter Simulation Systems GmbH	13				
Nicco Communications S.A.S.	6				
Elettronica S.p.A.	6		1		
Pegaso S.c.r.l.			7		
Automation Integrated Solutions S.p.A.			2		
Nahuelsat S.A.		2			
Ansaldo Trasmissione e Distribuzione S.p.A.	2				
Selex Sistemi Integrati De Venezuela S.A.	2				
Sostar GmbH	1				
Advanced Air Traffic Systems Sdn Bhd	1		3		
Consorzio START S.p.A.	2				
Sistemi Dinamici S.p.A.			1		
I.M Intermetro S.p.A.		2			
Eurofighter Aircraft Management GmbH	1				
Comlenia Sendirian Berhad	1				
Alenia Hellas S.A.			1		
Other companies with unit amount lower than €mil. 1	3	1		2	
Joint ventures (*)					
MBDA S.A.S.	84				8
GIE-ATR	54				
Alcatel Alenia Space S.A.S.	23		7		
Telespazio S.p.A.	3		1		1
Aviation Training International Ltd	1			1	
Consortiums (**)					
CMS Italia	14		36		
Trevi - Treno Veloce Italiano	21		2		
C.I.S. DEG	10		16		
Contact	2				
Consorzio Ferroviario San Giorgio Volla 2	2				
SESM - Soluzioni Evolute per la Sistemistica e i Modelli			1		
Filobus Vesuvio	1				
Saturno		1	2		
Total	**1,293**	**7**	**118**	**3**	**16**

31 December 2005	Revenues	Other operating revenues	Costs	Financial income	Financial expense
Subsidiaries					
Finmeccanica Inc.			2		
Oto Melara North America Inc.			1		
Other companies with unit amount lower than €mil. 1			1		
Associates					
Eurofighter Jagdflugzeug GmbH	446		4		
Iveco Fiat Oto Melara S.c.a.r.l.	100		3		6
Eurosysnav S.A.S.	60				
Eurofighter Simulation Systems GmbH	18				
Euromids S.A.S.	13				
Nicco Communications S.A.S.	9				
N.H. Industries S.a.r.l.	5				
Orizzonte Sistemi Navali S.p.A.		3	3		
Sostar GmbH	2				
Elettronica S.p.A.	1				
LMATTS LLC	1				
Remington Elsag Law Enforcement Systems LLC	1				
Comlenia Sendirian Berhad	1				
Consorzio START S.p.A.	1				
Other companies with unit amount lower than €mil. 1	7		4	2	
Joint ventures (*)					
MBDA S.A.S.	145		8		7
GIE-ATR	26				
Alcatel Alenia Space S.A.S.	11		8		
Alenia Marconi Systems S.p.A.	2	2	15		
Telespazio S.p.A.	2				
Dataspazio S.p.A.			2		
Other companies with unit amount lower than €mil. 1				1	
Total	**851**	**5**	**51**	**3**	**13**

(*) Amounts refer to the portion not eliminated for consolidation.
(**) Consortiums over which the Group exercises considerable influence or which are subject to joint control.

XXXII. Revenue

	2006	2005
Revenue from sales	7,879	7,934
Revenue from services	2,364	2,019
	10,243	9,953
Change in contract work in progress	936	148
Total revenue	**11,179**	**10,101**

The trends in revenue by business segment are described in the notes above.

XXXIII. Other operating income (costs)

	2006		2005	
	Income	Costs	Income	Costs
Grants for research and development costs	32	-	18	-
Other subsidies	11	-	13	-
Gains on the sale of intangible assets and property, plant and equipment	34	-	31	-
Accruals to/Reversals of provisions for risks and charges	138	162	155	155
Reversal of impairment of receivables	13	-	15	-
Exchange rate difference on operating items	88	70	102	112
Adjustment of receivables and liabilities in a foreign currency at the end-of-period exchange rate	33	28	34	22
Insurance reimbursements	12	-	23	-
Reorganisation costs	12	17	-	15
Indirect taxes	-	47	-	26
Other operating income (costs)	114	109	97	184
	487	**433**	**488**	**514**

"Gains on the sale of intangible assets and property, plant and equipment" refer primarily to the sale of buildings by Selex Communications Ltd (€mil. 21) and other Group companies.

"Other income" includes the interest income on commercial transactions in the amount of €mil. 31 (€mil. 3 in 2005) and extraordinary items relating to receivables, previously written down, from insolvent countries for €mil. 13 (€mil. 2 in 2005).

Accruals to "provisions for risks and charges" of €mil. 138 (€mil. 155 in 2005), mainly regard the following provisions: product guarantees for €mil. 29 (€mil. 14 in 2005), guarantees given for €mil. 11 (€mil. 18 in 2005), penalties for €mil. 16 (€mil. 9 in 2005) and other provisions for €mil. 82 (€mil. 114 in 2005). In other provisions, the accruals primarily related to the GIE-ATR fund for €mil. 32 (€mil. 0 in 2005) and the C27J and AMX programmes in the Aeronautics segment, for €mil. 11 (€mil. 14 in 2005). Overall, the accruals related to the Aeronautics, Space, Helicopters, Defence Electronics, Defence Systems and Other activities segments.

"Reversals of provisions for risks and charges" of €mil. 162 (€mil. 155 in 2005), regard: disputes with third parties for €mil. 10 (€mil. 21 in 2005), product guarantees for €mil. 52 (€mil. 63 in

2005), penalties for €mil. 14 (€mil. 9 in 2005) and other provisions for €mil. 86 (€mil. 62 in 2005). The largest reversals involved the Aeronautics, Helicopters and Defence Electronics segments.

Specifically, "other operating costs" include contractual penalties of €mil. 32 (€mil. 53 in 2005), losses on disposals of €mil. 3 (€mil. 4 in 2005) and interest expense on commercial transactions of €mil. 22 (€mil. 7 in 2005).

XXXIV. Costs of goods and services

	2006	2005
Purchase of materials from third parties	4,998	4,367
Change in inventories	(210)	(234)
Total cost of goods	**4,788**	**4,133**
Services rendered by third parties	3,307	2,941
Costs of acquiring satellite capacity	70	93
Costs of airplane leases	12	15
Costs of rents and operating leases	124	111
Rental fees	30	17
Total cost of services	**3,543**	**3,177**

The "costs of acquiring satellite capacity" relate to satellite capacity trading business conducted by the Telespazio joint venture with a counter-item in revenues from sales. The costs of leasing airplanes relate to leasing and sub-leasing transactions entered into by GIE-ATR.
The amount for the purchase commitments undertaken to that regard through Telespazio and GIE-ATR are described in Note 30.

XXXV. Personnel costs

	2006	2005
Wages and salaries	2,456	2,201
Cost of PSP (Note 23)	20	16
Cost of LTIP	6	3
Social security contributions	637	602
Severance pay costs (Note 26)	90	88
Costs related to other defined-benefit plans (Note 26)	82	58
Costs related to defined-benefit plans	35	29
Employee disputes	10	6
Reorganisation costs	5	17
Other costs	50	22
	3,391	**3,042**

The average workforce at 31 December 2006 numbered 56,653, as compared with 52,844 in 2005. The increase is essentially due to the change in the scope of consolidation, especially the acquisition of LFK Group by MBDA and, in the Energy segment, the Dutch company Thomassen Turbine Systems B.V. and the Swiss company Energy Service Group Ltd, as well as positive turnover in certain segments. The greatest increase, in part due to the use of new types of contracts, occurred in the Aeronautics segment as a result of the development of new programmes.
Significant growth was also achieved in the Helicopters and Transportation segments.
The total workforce increased from 56,603 in 2005 to 58,059 at 31 December 2006.

Personnel costs rose from €mil. 3,042 in 2005 to €mil. 3,391 in 2006. The increase is mainly due to the change in the scope of consolidation, the expansion in incentive plans and compensation dynamics and, specifically for foreign companies, also due to social security liabilities payable by enterprises in connection with the pension benefits due legally and contractually, especially to employees in the UK.
"Cost of PSP" relates to the stock-grant plan 2005-2007 (Note 23).

XXXVI. Depreciation, amortisation and impairment

	2006	2005
Depreciation and amortisation:		
· intangible assets	172	59
· property, plant and equipment	310	288
	482	347
Impairment		
· operating receivables	23	16
· other assets	-	2
	23	18
Total depreciation, amortisation and impairment	**505**	**365**

XXXVII. Capitalisation of internal construction costs

	2006	2005
Personnel costs	312	16
Materials	121	10
Other costs	281	29
	714	**55**

The increase in the item is attributable to the different method for recognising "non-recurring costs" (Note 6.1) compared with 2005. Inclusion of these costs among intangible assets is recognised as capitalisation of costs (in the item "Increases in capitalisation of internal construction costs") and no longer as a separate component of revenue (in the item "Change in work in progress, semi-finished goods and finished products", which decreased by a corresponding amount from a positive change of €mil. 517 in 2005 to a negative change of €mil. 24 in 2006).

XXXVIII. Financial income and expense

	2006			2005		
	Income	Expense	Net	Income	Expense	Net
Income from Ansaldo STS IPO	416	-	416	-	-	-
Capital gain from sale of AvioGroup S.p.A.	291	-	291	-	-	-
Dividends	3	-	3	1	-	1
STM dividends and capital gains from the sale of STM shares	5	-	5	17	-	17
Gains on investments and securities	7	-	7	6	-	6
Discounting of receivables, liabilities and provisions	3	(2)	1	2	(3)	(1)
Interest income/expense (*)	75	(269)	(194)	119	(216)	(97)
Commission income/expense (including commissions on non-recourse items)	-	(31)	(31)	-	(18)	(18)
Fair value adjustments through profit or loss	47	(54)	(7)	44	(39)	5
Premiums paid/received on forwards	5	(27)	(22)	9	(13)	(4)
Exchange rate differences	322	(340)	(18)	201	(215)	(14)
Value adjustments of equity investments	3	(22)	(19)	3	(6)	(3)
Other financial income and charges	14	(34)	(20)	30	(36)	(6)
	1,191	**(779)**	**412**	**432**	**(546)**	**(114)**

(*) Of which financial expenses arising from the application of the effective (not liquidated) interest rate on bonds for €mil. 25 (€mil. 38 in 2005).

In 2006, financial income and expense, which came to a positive €mil. 412 for the period (negative by €mil. 114 in 2005) was strongly affected by the capital gain arising from the stock exchange placement of Ansaldo STS Group (€mil. 416) and the sale of AvioGroup for €mil. 291 (Note 5).
During the year, “dividends” totalling €mil. 8 (€mil. 6 in 2005) were received from associated and other companies, mainly relating to the investments in STM (€mil. 5) and Vitrociset S.p.A. (€mil. 2).
“Gains on investments and securities” includes capital gains arising from the sale of Elsag STI and Elsag Gest for €mil. 6.
In addition to the €mil 114 relating to interests on advances made to AnsaldoBreda that will be paid during the next period, the item “Interest income/expense” includes results of the Group’s financial management, including premiums received/paid on interest rate hedges (interest rate swap). The net item shows a slight improvement over the previous year. Despite the increase in interest rates, the Group’s debt structure, which is primarily fixed rate, made neutralisation of the negative impact of the rate effect possible.
Commissions relate primarily to transactions for the sale of receivables. The total amount of these sales transactions for the period was around €mil. 1,000, of which about €mil. 800 in the month of December.

Net income from measurement of fair value through profit or loss is as follows:

	2006			2005		
	Income	Expense	Net	Income	Expense	Net
Swaps and forex options	2	-	2	21	(19)	2
Interest rate swaps (Note 29)	3	(7)	(4)	-	(3)	(3)
Options on STM (Note 29)	9	-	9	-	(12)	(12)
Ineffective portion of hedging swap	10	(21)	(11)	2	(5)	(3)
Option embedded in the exchangeable bond (Note 24)	23	(23)	-	21	-	21
Other equity derivatives	-	(3)	(3)	-	-	-
	47	**(54)**	**(7)**	**44**	**(39)**	**5**

Net expense on swaps and forex options include changes in the fair value of the components that have been excluded from the hedging contracts on efficient instruments (swap and forward premium or discount points and time value on options of €mil. 11), and the effects of derivative instruments which, although they meet the objective of limiting the fluctuations of the underlying position within a specific range, do not meet the particularly restrictive conditions of IAS 39, either because of the nature of the instruments themselves or the inability to mathematically demonstrate their effectiveness.
Income from options on STM stems from the decrease in the value of the underlying position. During the period, additional options were made in respect of 15 million STM shares, bringing the total of shares with options to 45 million. The Group also has an offsetting call option on STM shares with the same underlying and same key parameters as that embedded in the exchangeable bonds issued in 2002. As a result of this transaction, the Group is in an essentially neutral position with regard to further variations in the fair value of the call option sold (income of €mil. 23 from the call option sold and expense of €mil. 23 for the call option acquired).
The income statement 2005 included the difference in fair value from the date of first-time application of IAS 39 and that of the purchase of the call option (€mil. 21). In 2005 other financial income included (€mil. 18) the positive effects of the closure of previous transactions in options to hedge the investment in STM.

In 2006, “premiums on forwards” were paid in the amount of €mil. 27 (€mil. 13 in 2005), and premiums received amount to €mil. 5 (€mil. 9 in 2005). The increase in net expense relating to premiums paid is due to the higher differences between the euro and US dollar interest rates, as more fully described in the Note on “Financial risk management”.
The effect of “exchange rate differences”, negative for €mil. 18 (€mil. 14 in 2005) was essentially due to the realignment with the current exchange rates of the foreign currency current accounts held by the GIE-ATR consortium (of which the subsidiary Alenia Aeronautica is a participant) with regard to the other shareholders, not subject to exchange rate risk hedging up to now due to its special nature which does not allow for the signing of IAS compliant operations. The risk of fluctuation in the future foreign exchange rate, however, will be partially mitigated starting in 2007 with the signing of forward contracts specifically for that purpose.

“Value adjustments of equity investments” primarily includes the writedown of Ansaldo Trasmissione e Distribuzione amounting to €mil. 12 and of Nahuelsat for €mil. 8.

“Other financial income and charges” includes income generated by the closing of hedging operations for €mil. 8, charges related to the purchase of the call option on Avio for €mil. 7, the effect of the purchase price adjustment connected with the joint venture with Alcatel for €mil. 6, and charges on contracts for the sale of the receivables completed during the previous years that do not fall under the scope of IAS 39 for €mil. 10.

XXXIX. Effect of recognition using the equity method

	2006	2005
Recognition of AvioGroup S.p.A.	-	(26)
Net recognition of other investees	(5)	1
	(5)	**(25)**

XL. Income taxes

Income tax expense can be broken down as follows:

	2006	2005
Corporate income tax (IRES)	232	131
Regional business tax (IRAP)	126	105
Benefit under consolidated tax mechanism	(151)	(129)
Other income taxes	89	77
Tax related to previous periods	(4)	-
Provisions for tax disputes	14	9
Deferred tax (net)	(63)	7
	243	**200**

Income from adopting the consolidated taxation mechanism from 1 January 2004 was considered in the calculation of IRES (corporate income tax), which was introduced by Legislative Decree 344/2003. According to this mechanism, there is only one taxable income for all the Group companies included in the scope of consolidation. This option makes it possible to offset the tax results (taxable income and losses in the consolidation period) of the participating companies. As a result, the income statement includes the benefit resulting from the tax losses for the period up to the limit of the taxable income included in the consolidated tax base. This income was then allocated to all the consolidated companies reporting a fiscal loss.

With regard to the Group Parent, the consolidated income statement includes neither current taxes (as there was no taxable income during 2006) nor net deferred tax assets, as there is a lack of the prerequisites established by the applicable accounting standard.

Following is an analysis of the difference between the theoretical tax rate and the effective tax rate for 2006 and 2005:

	2006	2005
Income before taxes	**1,272**	**586**
Percentage impact of Italian and foreign taxes		
IRES (net of tax receipts)	6.37	0.34
IRAP	9.91	17.92
Other income tax	7	13.14
Taxes for previous periods	(0.31)	-
Allocations for tax disputes	1.10	1.54
Net deferred taxes	(4.95)	1.19
Effective rate	**19.12**	**34.13**
Increase (Decrease)		
Percentage impact of the permanent difference on the effective rate	19.62	7.59
Theoretical rate	**38.74**	**41.72**

The permanent differences relating to 2006 regard the capital gains on the equity investments sold under the rules for participation exemption (Note 38).
Deferred taxes and their related receivables and payables at 31 December 2006 were the result of the following temporary differences:

	Income statement		Balance sheet
	Assets	Liabilities	Net effect
Derivatives at fair value through profit or loss	(1)	-	11
Stock option/stock grant	3	-	3
Inventory impairment	(15)	-	(29)
Provisions for risks and charges	15	-	83
Past losses	40	-	160
Severance pay, pension funds and seniority bonuses	1	(3)	92
Carrying value of non-current assets	-	(12)	(197)
Finance leases	1	1	6
Grants	-	4	(10)
Other	29	-	(11)
	73	**(10)**	**108**

Deferred taxes include €mil. 23 relating to net deferred tax liabilities allocated directly to equity, for derivative instruments recognised as cash-flow hedges. The changes for the period for the equity item were as follows:

	31 December 2005	Recognition in the income statement	Fair value adjustments	Other changes	31 December 2006
Deferred taxes recognised directly in equity	8	4	(35)	-	(23)

XLI. Discontinued operations and assets held for sale

Group operations in the bus manufacturing sector were classified as discontinued operations as they are about to be sold. As such, the balance sheet includes the assets and liabilities attributed to this business segment, net of impairment charges to realign the carrying value with the fair value (sales value less transaction costs).
Similarly, the results of the operations identified as discontinued have been shown separately on the income statements. Therefore, the item includes the results for the period of such assets:

- for 2006, the results regarding assets to be sold held by the Group in the bus manufacturing sector;
- for 2005, the result on the UK operations in the radar-devices segment through the sale date (29 April 2005), the results of assets in the process of being sold held by the Group in the bus manufacturing sector and income relating to the sale of the "Atlantic Bird" programme.

	2006	2005
Income	88	214
Costs	(96)	(214)
Net financial income (expense)	(1)	1
(Write-down) Net write-backs	-	9
Tax expense	-	-
	(9)	**10**

With regard to balance sheet items:

	31 December 2006	31 December 2005
Assets		
Intangible assets	1	1
Property, plant and equipment	10	20
Investment properties	-	-
Equity investments	-	-
Securities held to maturity	-	-
Financial assets at fair value	-	-
Non-current receivables from related parties	-	-
Receivables	-	-
Deferred taxes	-	-
Other non-current assets	-	-
	11	21
Inventories	26	26
Contract work in progress	-	-
Current receivables from related parties	-	-
Trade receivables	67	69
Short-term securities held to maturity	-	-
Current financial assets at fair value	-	-
Tax receivables	-	-
Financial receivables	-	-
Other current assets	1	1
Cash and cash equivalents	5	3
	99	99
	110	**120**

	31 December 2006	31 December 2005
Liabilities		
Non-current payables to related parties	-	-
Non-current financial payables	-	-
Severance pay and other employee provisions	5	4
Provisions for risks and charges	28	27
Deferred tax assets	-	-
Other non-current liabilities	-	-
	33	31
Advances from customers	-	3
Current payables due to related parties	-	-
Trade payables	36	46
Current financial payables	11	8
Tax payables	1	3
Current provision for risks and charges	-	-
Other current liabilities	2	1
	50	61
	83	**92**

XLII. Earnings per share

Earnings per share (EPS) are calculated as follows:
- for basic EPS, by dividing net profit attributable to holders of ordinary shares by the average number of ordinary shares for the period less treasury shares;
- for diluted EPS, by dividing net profit by the average number of ordinary shares and the average number of ordinary shares potentially deriving from the exercise of all the option rights for stock option plans less treasury shares.

Basic EPS	2006	2005
Average number of shares for the period (in thousands)	423,323	421,941
Net result (not including minority interests) (€mil.)	988	373
Result of continuing operations (not including minority interests) (€mil.)	997	363
Basic EPS	2.333	0.883
Basic EPS from continuing operations	2.353	0.861

Diluted EPS	2006	2005
Average number of shares for the period (in thousands)	425,094	424,994
Result adjusted (not including minority interests) (€mil.)	988	373
Adjusted result of continuing operations (not including minority interests) (€mil.)	997	363
Diluted EPS	2.323	0.877
Diluted EPS from continuing operations	2.344	0.854

XLIII. Cash flow from operating activities

	For the twelve months ended 31 December	
	2006	2005
Net profit	1,020	396
Losses connected with assets sold	9	(10)
Depreciation, amortisation and impairment	505	365
Effect of the measurement of equity investment on the equity method	5	25
Income taxes	243	200
Provisions	24	182
Cost of severance pay, defined-benefit plans and stock grant plan	192	162
Gains from the sale of assets	(34)	(31)
Gains from sale of Avio and Ansaldo STS (STM in 2005)	(707)	(10)
Financial expense, net of gains from the sale of Avio and Ansaldo STS (STM in 2005)	308	134
	1,565	**1,413**

The changes in working capital, net of the effects of the acquisition and sale of consolidated companies and translation differences, are as follows:

	2006	2005
Inventories	(288)	(811)
Contract work in progress and advances received	828	546
Trade receivables and payables	(193)	469
Changes in working capital	**347**	**204**

The changes in other operating assets and liabilities, net of the effects of the acquisition and sale of consolidated companies and translation differences, are as follows:

Payment of severance pay, other defined-benefit plans and stock grant plan	(168)	(131)
Changes in provisions for risks and in other operating items	(54)	(245)
	(222)	**(376)**

XLIV. Financial risk management

The section describes the operating criteria adopted to manage foreign exchange risk, interest rate risk and equity risk relating to listed shares held.

The application of IFRSs by Finmeccanica involves the adoption of fair value to measure the total portfolio of derivatives. With this in mind, it should be pointed out that the criteria and the related IFRS interpretations in effect create a choice between derivatives treated as hedges, for which it is possible to apply hedge accounting and for which the fair value is only significant for the purposes of the balance sheet, and those operations for which such method may not be applied and for which the change in fair value is indicated in the income statement as well as in the balance sheet.

Exchange rate risk management is governed by the directive issued by Finmeccanica in December 2002. The goal of the directive is that of creating uniformity in management criteria based on industrial – not speculative – strategies so as to contain risks within specific limits by carefully and constantly assessing all foreign currency positions. The methodology adopted calls for the systematic hedging of commercial cash flows resulting from the assumption of contractual commitments of a specific nature as either buyer or seller, thereby ensuring current exchange rates at the date of acquisition of multi-year contracts and neutralising the effects of exchange rate fluctuations.
Therefore, at the moment of receiving payment from a customer or making payment to a vendor, which takes place at the current exchange rate on that day, the related hedging transactions are extinguished in order to offset the effects of the difference between the current exchange rate and the rate of the hedging instrument. These transactions are carried out almost exclusively with banks by Finmeccanica's Group Finance Department and then matched with the companies of the Group. The companies that have the greatest need for such hedging transactions are: Alenia Aeronautica and its subsidiaries, Ansaldo Energia, Oto Melara, Selex Sensors and Airborne Systems and its subsidiaries, Alcatel Alenia Space Italia, Ansaldobreda, AgustaWestland and its subsidiaries, Selex Communications and its subsidiaries, and Selex Sistemi Integrati. At 31 December 2006 Finmeccanica had outstanding foreign exchange transactions with highly rated financial counterparties in the interest of other Group companies totalling €mil. 2,928 (a decrease of about 6% over 2005), €mil. 2,772 of which for swaps and forwards, divided between those sold for €mil. 1,986 and those purchased for €mil. 786, and €mil. 156 for foreign exchange options. As a result, the Finmeccanica Group recognises the fair value of foreign exchange derivatives as follows:

- forward instruments for which it is possible to apply hedge accounting, the fair value of which totalled a positive €mil. 46 at 31 December 2006.
- options not eligible for hedge accounting, the fair value of which came to a positive €mil. 1.

In addition, the Finmeccanica Group recognises in the income statement the fair value of the ineffective portion of forwards, i.e. the premium points the value of which represents a cost of €mil. 11 offset by gains arising from valuing the options at €mil. 2.
The fair value of forward instruments represents the change in the value of instruments hedging commercial risks and was mainly affected by the great volatility of the euro/US dollar exchange rate, which was 1.3170 at 31 December 2006 from 1.1797 at 31 December 2005, indicating a significant depreciation of the US dollar against the euro. This depreciation determined the recovery of the net fair value of instruments held from a negative €mil. 44 at 31 December 2005 to a positive €mil. 46 at 31 December 2006. This change is not adequately expressed through trading activities since hedging is carried out for the entire life-cycle and on the total amount of the contracts underlying the derivatives transactions while the contracts themselves are recognised in the financial statements only with regard to work in progress and trade receivables and/or payables. As a result, there is inevitable volatility that impacts net capital.
Another significant case is that of premium points which represent the expression of the difference in the interest rate between the currency being hedged (e.g. US dollar) and the currency used in the financial statements. This difference, added to the spot rate, provides the forward value of a swap or forward operation and, in the case of currency sales, generates a cost (pay the US dollar interest rate and receive the euro interest rate). In applying international accounting standards, this component is inapplicable and therefore the fair value is used in the income statement. The predominance of sales contracts hedging trade receivables generally leads to a negative fair value, which is made more apparent by the euro/US dollar interest rate spread trend. Most widening of this spread occurred between the end of 2005 and the start of 2006, as a result of which the fair value measurement of the premium points for 2005 benefited from this impact (negative €mil. 3) since operations entered into in past periods have premium points calculated using more restricted spreads, unlike at the end of 2006 when the US dollar rate stability and the simultaneous rise in the euro rate contributed to a reversal of the trend amplifying the negative value (€mil. 11) at the end of 2006.
The weakness of the dollar was mainly caused by expectations of a slowdown in the US economy. There was a 11.6% difference between the recognition at the end of 2005 and at the end of 2006, reflecting, too, the average exchange rate for the year of 1.2556 compared with 1.2448 for 2005. The depreciation of the dollar in 2006 and the risk of its further weakening led Finmeccanica and the other Group companies to place greater focus on expected new orders and participating in tenders in which the US dollar is the functional currency. Under IAS/IFRS, any hedging activities relating to highly-probably orders will be subject to hedge accounting and not just all potential orders. The Group is currently considering possible hedges for highly-probable orders, perhaps even using non-IAS compliant instruments.
In any event, the Finmeccanica Group does not have financial transactions of a speculative nature, in the sense that none of its transactions add risk to that which is already implicit in its operations. On the contrary, in compliance with the Group directive, all existing financial transactions have the specific objective of eliminating or minimizing such risks.

The management of interest rate risk is consistent with the long-standing practice of reducing the risk of fluctuations in interest rates while seeking to minimise related financial expense. To that end, at 31 December 2006, Finmeccanica had outstanding interest rate swaps for medium and long-term financing with highly rated financial counterparties totalling €mil. 830. Thanks to these transactions, it was possible to earn benefits from low costs of floating rates, especially in 2004-2005, by returning the debt structure to fixed rates at the start of 2006, while shielding the Company from rises such as those, starting in December 2005, that made short-term interest rates increase by more than 1%. At 31 December 2006, the total fair value of the interest rate derivatives portfolio was negative €mil. 14 compared with the negative €mil. 18 at 31 December 2005. The transactions eligible for hedge accounting experienced a positive change of €mil. 8 in the fair value at 31 December 2006 (from negative €mil. 11 to negative €mil. 3), while transactions not eligible for hedge accounting saw a deterioration in the fair value for the period of €mil. 4 (from negative €mil. 7 at 31 December 2005 to negative €mil. 11). Transactions eligible for hedge accounting, where collections were made at a variable rate and payments at a fixed rate, caused the fair value to improve.
The restrictive IFRS standards and related interpretations make it necessary to consider certain transactions as speculative even when they are essentially intended to contain financial costs mitigating the risk adding a percentage of variable interest to the composition of the debt.
In 2006, the European Central Bank applied a policy for the control of inflationary risks by increasing bank rates by 1.25% overall. This created a market expectation that rises might occur which are partly included in the current rates (Euribor 6 months at 3.85% from 2.63% 12 months ago).

The management of price risk on equity concerns hedging transactions using derivatives primarily relating to the management of the indirect investment held in STMicroelectronics N.V. (STM). At 31 December 2006 options are in place with an underlying position of 45 million of STM shares. These hedges are classified as trading operations and therefore the fair value is recognised in the income statement. In 2006, gains were realised at

the closing of the hedging transactions in the amount of €mil. 8. The recognition of the fair value through profit or loss of the changes in the fair values of these instruments led to a further gain of €mil. 9. This amount includes the positive change in fair value of €mil. 13 adjusted with premiums paid of €mil. 4. However, the intrinsic value of the derivatives in being at the same date, i.e. the value calculated as it was the maturity date of the derivatives, was €mil. 29.
The strategy implemented using put spreads and the sale of calls allows Finmeccanica to limit the negative impact of a partial depreciation of STM shares while leaving open the possibility of benefiting, within certain limits, from any appreciation in the shares and exposing the Company to potential costs/lost revenues in the event this limit is exceeded.
The equity investment is treated as an asset held for sale and therefore the change in value between the start and end of the period (from € 15.15 to € 14.064 per share), a negative €mil. 66, only had an impact on the balance sheet.
It should also be noted that the management of derivatives on STM shares has permitted the Group to receive about €mil. 63 between 2004 and 2006, improving its portfolio position.
Under IFRS, the option sold to bondholders on exchangeable STM bonds with a maturity of August 2010 is accounted for separately from the underlying bonds. It should also be noted that, in 2005, Finmeccanica acquired a virtually identical option on the open market to hedge the option sold to bondholders thereby neutralising the effects while at the same time freeing up the 20 million underlying STM shares. At 31 December 2006, the change in the fair value of these options was €mil. 23, negative for one, positive for the other and therefore there was no net impact on the income statement.
Finally, with regard to the placement of 60% of the shares of Ansaldo STS on the stock market in April 2006, Finmeccanica made a commitment to grant, for no further compensation, to subscribers who retained possession of the shares for at least 12 months, one share for every 20 held in the case of the public-at-large and Finmeccanica shareholders, and one share for every 10 held for employees.
The final accrual date for which the right to receive the free shares will be 28 March 2007.
Subscribers must submit a request to receive the shares by 30 April 2007, else the right lapses. The grant shall be made within 30 days following 30 April 2007. The fair value of this commitment at 31 December 2006 was treated as a cost of €mil. 3. It is expected that Finmeccanica will purchase these shares directly on the open market.

XLV. Remuneration to key management personnel

Remuneration paid to persons who have power and responsibility over the planning, management and control of the Company, including executive and non-executive directors, came to:

	2006	2005
Compensation	72	55
Post-employment benefits	3	1
Other long-term benefits	-	-
Severance indemnity	4	1
Stock grant	6	-
Total	**85**	**57**

Remuneration paid to directors and managers with strategic responsibility came to €mil. 83 in 2006 and €mil. 55 in 2005. Remuneration to the statutory auditors came to €mil. 2 and €mil. 2 for 2006 and 2005, respectively.
These figures include fees and other compensation, pensions and other benefits, including the portion borne by the Company, owed as a result of holding the position of director or statutory auditor of the Group Parent and of the other Group companies included in the scope of consolidation, that represented a cost for the Group.

Details on the remuneration paid to Directors, Statutory Auditors, the General Manager and the Managers exercising strategic responsibility of the Group Parent are found in the table below (*):

PERSON	DESCRIPTION OF POSITION			Emoluments by position in the reporting Company		Non-cash benefits	Bonuses and other incentives		Other remuneration	
Name	Position	Office term	Term of office expiring							
Guarguaglini Pier Francesco	Chairman/ Chief Executive Officer	1.1/31.12.2006	year 2007	77		9	1,922	(1)	1,500	
Alberti Piergiorgio	Director	1.1/31.12.2006	year 2007	70					34	
Bonferroni Franco	Director	1.1/31.12.2006	year 2007	64						
Castellaneta Giovanni	Director	1.1/31.12.2006	year 2007	66						
De Tilla Maurizio	Director	1.1/31.12.2006	year 2007	96						
Lombardi Cerri Gian Luigi	Director	1.1/31.12.2006	year 2007	72						
Monti Ernesto	Director	1.1/31.12.2006	year 2007	88						
Petri Roberto	Director	1.1/31.12.2006	year 2007	66						
Scannapieco Dario	Director	1.1/31.12.2006	year 2007	79	(2)					
Varaldo Riccardo	Director	1.1/31.12.2006	year 2007	69						
Venturoni Guido	Director	1.1/31.12.2006	year 2007	66						
Vigevano Paolo	Director	1.1/31.12.2006	year 2007	66						
Piacenza Domenico	Chairman of the Board of Statutory Auditors	1.1/23.05.2006		31						
Gaspari Luigi	Regular Member	1.1/23.05.2006	year 2008	21						
Gaspari Luigi	Chairman of the Board of Statutory Auditors	24.5/31.12.2006	year 2008	47					36	
Cumin Giorgio	Regular Member	1.1/31.12.2006	year 2008	52					52	
Forchielli Francesco	Regular Member	1.1/31.12.2006	year 2008	57					8	
Montaldo Silvano	Regular Member	24.5/31.12.2006	year 2008	31					1	
Tamborrino Antonio	Regular Member	1.1/31.12.2006	year 2008	59					42	
Zappa Giorgio	General Manager	1.1/31.12.2006				115	1,207	(1)	954	(3)
	Managers with strategic responsibility	1.1/31.12.2006				200	2,300	(1)	1,439	(4)

(1) - Variable remunerations, to be paid, are shown at their estimated value recorded in the Company's financial statements.

(2) - Of which €th. 57 paid to the Ministry of Finance.

(3) - Of which €th. 28 for emoluments by position in the Group company, paid by Finmeccanica S.p.A.

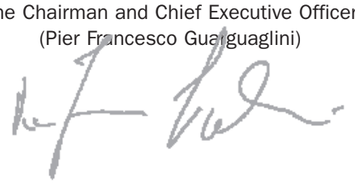
(4) - Of which €th. 111 for emoluments by position in the Group company, paid by Finmeccanica S.p.A.

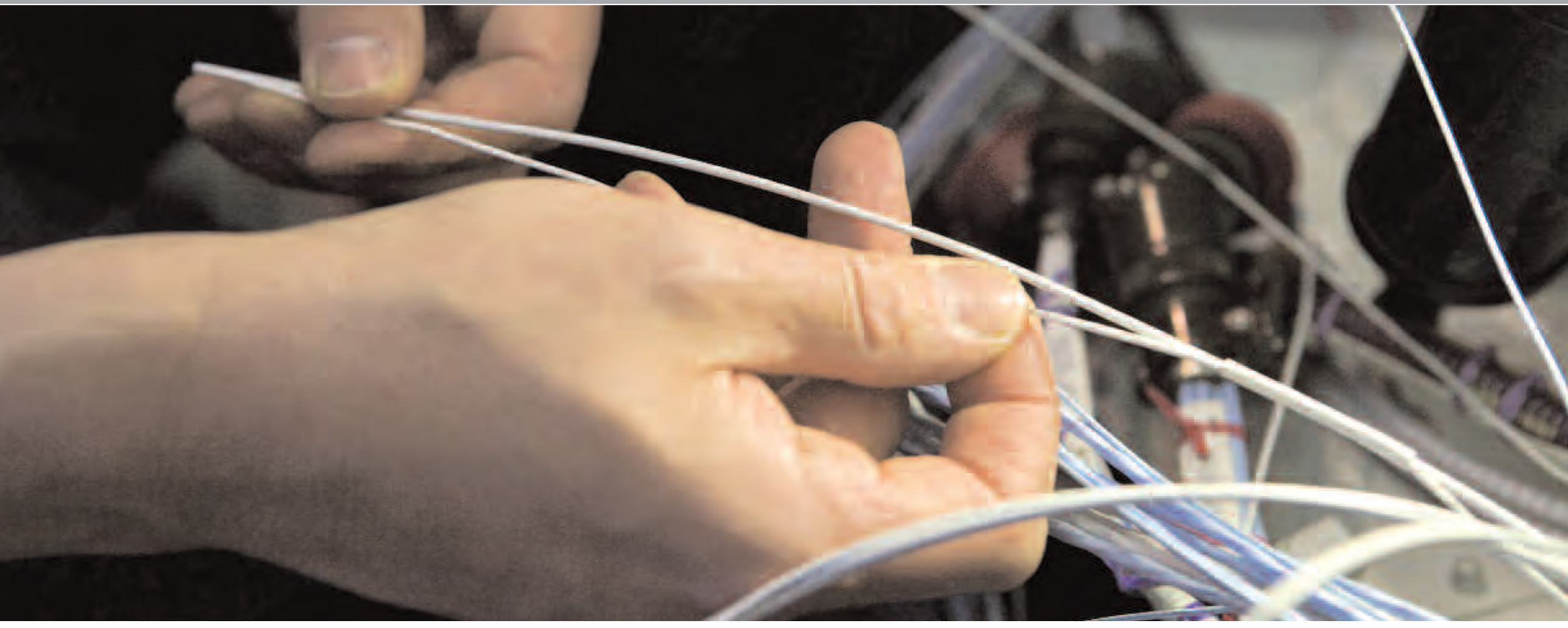
(*) Figures extracted from the 2006 financial statements of Finmeccanica S.p.A.

The parent, Finmeccanica S.p.A., in order to create an incentive and retention system for Group employees and consultants, implemented incentive plans providing for the granting of Finmeccanica shares, subject to the attainment of specific objectives.
At 31 December 2006 there were commitments to grant 4,562,310 ordinary Finmeccanica shares having a nominal value of €15.90 without compensation to Finmeccanica employees and consultants. The changes in the stock grant plans are as follows:

	2006 (number of shares)	2005 (number of shares)
Rights existing at 1 January	**-**	**-**
New rights assigned	888,456	-
Rights exercised during the year	888,456	-
Rights lapsed during the year	-	-
Rights existing at 31 December	**-**	**-**

For the Board of Directors
The Chairman and Chief Executive Officer
(Pier Francesco Guaguaglini)





Report of the Board of Statutory Auditors on the consolidated financial statements at 31 December 2006

REPORT OF THE BOARD OF STATUTORY AUDITORS TO THE 2006 CONSOLIDATED FINANCIAL STATEMENTS

Shareholders,

as in the past, the consolidated financial statements of the Finmeccanica Group have been prepared in accordance with the provisions of law on financial reporting and comply with the Articles of Association and the Board of Directors' directions.

In application of Regulation (EC) no. 1606/2002 of 19 July 2002 and in implementation of CONSOB resolution no. 14990 of 14 April 2005, the consolidated financial statements of the Finmeccanica Group at 31 December 2006 are prepared in accordance with the International Accounting and Financial Reporting Standards (IAS/IFRS) as approved by the European Commission, supplemented by the interpretations existing at the consolidated balance sheet date.

In particular, the standards used are those approved by the EU and contained in the EU Regulations enacted until the consolidated balance sheet date.

The Board of Statutory Auditors has ensured that the Parent Company has appropriately organised the flow of the necessary information from the companies included in the consolidation scope and that the consolidation procedures are adequate.

The Auditors who issued their report on the consolidated financial statements at 31 December 2006 have informed us that they have appropriately checked that the figures of the consolidated accounts matched the accounting records of the Parent Company and the data provided by the subsidiary companies and that these data have been interpreted in an appropriate manner. To this regard the Auditors have not delivered any observations or remarks worth mentioning herein.

Rome, 7 May 2007

The Board of Statutory Auditors

"This report has been translated from the original which was issued in accordance with Italian legislation".

Auditors' Report on the consolidated financial statements at 31 December 2006

PRICEWATERHOUSECOOPERS

AUDITORS' REPORT IN ACCORDANCE WITH ARTICLE 156 OF LAW DECREE NO. 58 DATED 24 FEBRUARY 1998

FINMECCANICA SPA

CONSOLIDATED FINANCIAL STATEMENTS AT 31 DECEMBER 2006

PRICEWATERHOUSECOOPERS

PricewaterhouseCoopers SpA

AUDITORS' REPORT IN ACCORDANCE WITH ARTICLE 156 OF LAW DECREE NO. 58 DATED 24 FEBRUARY 1998

To the Shareholders of
Finmeccanica SpA

1 We have audited the consolidated financial statements of Finmeccanica SpA and its subsidiaries ("Finmeccanica Group"), which comprise the balance sheet, income statement, statement of changes in shareholders' equity, cash flow statement and the related notes as of 31 December 2006. These consolidated financial statements are the responsibility of Finmeccanica SpA's directors. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

2 We conducted our audit in accordance with the auditing standards and criteria recommended by CONSOB. In accordance with those standards and criteria, the audit has been planned and performed to obtain the necessary assurance about whether the consolidated financial statements are free of material misstatement and, taken as a whole, are reliable. An audit includes examining, on a sample basis, evidence supporting the amounts and disclosures in the financial statements, as well as assessing the appropriateness of the accounting principles used and the reasonableness of the estimates made by the directors. We believe that our audit provides a reasonable basis for our opinion.

For the opinion on the consolidated financial statements of the prior period, which are presented for comparative purposes as required by law, reference is made to our report dated 4 May 2006.

3 In our opinion, the consolidated financial statements of Finmeccanica SpA as of 31 December 2006 comply with IFRS as adopted by the European Union, as well as the provisions enacted to implement Article 9 of Law

PRICEWATERHOUSECOOPERS

Decree no. 38/2005; accordingly, they give a true and fair view of the financial position, the results of operations, the changes in shareholders' equity and cash flows of the Finmeccanica Group for the year then ended.

Rome, 7 May 2007

PricewaterhouseCoopers SpA

Signed by

Corrado Testori
(Partner)

"This report has been translated from the original which was issued in accordance with Italian legislation. References in this report to the Financial Statements refer to the Financial Statements in original Italian and not to their translation".

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