Annual Report 2017

RUAG performs well in a challenging year. The result reflects solid growth plus the impact of one-off factors on profitability.

Together ahead. RUAG

Contents

The 2017 financial year

With net sales of CHF 1,955 million (previous year: CHF 1,858 million), RUAG once again topped its record prior-year performance – this time by 5.2 %. Earnings before interest and taxes (EBIT) fell to CHF 119 million (CHF 151 million) and net profit to CHF 89 million (CHF 116 million).

In 2017 around 56 % (57 %) of RUAG's contracts were in the civilian sector, and 62 % (63 %) of its net sales came from outside Switzerland. Overall, the Group generated net sales of CHF 1,955 million, representing an increase of CHF 97 million, or 5.2 %. Alongside organic growth, international acquisitions such as Clearswift also contributed to this further increase. However, the international technology group was unable to uphold last year's record result.

Earnings before interest and taxes (EBIT) fell to CHF 119 million (CHF 151 million) and net profit to CHF 89 million (CHF 116 million). Except for the Defence division, all divisions have generated a profit. The order backlog rose overall to CHF 1,607 million (CHF 1,556 million); new orders declined to CHF 1,961 million (CHF 2,036 million). Both numbers indicate that there is still a sound basis for the further development of the business.

As of the beginning of 2018, responsibility for the Cyber Security business unit – previously run by the Defence division – passed to the Group's CEO. The Cyber Security area is one of RUAG's most important growth pillars. The software-based business requires a broader route to market, as it differs fundamentally from the defence technology business.

Key personnel changes occurred in the Ammotec and Defence divisions. At the beginning of October Christoph M. Eisenhardt replaced Cyril Kubelka, who had spent 14 years at the helm of the Ammotec division. The Defence division is being run by Andreas Berger following Dr Markus A. Zoller's departure from RUAG at the end of October.

Dividend of CHF 40 million proposed
The Board of Directors proposes a dividend of CHF 40 million (CHF 47 million) for the 2017 financial year. This represents 45% of consolidated net profit.

The Federal Department of Defence, Civil Protection and Sport (DDPS) remains RUAG's largest and most important single customer; its share of sales is an unchanged 31 %.

Research and development spending increased slightly (by CHF 10 million to CHF 181 million) and at 9.2% remains unchanged in relation to net sales.

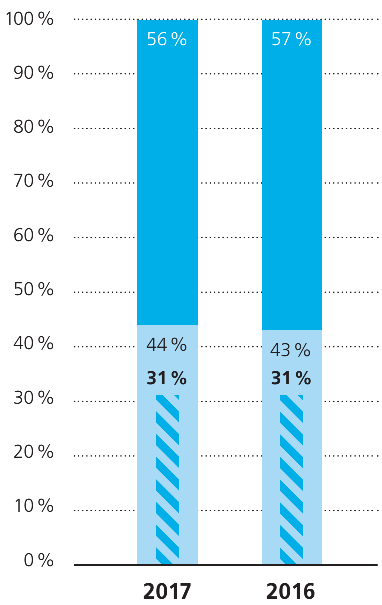
The number of full-time equivalent employees (FTE) in the Group increased to 9,189 (+5.2 %) as at 31 December 2017; this is attributable to the acquisition of Clearswift, the establishment of the new sites in the United States and Hungary, and the general growth in sales.

RUAG is still on a solid financial footing. The Group's net financial position stands at CHF 77 million (CHF 237 million). Due to the lower operating result and to investments in current assets, cash flow from operating activities fell to CHF 88 million (CHF 135 million). Free cash flow in 2017 stood at minus CHF 58 million (CHF 56 million). This primarily reflects the purchase prices paid for the acquisitions concluded during the financial year as well as investments in capacity increases for additional orders.

Change on the Board of Directors

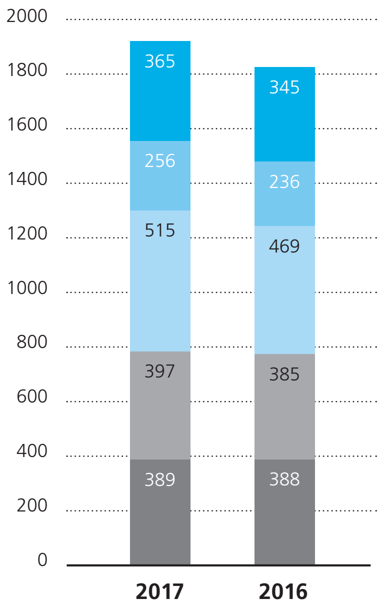
After 16 years on the Board of Directors, Board Chairman Hans-Peter Schwald will not be standing for re-election again in 2018. "Hans-Peter Schwald played a decisive role in the Group's development into an international technology group. The Board of Directors and management of RUAG wish to thank him formally for his tireless commitment and expertise", said Group CEO Urs Breitmeier.

Net sales by application
in %



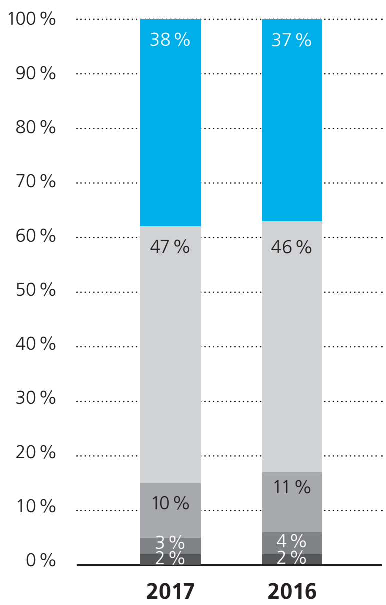
Civil	56 %
Military	44 %
DDPS	31 %

Net sales by division
in CHF million



Space	365 m
Aerostructures	256 m
Aviation	515 m
Ammotec	397 m
Defence	389 m

Net sales by market
in %



Switzerland	38 %
Europe	47 %
North America	10 %
Asia / Pacific	3 %
Rest of the world	2 %

Overview of key figures

in CHF million	2017	2016	Change in %
Net sales	1 955	1 858	5.2 %
Operating income	1 990	1 882	5.8 %
Earnings before interest, taxes, depreciation and amortization (EBITDA)	196	232	–15.6 %
Earnings before interest and taxes (EBIT)	119	151	–21.5 %
Net profit	89	116	–22.8 %
Cash flow from operating activities	88	135	–35.0 %
Free cash flow	(58)	56	–203.2 %
Net financial position	77	237	–67.6 %
Order inflow	1 961	2 036	–3.7 %
Order backlog	1 607	1 556	3.3 %
Research and development expenses	181	171	5.8 %
Employees (FTE) as at 31 December incl. apprentices	9 189	8 734	5.2 %

For detailed figures, see Note 5 "Segment information" in the financial statements.

Good growth, reduced profitability

RUAG's sales outstripped the previous year. However, isolated one-off events reduced profitability. The outlook is promising, thanks in part to investments in the high-growth US market.

Dear shareholder,
customers and readers

RUAG was not able to top last year's highly satisfactory result in 2017. Sales increased again – by 5.2 % to CHF 1,955 million – and order intake also remained high at CHF 1,961 million. However, EBIT fell by CHF 32 million to CHF 119 million. RUAG generated 56 % of its total sales in the civilian sector. Its most important customer remains the DDPS, accounting for 31 % of sales. Overall, 62 % of the Group's net sales came from outside Switzerland, where it also has around 4,800 of its 9,200 or so employees. In addition to Switzerland, RUAG now has business locations in 15 countries.

Four out of the five divisions operated profitably. The Defence division closed the year with a loss, however. As a result, RUAG as a whole was unable to achieve its budgeted earnings targets. Positive surprises came from the Space division and the Real Estate service unit, both of which surpassed the high expectations set for them.

The results achieved by the Aerostructures and Aviation divisions were impacted to some extent by unforeseen sales losses and additional costs incurred for two projects as a result of quality and scheduling issues with individual suppliers. Thanks to an exceptional effort, adherence to quality and schedules has now been restored for the Aerostructures suppliers, and the issues at RUAG Aviation have been contained.

The Ammotec division was forced to accept an unusually large decline in sales in the United States as an indirect consequence of Donald Trump's election as the new US President. In anticipation of an election victory by Trump's opponent Hillary Clinton, who favoured more restrictive gun laws, many private individuals stockpiled ammunition in 2016, which resulted in a marked decline in demand in 2017.

The biggest negative influence on the consolidated result came from adverse developments in some major Defence division projects. Here, both the Group Executive Board and the division's management reacted decisively. As well as carrying out restructuring in the Land Systems area, the division also had to reassess the costs and returns for various projects, putting a CHF 20 million dent in its earnings. At the personnel level, there were changes all the way to the top. The Defence division will continue to focus on its core competencies. In this context, the Cyber Security operation is being separated out from the division, and from 1 January 2018 will be run by the CEO as a stand-alone unit. This is also intended as a clear signal to further strengthen the Cyber Security area.

Aside from the disappointing result of the Defence division and the negative developments in a few projects, RUAG's business has continued to develop steadily overall.

A year of investments

With a view to the Group's future, several major investments in the strategic growth areas of Space and Aerostructures were the main focus of RUAG's development in 2017. The Space division started production at not one but two new sites in the United States. The facility in Decatur, Alabama, will be producing carbon fibre structures along the same lines as the out-of-autoclave procedure successfully introduced for the US launch vehicles in Emmen last year. Titusville, Florida, has successfully begun large-scale production of structures for the 900 satellites of the OneWeb satellite internet project. In addition, in Emmen the Aerostructures division has put into operation a state-of-the-art surface treatment facility using the environmentally friendly TSA method (chromic acid free anodizing). Moreover, in Eger, Hungary, the division has opened a new production facility in a "best-cost" country.

With a view to the Group's future, several major investments in the strategic growth areas of Space and Aerostructures were the main focus in 2017.

Game-changing contracts and successful projects

The encouraging order intake figure reflects the numerous successes in acquiring contracts and implementing projects. RUAG Space, for example, has won the right to supply (among other things) the control computer, various mechanical components and the protective thermal insulation for the next twelve satellites for the European navigation system Galileo.

RUAG Aerostructures was able to complete its transfer-of-work project begun in 2014, taking on full responsibility for the supply chain for two fuselage sections of the Airbus A320. With this, RUAG is making a key contribution to the manufacture of the A320 and will be able to fully exploit the model's enduring commercial success.

The Aviation division has ensured longer-term capacity utilization by renewing the 5-year service-level agreement (SLA) for maintaining the Swiss Air Force's aircraft fleets. The upgrade programmes for the Swiss F/A-18, F-5, Cougar transport helicopter, PC-6 and 35mm anti-aircraft guns progressed as scheduled. With these projects, RUAG can make an important contribution to the longer-term operational capability of these systems, which are also crucial to preserving the Swiss defence sector's know-how, for ensuring this industry's continuing development and for maintaining RUAG's own level of expertise. Moreover, the development of the business in MRO services in Australia for the F/A-18 and the new American F-35 Joint Strike Fighter was exceptionally successful.

RUAG Ammotec chalked up a success which bodes well for the future: the division gained consent for a licence to set up an ammunition production facility in Brazil, a market which had until now been completely closed. For RUAG Ammotec, this not only opens the doors to the world's second-largest ammunition market, but also gives it additional options for increasing the flexibility of its production. The division is currently looking into a variety of scenarios to see whether, how and when it will be able to put its plans into action. In this regard, RUAG is also looking to preserve and increase its ability to compete at international level, which will ultimately also benefit its main customer, the DDPS.

For RUAG Defence, too, the renewal of the 5-year SLA for over 100 systems used by the Swiss Armed Forces was pivotal. It allows the division to make long-term plans and increase its efficiency, to the benefit of both partners. It also succeeded in forays into two new markets. Swiss manufacturer Boschung is developing its snow-clearing systems for airports based on RUAG's robotics platform, and with the deployment of the "Tactical Access Node" (TAN) voice and data router by the multinational battle group in Lithuania, the division was able to acquire its first ever NATO contract. RUAG's communications technology is allowing different armed forces with different systems to communicate with each other.

An important step for the future is the separation of the Cyber Security area from RUAG Defence. The software-based business with internet security is fundamentally different from defence technology and requires a broader route to market. From 1 January 2018, the business unit will operate as a separate entity at Group level and is thus being further strengthened for its planned and essential growth.

A year of personnel changes

The announced resignation of Board Chairman Hans-Peter Schwald on the occasion of the AGM of 26 April 2018, which had been planned for some time, marks the end of an era for RUAG. Hans-Peter Schwald, who has been a member of the Board since 2002 – a total of 16 years – and its Chair since 2014, has played a decisive role in the Group's development from four state-owned and operated enterprises into an international technology group. After completing this process of growth and reorganization and successfully realigning itself, RUAG is now entering a new phase in its development.

Another change at the highest level of management occurred at the top of RUAG Ammotec. Cyril Kubelka left the Group after 14 successful years as the division's CEO. The handover to Christoph M. Eisenhardt was seamlessly completed on 1 October. There was also a change at the top at RUAG Defence. Due to the way the division was developing, CEO Dr Markus A. Zoller made the decision to embrace a new challenge and left the company at the end of October. Since then, RUAG Defence's Senior Vice President NEO Andreas Berger has been running the division on an interim basis.

Expediting development

Since 2015, the Swiss Federal Council has been giving some thought to RUAG's future development in its role as the Group's owner, together with the Federal Department of Defence, Civil Protection and Sport (DDPS), the Federal Department of Finance (FDF) and RUAG itself. The Confederation and RUAG are seeking a solution which guarantees RUAG's provision of services to the Swiss Armed Forces and thus ensures that Switzerland's security is not compromised. At the same time, the solution should allow the business to continue to grow, while reducing the risks for the Confederation, in particular with regard to IT security and financial liability. Existing jobs are to be protected to ensure that the company's industrial capabilities remain in place.

To allow relations between the Confederation and the company to be configured in the best possible way and further strengthened, the Board of Directors has also created a new role, that of Vice President Owner Relations. The company was able to attract a competent, experienced figure for this challenging job in the person of the former Treasurer for the City of Bern, Alexandre Schmidt.

Forward-looking corporate projects

RUAG went ahead with several Group-level projects in 2017 with the aim of fundamentally improving the Group's efficiency and performance across the board. Pivotal to the Group's sustainable development is the multi-year Integrity@RUAG initiative. This provides a consistent anchor for compliance within the Group at all levels. Among other things, the Group introduced a new Code of Conduct in 2017. It also created an autonomous Compliance & Risk Management unit with its own Vice President, and every division will now have a Compliance Officer.

RUAG is looking to strengthen its ability to compete with the Group-wide ROS (RUAG Operating System) initiative. With this, the Group is introducing uniform lean management principles across the board in production and service delivery. These principles will make RUAG's processes leaner and more efficient, as well as improving the learning capacity and accountability of the organization.

The Swiss Confederation and RUAG are seeking a solution which guarantees RUAG's provision of services to the armed forces while also allowing the business to continue growing.

Outlook

The economic environment seems set to remain unchanged for RUAG in the coming year. On the one hand this means that a positive global economic climate is providing growth stimuli in all areas. Added to this, defence budgets in the core markets of Switzerland and Europe are continuing to rise in general. On the other hand we have the worldwide increase in regional conflicts. These are making more countries subject to Swiss export restrictions, and they can thus no longer be considered as markets for military products and services. Accordingly, RUAG is expecting a further shift in the balance of its sales from the defence to the civil segment.

Prospects for the three strategic growth pillars of Space, Aerostructures and Cyber Security are looking promising. The Space division's new production sites in Decatur and Titusville will also improve the market opportunities in the institutional space business in the United States. The Aerostructures division can expect to see continuing growth in global demand for aircraft, and in particular increasing demand for the single-aisle models produced by Airbus. For the Cyber Security business unit, the global megatrend of digitization will continue to be the driver of growth in 2018.

RUAG's top priority for 2018 is the "RUAG Future Development" project. The owner's strategy of the Swiss Confederation must in future define appropriate parameters for the two areas which make RUAG what it is: on the one hand the activities it performs in a competitive environment (80 % of its goods and services) and, on the other, its duties to supply the armed forces, which are almost statutory in nature. The spectrum of solutions spans both the incipient – and necessary – process of decoupling of relations between the Confederation and the Group, and a possible privatization or partial privatization.

The Swiss Federal Act of 10 October 1997 on Federal Armaments Companies was a milestone for the Swiss defence industry and is what made the establishment of RUAG possible in the first place. Based on know-how which had been built up over decades, a target-oriented owner's strategy on the part of the Federal Council and an entrepreneurial Board of Directors and Management, an internationally respected and successful technology and defence company was developed and built up. However, to allow RUAG to continue to write the success story which started at its foundation and to develop further, the company needs to retain commercial freedoms and opportunities to assert itself against its competitors in the international arena. Its future competitiveness is also of vital importance to Switzerland as a centre for industry and technology, as well as to the country's defence and security policy. RUAG has to be in a position to adapt in line with constantly changing markets. Thus changes also need to be made to the current operating conditions for the business. Otherwise we would run the risk of RUAG being confined to a "straitjacket" that no longer reflects the times.

The Board of Directors and Group Executive Board are convinced that RUAG can still succeed even as global competition becomes fiercer. We look forward to further developing the business together with our shareholder, our customers, partners and employees, and thank you for your loyalty and your trust, as well as for the opportunity to work with you and for your dedication.

RUAG Holding Ltd.

Hans-Peter Schwald
Chairman of the Board of Directors

Urs Breitmeier
CEO RUAG Group

RUAG Space

RUAG's space business is exhibiting profitable growth both in Europe and in the United States. The Swiss side of the operation is also benefiting from the new business. Optimized manufacturing processes and a market-driven product range have resulted in major contracts for ESA, NASA and commercial programmes. With a focus on process optimization, RUAG Space is looking to hone its competitive edge still further in 2018.

Business performance

Lower market entry barriers, higher cost pressure, new players – that is the setting in which RUAG Space is operating. As always, the space industry is on the move, and in this new era there is as yet no sign of consolidation. The institutional and commercial ("New Space") markets are coexisting and challenging each other. For RUAG Space as a product manufacturer this means, more than ever, being close to its customers. In 2017, it once again succeeded in this regard. The Space division closed the year with EBIT of CHF 34 million (CHF 32 million) and sales of CHF 365 million (CHF 345 million).

Moreover, RUAG Space also ended 2017 with an important contract in the electronics domain. While the ESA was using a central control computer supplied by RUAG Space to send another four Galileo satellites into orbit in December, the division announced that it would also be supplying the central computer – in a sense the "brain" – for the next batch of navigation satellites. And the RUAG Space computer from Sweden will also be used in the first electrically driven satellite, Electra. In the segment of navigation receivers, which are manufactured by RUAG Space in Austria, the division is leading the market in Europe, and it was also able to gain new business in the United States.

In the other product groups, too, new orders in 2017 showed that RUAG Space had made the right decisions in previous years in terms of locations, products and processes. For example, RUAG Space is a member of a consortium of companies that will be manufacturing the so-called "Universal Stage Adapter" for NASA's new Space Launch System. This has been made possible by the new facility in Decatur, Alabama (USA) – and by systematically expediting an optimized manufacturing process for carbon structures using state-of-the-art production methods. The first payload fairings to come out of Emmen (Switzerland) which are likewise based on this process had their maiden flight in June 2017 and will proportionally reduce the costs for the future European launch vehicle Ariane 6 by 40 %.

In the case of new orders, such as that for the OneWeb telecommunications network, the synergies between the international RUAG Space locations and its broad product portfolio were brought to bear. As well as structures and dispensers from the production facilities in Titusville, Florida (USA), and Linköping (Sweden) – which, respectively, were recently opened or expanded – cooperation was extended to include other products from the RUAG Space portfolio.

In parallel to growing its business, RUAG is working intensively on the products of the future. RUAG Space is thus keen to establish itself increasingly as a centre of excellence for promising new processes in the mechanical domain, for example in the semi-automated manufacturing of satellite structures. In this regard, one strategic pillar within the industry falls under the heading "COTS" (commercials off the shelf). This means that RUAG Space is increasingly using standard components in its products, instead of individual designs, and qualifying these for space applications. This not only cuts manufacturing time and costs, but also generates higher performance, especially in the electronics field. The prototype of a COTS-based on-board computer developed by RUAG Space was presented this year at a trade fair.

Outlook

While the order intake figure for 2017 means that the division can look to next year with a certain degree of optimism, the space market remains strained. Thus the priority now is to get on the right track for long-term success in a market in which not every player will be able to prevail.

The institutional business remains an important pillar for RUAG Space; nonetheless, the requirements of the commercial business are leading it to adopt a focused, less country-oriented approach to developing and marketing its portfolio. The new organizational structure of the Space division is designed to meet this need; the division will no longer operate based on country units, but rather on three product groups: Electronics, Spacecraft and Launchers. It is also focusing on continuously improving its operating processes (Operational Excellence) – this is the only way for RUAG Space to remain competitive in the long term. Reducing costs and accelerating up to series production: these will continue to be important success parameters in the turbulent space industry in 2018.

Against this backdrop, the biggest growth potential for RUAG Space lies in the US market. Having extended its US presence to four locations, RUAG Space now fulfils a key condition to qualify for both commercial and institutional contracts. With its latest branch, a development site in Silicon Valley (USA), RUAG is also looking to establish itself as a supplier for high-throughput satellites. By expanding its portfolio in the area of digital electronics, RUAG is planning to have its products in the newest generation of telecommunications satellites too.

Last but not least, the increasing number of constellations – i.e. networks of mainly smaller satellites – and the corresponding need for launch frequencies, is also opening up new business opportunities. Product lines geared specifically to smaller satellites (e.g. CubeSats) or corresponding "small launchers" are well advanced.

Brief profile

RUAG Space is the leading supplier of products for the space industry in Europe and has a growing presence in the United States as well. With 14 production sites in six countries, the division specializes in components for use aboard satellites and launch vehicles. Its competencies fall into three areas: electronics for all space applications, mechanical and thermal products for satellites, and structures and separation systems for launch vehicles.

Customers/partners
ESA, NASA, ArianeGroup, Airbus Defence & Space, Thales Alenia Space, OHB, United Launch Alliance, Space Systems Loral, Orbital ATK, Boeing, Lockheed Martin

Numbers and facts

Net sales:	CHF 365 million
EBITDA:	CHF 46 million
EBIT:	CHF 34 million
Employees (FTE):	1,350
Based in:	Switzerland, Sweden, Austria, USA, Finland, Germany

RUAG Aerostructures

RUAG Aerostructures strengthened its position as a tier-one supplier with global operations for developing and manufacturing complete fuselage sections, wing components, and flap and system modules. Thanks to increasing demand for single-aisle aircraft, the division continues to expand.

Business performance

RUAG Aerostructures expanded its position as an internationally active business in the aviation industry in 2017. As a supplier to well-known customers such as Airbus, Boeing, Bombardier, Saab and Pilatus, the division develops and manufactures complete fuselage sections, wing and control surface components, parts, modules and systems. In doing so, RUAG Aerostructures has enjoyed a key role in the success of the medium range aircraft used by European manufacturer Airbus, and in 2017 delivered more fuselage structures for the latter's single-aisle programme than ever before in the company's history.

RUAG Aerostructures increased its sales by 8.5 % in 2017 to CHF 256 million (CHF 236 million). Its contribution to EBIT was CHF 8 million (CHF 12 million). One of the major challenges facing the division in 2017 was successfully completing the transfer-of-work project. In this project, RUAG Aerostructures has been assuming complete supply chain responsibility for the 1,000-plus parts for two Airbus fuselage sections since 2014. However, during the last of a total of six waves in which Airbus parts were taken on as part of the division's supply responsibilities, quality and supply problems arose with a supplier. Thanks to an outstanding effort by the supplier, employees and management, these problems were mostly resolved by the end of the year without any direct adverse effects for the end customer. For RUAG Aerostructures, however, this entailed substantial additional work which were reflected in decreased profitability compared to the previous year.

In March 2017 RUAG Aerostructures opened up an additional production site in Eger, Hungary, with a view to further enhancing the division's competitiveness. In the next few years, more than 180 employees will manufacture sub-assemblies and components such as side shells, seat rails and frames for emergency exits for the Airbus A320 programme and the Bombardier CRJ programme at this new "best-cost country" location. The total investment in Eger (Hungary) equated to CHF 6.8 million in the years 2016–18.

At its main facilities in Emmen (Switzerland) and Oberpfaffenhofen (Germany) RUAG Aerostructures continued systematically to implement its strategy of targeting efficiency gains. The aims are to identify weaknesses in the supply chain at an early stage, minimize friction losses in production and increase the efficiency of support functions.

At its Emmen site, RUAG Aerostructures invested CHF 23 million in the construction of a cutting-edge surface treatment facility in 2017. A major milestone after completion of the construction activities was the handover of the keys on 3 November 2017. In future, aircraft components of up to 7 metres in length will be galvanized, painted and checked for cracks at the facility.

In October 2017, RUAG Aerostructures was chosen by US military contractor Boeing Defense to continue series production of the rear wing flaps of the F/A-18 E/F multirole jet fighter. The contract strengthens the industrial partnership between Boeing Defense and RUAG Aerostructures, which goes back many years.

RUAG Aerostructures underscored its qualities as a reliable supplier with the acquisition of a contract from Swedish aircraft manufacturer Saab to manufacture drop tanks. Moreover, the division chalked up another major contract from its customer Pilatus to manufacture fuselage and wing structures for the PC-21 aircraft.

The critical success factors for the division are lean processes and cutting-edge automation technologies. In terms of R&D, RUAG Aerostructures is currently focusing on new, automated assembly processes while at the same time implementing additive manufacturing processes for new aircraft programmes.

Outlook

According to the manufacturer's forecasts, the environment in the commercial aviation market is set to remain positive in the years ahead. Airbus anticipates a further increase in demand for commercial aircraft over the next 20 years. According to the latest estimates, Airbus expects a global requirement of around 34,900 new passenger jets and cargo aircraft by 2036 (deliveries). This could almost double the size of the worldwide fleet by 2036.

RUAG Aerostructures is focusing on strengthening and enhancing its position as a global first-tier supplier with the aim of generating profitable growth. The global supply chain will be continuously expanded, with cultivation of new suppliers in emerging countries and systematic enlargement of the supplier network. The new production site in Eger, Hungary now gives the division, as a tier-one supplier with global operations, the opportunity to take direct advantage of production in a best-cost country location.

Finally, the division is working to lock in new business opportunities so as to further improve its market position among the top tier-one suppliers for aircraft structures. Specifically, it is aiming to develop the North American market, and particularly the business relationship with customer Boeing Commercial Airplanes, with a view to further differentiating the customer base.

To set itself apart from its competitors, RUAG Aerostructures is not only expanding its technological expertise in structural engineering, wing components and parts manufacturing but is also focusing on establishing its service offering. A core aspect of this service strategy is the new surface treatment facility at the Emmen site, which will be going into operation in 2018.

Brief profile

RUAG Aerostructures is a global first-tier supplier of aerostructures for civil and military customers. Key activities include the development, production and final assembly of complete fuselage sections, wing and control surface components as well as sophisticated component assemblies and parts for civil and military aircraft. One of the division's strengths lies in managing complex supply chain networks. Among other things, it is responsible for the complete global fuselage section supply chains for Airbus and Bombardier.

Customers/partners
Airbus, Boeing, Bombardier, Dassault Aviation, GE Aviation, Pilatus Aircraft, Saab

Numbers and facts

Net sales:	CHF 256 million
EBITDA:	CHF 11 million
EBIT:	CHF 8 million
Employees (FTE):	1,251
Based in:	Switzerland, Germany, Hungary

RUAG Aviation

The financial year was shaped by stronger sales and supply chain challenges. Another five-year fixed price contract was agreed for the Swiss Air Force. The international components business continued to grow strongly.

Business performance

RUAG Aviation's year was shaped by a variety of market challenges. While net sales rose from CHF 469 million to CHF 515 million, external factors caused EBIT to decrease from CHF 44 million to CHF 39 million.

In the Swiss market, the division was able to replace the service-level agreements expiring at the end of 2017 with new five-year fixed contracts for the maintenance of the Swiss Air Force's aircraft fleets. These provide scope for forward-looking planning as a basis for improved resource allocation along with substantial productivity gains in life cycle support.

In addition to life cycle support, the military business in the domestic market focused on the various upgrade programmes for the F/A-18 (Structural Refurbishment Programs 1 and 2), the F-5 (Upper Cockpit Longeron Replacement), the Cougar transport helicopter (TH98WE), the PC-6 (NCPC-6) and the 35mm anti-aircraft guns (MFlab NUV), all of which progressed as scheduled.

Highlights included the successful first flight of the prototype for the upgraded Cougar and the commencement of work on the prototype for the F/A-18 Structural Refurbishment Programs 2, both of which took place in November. In December the division was finally able to sign the option agreement for the series conversion of the Cougar fleet, subject to credit approval by the Swiss Parliament, starting in spring 2019.

With a few exceptions, the projects with the DDPS are well under way and are coming in on time and within budget. Despite the lasting and extremely persistent slump in the new helicopter business and the associated sustained and heavy price pressure in the MRO business, the division once again chalked up some impressive successes in its Helicopter MRO Global Business, in both the maintenance and upgrade segments. For example, it secured a two-year extension to the existing maintenance contract for the Cougar helicopters used by the Slovenian armed forces despite strong competition from Europe, and, thanks to a reputation for impeccable quality paired with short delivery times, the overhauls business for dynamic components (gears and rotor heads) for Super Puma and Cougar helicopters also put in an extremely satisfying performance.

Alongside various smaller-scale modification projects, one important success and clear proof of the division's abilities in this regard was the delivery of two brand new H125 helicopters with extensively modified cockpits to the Federal Office of Civil Aviation (FOCA) and the Swiss Transportation Safety Investigation Board (STSB). The modifications were carried out by RUAG Aviation on behalf of Airbus Helicopters.

The international components business continues to achieve double-digit growth. RUAG Australia, for example, further extended its existing five-year contract for maintenance of F/A-18 components for the Australian Air Force. As planned, in addition to the contract for the maintenance of key components for the new F-35 platform, the subsidiary was able to acquire further orders for manufacturing and assembly of components for the F-35.

The division pushed on with its MRO 4.0 project to carry out maintenance activities on a preventive and even better planned basis, and to use new and more efficient repair technologies. Due to the discounts agreed upon in the five-year fixed contract for the Swiss Air Force, the importance of this project has increased further.

The Business Aviation segment put in a disappointing performance. On the one hand, capacity utilization at the Geneva and Oberpfaffenhofen sites was insufficient due to poor market conditions in Europe, and margins were below expectations. On the other, due to quality problems with a supplier, none of the Dornier 228 aircraft could be delivered to the customer as scheduled. This weighed on RUAG Aviation's result.

Outlook

RUAG Aviation is expecting to see further growth in the international military market (Germany, Australia, United States), although the opportunities for exports out of Switzerland will remain restricted due to the political situation.

In the domestic military market, the division expects to achieve similar volumes to previous years. The focus here is on securing high availability and on reliably executing the F/A-18 upgrade and structural refurbishment and Cougar helicopter upgrade programmes.

In the civil market RUAG Aviation is anticipating growth in the relevant sub-markets, although price pressure will remain high, particularly considering the Swiss franc's exchange rate vis-a-vis the US and Australian dollars and the euro.

The division is expecting the challenging market conditions in the Business Aviation segment to remain in place in 2018. The maintenance contracts recently negotiated with the Federal Office for Defence Procurement (armasuisse) also constitute a challenge, particularly during the first few years when not all planned measures will have an impact. RUAG Aviation will need to make further efforts to achieve efficiency gains in processes and procedures, and to purposefully combine the civil and military businesses, in order to keep revenues and margins stable in 2018.

Brief profile

RUAG Aviation is a leading supplier, support provider and integrator of systems and components for civil and military aviation. Servicing aircraft and helicopters throughout their entire life cycle, the company's core competencies include maintenance, repair and overhaul services, upgrades, and the development, manufacturing and integration of subsystems. RUAG Aviation is also manufacturer (OEM) of the Dornier 228, a versatile aircraft for special missions as well as passenger and cargo operations.

Customers/partners
Swiss Air Force, German Bundeswehr, Royal Australian Air Force, Bombardier, Dassault, Embraer, Airbus, Pilatus Aircraft, Boeing, General Electric, Northrop Grumman, Saab, Lockheed Martin, British Aerospace, Honeywell, United Technology, Rheinmetall Air Defence, Elbit

Numbers and facts

Net sales:	CHF 515 million
EBITDA:	CHF 46 million
EBIT:	CHF 39 million
Employees (FTE):	2,296
Based in:	Switzerland, Germany, USA, Australia, Malaysia, Brazil

RUAG Ammotec

The division's long-standing sales growth continued. Pressure on margins from the civil market in the United States could only be partially offset.

Business performance

In 2017 RUAG Ammotec expanded net sales by 3.1 %, from CHF 385 million to CHF 397 million. EBIT fell from CHF 31 million to CHF 28 million. The main drivers of this decline in earnings were the US business, which suffered from pressure on margins, and higher commodity prices. There were no significant one-time effects in the period.

2017 was an exceptionally difficult year for the entire ammunition industry. The civil market in the United States declined significantly after the presidential elections. In the expectation that the new US government would enact more restrictive gun laws, ammunition had been stockpiled both at every level of the retail trade and by consumers. Donald Trump's victory proved these fears groundless, and the market subsequently plummeted. Satisfyingly, however, the market position in the division's original European business continued to strengthen.

A decisive factor for the years to come will be the change in the company's leadership. On 1 October, Christoph M. Eisenhardt became the division's new CEO and joined RUAG's Group Executive Board. He took over from Cyril Kubelka, who had held the position since 2004.

In the armed forces and law enforcement sector, where RUAG Ammotec supplies precision standard and special ammunition, domestic markets were further solidified. The high level of the previous year was maintained in Germany. In Switzerland business even improved considerably despite intensifying competition. The GP11 contract from the DDPS was particularly instrumental to this pleasing development. As expected, due to export policy restrictions the export segment was unable to make any gains.

In the hunting & sport segment, where RUAG Ammotec is represented with a broad range of top brands such as RWS, norma, Rottweil and GECO, the division improved its position in the key European markets. Overall, sales increased in over two thirds of RUAG Ammotec's relevant markets. Performance was again particularly positive in Germany, where growth was well above expectations. Gains were recorded in both new products in the retail goods assortment and innovative products for the hunting & sport segment, such as the new RWS 10.3x68 Mag. calibre, or the RWS SPEED TIP PRO cartridge, which successfully diversified into the .30-calibre range.

The components business, where RUAG Ammotec is the leader in heavy metal-free ignition technologies, held steady during the year under review. In the industrial segment, including actuator cartridges for the construction industry and special applications for automotive safety systems, the division was able to sustain the sales performance of the previous year. The components business with other ammunition producers was influenced by the negative conditions in the US market and thus declined.

The hunting & sport and industrial applications segments make up 58 % of total sales, with armed forces and law enforcement accounting for 42 %.

Outlook

In order to become more robust in the face of volatilities in individual markets, RUAG Ammotec will continue to push ahead with its strategy of internationalization. Thus, in May 2017 the division gained consent for a licence to set up an ammunition production facility in Brazil. The division is currently looking into a variety of scenarios. Based on this, a decision will need to be made as to whether, how and when RUAG will put its plans into action.

In the coming years, it must be assumed that export restrictions will be extended to other markets. In the armed forces & law enforcement segment in particular, this may have negative consequences. These circumstances require the division to concentrate on further developing the home markets, in which it anticipates stable or increasing demand over the next few years, and to maintain a clear focus on Europe and other NATO countries. Lucrative individual markets will be developed as part of projects.

For the hunting & sport segment, RUAG Ammotec anticipates moderate growth, although the US business is set to remain extremely challenging with the tight margin situation. The division will continue to systematically pursue expansion in neighbouring market segments, focusing on optics and hunting & sports weapons. This should contribute positively to the result in 2018. In addition to this, the division is planning to scale up its distribution network. Despite increasing online activity, specialist retail operations remain the backbone of the hunting and sport business.

Enhanced marketing activities will be needed to defend the division's strategically important European business against the increasingly export-oriented US competition. On top of this, conditions are growing more difficult due to environmental standards and restrictions in logistics for weapons and ammunition. This could have a slight negative impact on the segment's results.

For the industrial business, the division expects a positive impetus. The priorities here are to carry over the division's unique technological capabilities to new applications and to establish further strategic partnerships.

New processes and technologies will secure RUAG Ammotec's ability to face the future. The aim is to generate the requisite investments largely from cash flow. In 2018, one focus area will be on implementing planned investments to allow the division to transact its expected medium-term business and sustainably increase its profitability.

Brief profile

RUAG Ammotec, with its Hunting & Sport and Armed Forces & Law Enforcement business units, is the European market leader in small-calibre ammunition, pyrotechnic elements and components. Its precision ammunition for special forces is in high demand worldwide. The division is also the leader in heavy-metal-free primer technologies as used in actuator cartridges in the construction industry and automotive safety system applications. The product range also includes large-calibre training systems, hand grenades and environmentally safe disposal of pyrotechnic products.

Customers/partners

Swiss Armed Forces, German Bundeswehr and other foreign armed forces, law enforcement organizations, hunters and sporting marksmen, industrial partners

Numbers and facts

Net sales:	CHF 397 million
EBITDA:	CHF 43 million
EBIT:	CHF 28 million
Employees (FTE):	2,257
Based in:	Germany, Switzerland, Hungary, Sweden, France, USA, Austria, UK, Italy, Belgium, Finland, Brazil

RUAG Defence

The division looks back on a difficult financial year. The operating result was severely hit by major domestic contracts being postponed or failing to materialize, by significant competitive pressure on the international market, by rigorous export restrictions and by cost overruns in key projects.

Business performance

In 2017 RUAG Defence generated total sales of CHF 389 million (CHF 388 million), performing well below expectations. EBIT, at CHF –3 million (CHF 24 million), fell by a massive CHF 27 million compared to the previous year.

The Defence division was confronted with numerous challenges in the 2017 financial year. The ongoing downsizing of both equipment stocks and personnel by its main customer, the Swiss Armed Forces, is leading to a decline in order volumes. In addition, a number of ongoing projects met with internal challenges during implementation, as well as substantial cost overruns. And beyond that, some business-critical major projects were postponed by the customers involved. The division has also encountered difficulties in its international target markets: the current increase in armed conflicts and the concomitant export restrictions have hampered export activities in significant sales regions. This is related to the strict Swiss export legislation to which RUAG Defence consistently adheres. As a result, RUAG Defence has had to undergo restructuring in several areas, entailing a total of 30 redundancies. Moreover, the division's CEO, Dr. Markus A. Zoller, left the company in October 2017. Andreas Berger, until then head of the NEO Services business unit, took over the role of CEO on an interim basis.

Despite this challenging environment, RUAG Defence was able to secure some major contracts in 2017 as well as reaching a number of strategic milestones. Right at the start of the year, RUAG Defence was awarded the contract for the large-scale CERBERE programme. This contract, in the field of Simulation & Training, involves modernizing the national combat training centres for the French land forces, as well as supplying the corresponding items of equipment.

In mid-May 2017, the Swiss Federal Office for Armaments (armasuisse) commissioned RUAG Defence to integrate specific technical systems into the lightweight all-terrain Mercedes Benz G300 vehicles used by the Swiss Armed Forces. Among other things, this project will involve developing and manufacturing the newly required supply and climate control components and integrating them into the new vehicles. RUAG Defence will be acting as the general contractor for this project.

In addition, the Defence division has now secured its first NATO contract. The Tactical Access Node (TAN) integrated voice and data router is being used by the multinational NATO battle group in Lithuania.

The division was also able to acquire a pioneering contract in the civil robotics field. Well-known Swiss company Boschung will be relying on RUAG Defence's system for the robotization of its snow-clearing systems for airports in future. Series production is scheduled to start as early as the end of next year.

With the completion of its acquisition of Clearswift, in early 2017 RUAG Defence substantially expanded its Cyber Security business unit. In the year under review it went on to consolidate and enhance its strategy, though with Cyber Security remaining a significant growth pillar for the Group. Moreover, from 1 January 2018 Cyber Security will be run at Group level and thus strengthened even more.

In December 2017 an agreement was reached with armasuisse to continue with the tried and tested concept of multi-year service-level agreements for the years 2018–22. These SLAs cover support and maintenance services for over 100 systems in the fields of simulation and training, combat vehicles and weapons, command and control and reconnaissance.

Outlook

After the reorganization of 2017, continuity and stability are of key importance to RUAG Defence. The priority is to consolidate what has been achieved and establish the ongoing structural and procedural adjustments on a broad basis.

RUAG Defence remains committed to its existing business strategy. Consequently, over the course of the next year the division will be focusing on strengthening its home market of Switzerland, with projects and activities with the Swiss Armed Forces taking centre stage. RUAG Defence is keen to further strengthen its position as a competent, strategic technology partner in this regard, and thus contribute to ensuring the operational readiness of the Swiss Armed Forces.

The Defence division will also be further intensifying its collaboration with civil organizations and agencies in the rescue and security fields. With modern technology solutions, RUAG Defence is in a position to help shape the future of civil operations.

Furthermore, the Defence division has stated its aim of stepping up its activities in its other home markets of Germany and France. The strategic positioning of RUAG Defence Deutschland GmbH and RUAG Defence France SAS will thus play a key role in the years ahead. The division's strategy also includes a gradual internationalization of selected areas. The emphasis here will be on supplying mature, globally marketable products and services to accessible, high-volume markets.

Brief profile

RUAG Defence develops internationally sought-after technologies for armed forces, law enforcement and rescue and security organizations. Its core business includes products and services for tracked and wheeled vehicles, realistic military training, and reliable command, information and communication infrastructures. Its comprehensive portfolio also includes protection systems to counter ballistic threats and integration, maintenance, operation and innovative upgrades to relevant systems.

Customers/partners
Swiss Armed Forces, armed forces worldwide, rescue and security agencies and organizations, operators of critical ICT infrastructure, industrial partners

Numbers and facts

Net sales:	CHF 389 million
EBITDA:	CHF 9 million
EBIT:	CHF –3 million
Employees (FTE):	1,597
Based in:	Switzerland, Germany, France, UK, United Arab Emirates, USA, Australia, Japan

Corporate responsibility

RUAG discharged its corporate responsibility with a number of different activities in 2017.

For RUAG, embracing its own corporate responsibility is a vital prerequisite for sustainable commercial success. The Group takes a very broad view of this responsibility, which encompasses all repercussions of its actions on society, its employees, the environment and the economic context. Among other things, this means that RUAG is expanding the established definition of corporate responsibility, with its three key focus areas of economic, environmental and social responsibility, by adding an ethical component.

Embracing responsibility in all areas

In its day-to-day business, RUAG has for a long time very deliberately embraced its economic, environmental, social and ethical responsibility. The year under review was no exception, as shown by a large number of activities in all four areas.

In the sphere of economic sustainability, RUAG is focusing on fair compensation and working conditions, on sustainable promotion of safety, on Diversity and Inclusion, and on strict observance of legislation and regulations. In 2017, among other things the Group systematically went about strengthening its compliance framework by creating a self-contained organizational unit and launching a multi-year Group-wide project, Integrity@RUAG.

Commitment from within

Networking for tomorrow's challenges

Commitment from the workforce is crucial to the success of the business. Established by visionary employees and operated in their spare time, Agile@RUAG aims to raise awareness of agile working methods within the Group. In 2017, the network grew from 10 to over 80 members, held a range of events and was able to establish both a core team and several product teams. A particular highlight was the big summer event, which was also attended by CEO Urs Breitmeier. The event was held in RUAG Real Estate's new "RUAG Lab" in Bern – a space for free thinking and innovation.

Into the future with full thrust

RUAG Space is making student projects fly

The ideas of young people today are the technological innovations of tomorrow. This is the conviction behind RUAG Space's efforts to help proactive students make their visions reality. The company is most notably providing support to the teams in the form of expertise and infrastructure services. RUAG Space Sweden, for example, helped out students in Gothenburg who were building a Mars Rover. And a team of 15 Swiss students participating in the Spaceport America Cup 2017 were able to benefit from the expertise of RUAG engineers every bit as much as the Academic Motorsports Club Zurich did when constructing their electric-powered racing car for the Formula Student series.

Investing in young people

In the matter of social responsibility, RUAG stands for a highly diverse workforce in respect of age, gender and nationality, for attractive education and training programmes, for work-life balance and for an effective safety and health management system.

In 2017, the Group had a total of 401 apprentices being trained in 24 different professions. RUAG's commitment to vocational training was further underscored by the Group Executive Board's decision to support the 2018 SwissSkills championships by acting as a Presenting Partner.

RUAG has been supporting ambitious apprentices within its own workforce wishing to compete nationally and even internationally with other young professionals for over ten years, in a special Swiss Selection Team. At the WorldSkills championships in Abu Dhabi, another RUAG apprentice gained a podium place in 2017. Marco Michel, of RUAG Aviation, won the silver medal in the Polymechanics and Automation category.

Supporting older people and protecting travellers

RUAG also attaches equal importance to its older employees. At the end of 2017, just under 500 of RUAG's 4,400 employees in Switzerland had been working for the company for 30 years or more, and 88 have even been with RUAG for 40 years or more. In view of this exceptional loyalty, an additional loyalty bonus for 50 or more years of service was introduced in the personnel regulations.

In the wake of the constantly increasing internationalization of its business activities, in 2017 RUAG also decided to start working with the global health care provider International SOS. This will provide business travellers and expatriates with 24/7 assistance in the event of illness, accident, civil disturbances or other incidents occurring while they are abroad.

Opportunities for all
Hearing-impaired youngster starts apprenticeship in Emmen

RUAG is wholeheartedly in favour of the dual education system, and feels that it should be open to as many enthusiastic young people as possible. For example: Toplica "Topi" Bogicevic. This summer, he began his apprenticeship with RUAG Real Estate in Emmen, working to become a building maintenance specialist. What makes the 18-year-old different from most of the apprentices at RUAG is his hearing: it is severely impaired. This has an impact above all on communication in day-to-day working life. Visual contact is important for lip-reading. In addition, and completely in keeping with the times, more text messages are being used.

CO_2 commitment already more than fulfilled

With regard to environmental responsibility, in 2017 the focus was on implementing the universal target agreement for lowering energy consumption (as per the legislation governing large-scale consumers). RUAG has made a commitment to the Swiss Federal Office for the Environment to reduce its annual CO_2 emissions from the heating installations in its Swiss buildings by 189 tonnes to 3,807 tonnes by 2020. It was able to meet this target as early as 2016, reducing its CO_2 emissions by 283 tonnes. In 2017, RUAG managed to lower its emissions still further, by approximately 300 tonnes. This was mainly due to the changeover of the dual fuel burner system in Emmen from oil to natural gas and to Group-wide awareness-raising activities on environmental topics.

RUAG Environment, with its focus on recycling activities, once again recovered and destroyed a total of around 42 tonnes of climate-damaging refrigerants from 155,000 compressor appliances in 2017. This is the equivalent of preventing 110,000 tonnes of CO_2 emissions. Overall, RUAG Environment processed 34,000 tonnes of waste electrical and electronic equipment (WEEE) from SWICO and SENS. This included around 130,000 mobile phones (17,000 kilograms). In general, the proportion of metal in WEEE is declining steadily while the proportion of plastic is growing. Overall, RUAG Environment achieved a recycling rate of 75 %.


Certificate of the Swiss Private Sector Energy Agency

Voluntary Climate Protection and Energy Efficiency

RUAG Corporate Services AG

RUAG Corporate Services AG is convinced of the need to stand up for sustainable climate protection. By voluntarily declaring its adherence to the Swiss Private Sector Energy Agency programme, **RUAG Corporate Services AG** commits to actively reducing CO_2 emissions and optimizing energy efficiency. The Swiss Federal Government, cantons and private sector partners honor the target agreement.

Dr. Armin Eberle
Swiss Private Sector Energy Agency

1st January 2017

Erich A. Kalbermatter
Swiss Private Sector Energy Agency

ENERGY AGENCY
SWISS PRIVATE SECTOR EnAW

Digital. But secure!
Committed to internet security in Switzerland

Internet security is a matter of concern not only to the government and economy, but also to every single citizen. That's why RUAG was specifically promoting the topic of ICT security at the first Swiss Digital Day. At Zurich's main station, RUAG gave interested visitors a chance to complete a short awareness training session which included a live link to its Cyber Training Range in Berne. RUAG sees these activities as helping the Swiss people, as well as managers and businesses, to navigate the internet securely.

For more transparency
Backing for report on real estate sector

With financial support from RUAG Real Estate, Transparency International Switzerland was able to prepare and publish a report entitled "Offene Türen für illegale Gelder" (Open doors for illegal funds). This report calls attention to loopholes for money laundering in Switzerland's real estate sector and proposes appropriate solutions. With this commitment, RUAG testifies to a broad understanding and clear action beyond the industrial sector.

Compliance & risk management

Integrity@RUAG, a Group-wide initiative stretching over several years, is sustainably strengthening compliance within the Group. A new Code of Conduct and accompanying training measures are helping all employees worldwide to internalize its basic values. The whistleblower desk received a total of 14 reports in 2017.

In the year under review, RUAG integrated its Risk Management and Compliance areas into a new and self-contained organizational unit reporting directly to the General Counsel. This will further strengthen both the Risk Management and Compliance functions.

As a key element in Corporate Governance, the Group-wide risk management system protects RUAG's assets, facilities and employees. Risks are identified and addressed using a broad-based methodology based on the international COSO II, ISO 31000 and DIN EN 62198 standards. Under this methodology, risks are identified, analysed and assessed twice a year in all business units in a structured process using the seven main categories of external risks, strategy, markets, processes, resources, compliance and culture, and finance. By gradually consolidating at the division and Group levels, each level of the corporation gains a management tool geared to its requirements.

Compliance as a core task

RUAG sees compliance as part of risk management, and sets an ambitious benchmark for its own actions as a Group. This goes beyond compliance with all guidelines, international agreements and domestic laws. The Group critically examines its own conduct and expects its employees, too, to behave with integrity at all times.

All senior managers, members of the Board of Directors and employees are expected to adhere to a strict policy of zero tolerance to corruption. They are forbidden from making any direct or indirect payments or granting any other advantages in order to secure advantages for themselves or the company. This specifically includes any contributions to political parties. To reinforce this commitment, RUAG joined Transparency International, the international organization leading the global fight against corruption, back in 2015.

As an enterprise owned by the Swiss Confederation, RUAG is committed to upholding particularly high ethical principles. In particular, this includes a commitment to comply with Swiss export control requirements on military equipment and dual-use goods on the part of not only its Swiss subsidiaries, but also all foreign subsidiaries. For this reason, RUAG maintains open contacts with government agencies and administrative bodies, and resolves any questions relating to exports actively with the appropriate experts in the federal administration.

Openness and transparency are also core elements of compliance, both in respect of government agencies/the public and within the company. RUAG promotes an open discussion culture with a view to learning from mistakes and thus advancing the company as a whole.

The only limits on openness and transparency are those imposed by the rules on data protection and by the discretion RUAG is bound to exercise towards business partners, employees and other stakeholders. Sensitive information is protected and handled confidentially. RUAG's employees protect all business and trade secrets of both RUAG and third parties.

Multi-year "Integrity@RUAG" project launched

In 2017, the priority for the Compliance & Risk Management area was implementing the Integrity@RUAG initiative to strengthen compliance, which was initiated in 2016. Together with representatives from all the divisions, various aspects of compliance were analysed and improved with a view to firmly establishing the new Compliance organization as a partner throughout the Group.

The basis for the compliance culture throughout the Group is laid down in the Code of Conduct, which was rewritten in 2017. Moreover, in the year under review detailed risk analyses in the areas of business ethics, corruption, third-party management and trade compliance were undertaken in all divisions. The existing processes for collaboration with external agents were refined in view of RUAG's commitment to legally faultless conduct, especially in the area of corruption. Likewise, improvements were made to RUAG's internal directives and organization.

A detailed road map for 2018 has already been drawn up: thus, within the framework of Integrity@RUAG, there are plans for further action in the areas of corruption, trade compliance, competition law, human resources and finance, on the one hand to ensure compliance and on the other to make the existing processes more efficient.

Building an effective organization

In order to give compliance deep and lasting roots, a variety of organizational measures were adopted in 2017. Effective from 1 January, the Group created new positions for a Vice President (VP) and a Senior Manager for Compliance & Risk Management and put them together in a self-contained organizational unit. The VP Compliance & Risk Management reports directly to the General Counsel. Due to the major importance of the subject matter, the CEO took on the supervision of this role on an ad interim basis over the course of the year under review while the position of General Counsel was vacant. Moreover, it was decided that in future every division will have a Compliance Officer of its own who will report to the VP Compliance & Risk Management. This is intended to ensure that every division has compliance services and processes which are geared to its specific risk position. At the same time, it will also safeguard the autonomy of the compliance function.

The long-term prioritization of the subject ensures that the VP Compliance & Risk Management will have direct access to the Board of Directors (BoD). Compliance is a standard item on the agenda of every BoD meeting. Regular updates in the responsible Audit Committee ensure a transparent flow of relevant information. In addition, specific expert groups take the topics into the divisions and in return ensure that the divisions can bring their concerns directly to the Group.

New Code of Conduct sets high standards

The reworded Code of Conduct adopted in 2017 defines RUAG's values and its requirements in terms of integrity even more precisely and serves as a compass for day-to-day conduct. The following applies to all RUAG managers and employees: We justify the trust placed in us every day, set ourselves high targets, act responsibly, hold true to our word – and follow "the 10 Golden Rules".

The 10 Golden Rules

1. We adopt an entrepreneurial mindset and act responsibly.
2. We engender trust and justify the trust that is placed in us.
3. We keep our word by saying what we do and doing what we say.
4. We act honestly, communicate openly and stand by our own behaviour.
5. We keep all business secrets that we are entrusted with.
6. We are sincere and openly communicate our mistakes. We learn from our mistakes and pass on this experience to our colleagues.
7. We address errors with our colleagues with the aim of working on correcting them together.
8. We stand out from our competitors by virtue of our performance, expertise, quality and innovation.
9. We follow the rules – including and in particular in difficult situations and market conditions.
10. We do not neglect or disregard these ground rules in the interests of securing business success.

Training employees worldwide

All around the world, in groups of 15 or 20, employees are attending face-to-face workshops to learn how to apply the new Code of Conduct in practice. The focus of these workshops is on specific case studies from the fields of corruption, dealing with donations, facilitation payments, competition law, conflicts of interest, customs and export controls, discrimination and protecting data and secrets. RUAG's Board of Directors together with its Executive Board and its top 70 managers led the way on this in 2017. Within the context of a management meeting, on 20 September they devoted an entire day to the topic of Integrity & Compliance. In the year under review, a total of around 600 RUAG employees in Switzerland, Germany, Sweden and the USA received training within a three-month period. By mid-2018 workshops will have been held in all RUAG's operating countries.

Additional strengthening of trade compliance

As an enterprise under the ownership of the Swiss Confederation, RUAG invariably bears a special responsibility – one which comes to the fore especially in cases where the Group is acting as an international supplier of military products and services. In these cases, regardless of where the relevant unit is based and from whence the goods are to be exported, the following applies: RUAG supplies military applications only in compliance with Swiss export control policy, and only to clearly identifiable counterparties. All exports of military applications are transacted in conformity with international law, Switzerland's international commitments and the principles of Swiss foreign policy. Where exports are not permitted from Switzerland, RUAG does not circumvent these restrictions by acting through foreign subsidiaries.

In 2017, coordination of trade compliance within the Group was further optimized with the creation of a central team under the VP Compliance & Risk Management. In collaboration with the relevant people in the business units, the team ensures that the rules are implemented consistently and systematically, and coordinates the work on further developing trade compliance processes and increasing their efficiency throughout the Group.

Compliance reports

An important part of RUAG's compliance organization is the whistleblower system. The system can be used not only by all employees worldwide, but also by all external partners. The system ensures that communications can be seen only by the Compliance Team and that the identity of the reporting individuals is also kept confidential. The Compliance Team investigates every report, and is also responsible for taking appropriate measures as and when required.

As well as the anonymous whistleblower system, employees and external partners also have the option to report questionable activities and situations to their line manager, the HR department, the General Counsel or the members of the Compliance Team at any time, or to send an e-mail via the general address compliance@ruag.com. In 2017 a total of 14 reports were recorded. Specific measures were taken in six of these cases.

Financial statements

Overview of key figures

in CHF m	2017	2016
Order inflow	1 961	2 036
Order backlog	1 607	1 556
Net sales	1 955	1 858
Operating income	1 990	1 882
Cost of materials and purchased services	(688)	(620)
Personnel expenses	(914)	(859)
Other operating expenses, net	(193)	(171)
Earnings before interest, taxes, depreciation and amortization (EBITDA)	196	232
EBITDA in % of net sales	10.0 %	12.5 %
Earnings before interest and taxes (EBIT)	119	151
EBIT in % of net sales	6.1 %	8.1 %
Net profit	89	116
Net profit in % of net sales	4.6 %	6.2 %
Cash flow from operating activities	88	135
Cash flow from investing activities	(146)	(79)
Free cash flow	(58)	56
Cash flow from financing activities	22	(49)
Equity attributable to the RUAG shareholder	1 007	1 005
Equity in % of total assets	51.3 %	55.4 %
Return on equity[1]	8.9 %	11.9 %
Depreciation, amortization and impairment	77	81
Research and development expenses[2]	181	171
in % of net sales	9.2 %	9.2 %
Net sales per employee (in CHF thousands)	215	218
Added value per employee (in CHF thousands)	132	134
Employees (FTE) as at 31 December incl. apprentices	9 189	8 734
Number of employees (average FTE for year, incl. apprentices)	9 083	8 543
Number of registered shares (par value CHF 1,000)	340 000	340 000
Earnings per registered share	263.11	340.95
Dividend per registered share[3]	117.65	138.24
Distribution ratio	44.7 %	40.5 %
Book value per registered share in CHF	2 963	2 957

[1] Net profit as a percentage of average equity.
[2] Comprises both self-financed and third party-financed research and development expenses.
[3] Probable dividend of CHF 40 million for 2017 according to the proposal of the Board of Directors.

Five-year overview

in CHF m	2017	2016	2015	2014	2013[3]
Order inflow	1 961	2 036	1 828	1 785	1 851
Order backlog	1 607	1 556	1 378	1 370	1 405
Net sales	1 955	1 858	1 744	1 781	1 752
Earnings before interest and taxes (EBIT)	119	151	137	113	115
EBIT in % of net sales	6.1 %	8.1 %	7.8 %	6.4 %	6.6 %
Net profit	89	116	117	84	94
Net profit in % of net sales	4.6 %	6.2 %	6.7 %	4.7 %	5.4 %
Cash flow from operating activities	88	135	145	135	142
Cash flow from investing activities	(146)	(79)	(81)	(79)	(42)
Free cash flow	(58)	56	64	57	100
Cash flow from financing activities	22	(49)	(26)	(61)	(88)
Equity attributable to the RUAG shareholder	1 007	1 005	949	882	943
Equity in % of total assets	51.3 %	55.4 %	55.2 %	51.6 %	50.5 %
Return on equity[1]	8.9 %	11.9 %	12.7 %	9.8 %	11.3 %
Research and development expenses[2]	181	171	146	140	132
in % of net sales	9.2 %	9.2 %	8.4 %	7.9 %	7.5 %
Employees (FTE) as at 31 December incl. apprentices	9 189	8 734	8 163	8 114	8 241
Number of employees (average FTE for year, incl. apprentices)	9 083	8 543	8 115	8 182	8 336

[1] Net profit as a percentage of average equity.
[2] Comprises both self-financed and third party-financed research and development expenses.
[3] According to IFRS (not adjusted as per Swiss GAAP FER).

Consolidated income statement 1 January to 31 December

in CHF m	Note	2017	2016
Net sales	6	1 955	1 858
Own work capitalized		9	4
Changes in inventories and work in progress		26	20
Operating income		1 990	1 882
Cost of materials and purchased services		(688)	(620)
Personnel expenses	7	(914)	(859)
Other operating expenses, net	8	(193)	(171)
Earnings before interest, taxes, depreciation and amortization (EBITDA)		196	232
Depreciation and impairment of property, plant and equipment/investment property	17, 18	(66)	(64)
Amortization and impairment of intangible assets	19	(11)	(17)
Earnings before interest and taxes (EBIT)		119	151
Financial income	10	2	2
Financial expenses	10	(10)	(9)
Share in income of associates	20	3	3
Earnings before taxes		114	147
Income taxes	11	(25)	(31)
Net profit		89	116
Net profit attributable to:			
Shareholders of RUAG Holding Ltd		89	114
Non-controlling interests		0	2
Net profit		89	116

The notes to the consolidated financial statements on pages 36 to 74 form an integral part of the consolidated financial statements.

Consolidated balance sheet as at 31 December

in CHF m	Note	2017	2016
Cash and cash equivalents	12	201	239
Current financial assets	13	7	4
Trade receivables	14	263	266
Prepayments to suppliers	14	17	30
Other current receivables	14	21	23
Tax assets		9	3
Prepaid expenses and accrued income		18	15
Inventories and work in progress	15, 16	717	603
Current assets		1 253	1 183
Property, plant and equipment	17	497	464
Investment property	18	84	88
Intangible assets	19	69	24
Associates	20	40	39
Non-current financial assets	13	3	3
Deferred tax assets	11	17	13
Non-current assets		710	631
Total assets		1 963	1 813
Current financial liabilities	21	56	13
Trade accounts payable	22	93	118
Prepayments from customers	22	213	182
Other current liabilities	23	40	55
Tax liabilities		20	25
Deferred income and accrued expenses	25	220	199
Current provisions	26	76	75
Current liabilities		718	666
Non-current financial liabilities	21	76	0
Other non-current financial liabilities	24	1	4
Employee benefit obligations	27	70	58
Non-current provisions	26	39	41
Deferred tax liabilities	11	47	36
Non-current liabilities		234	139
Share capital	28	340	340
Capital reserves		10	10
Retained earnings		837	795
Offsetting of goodwill		(156)	(84)
Other reserves		(9)	(12)
Foreign currency translation adjustments		(14)	(43)
Equity attributable to the RUAG shareholder		1 007	1 005
Equity attributable to non-controlling interests		4	3
Total equity		1 011	1 009
Total liabilities and equity		1 963	1 813

The notes to the consolidated financial statements on pages 36 to 74 form an integral part of the consolidated financial statements.

Consolidated statement of cash flows, 1 January to 31 December

in CHF m	Note	2017	2016
Net profit		89	116
Depreciation, amortization and impairment	17, 18, 19	77	81
Change in non-current provisions and deferred taxes		(4)	(2)
Use of non-current provisions		(3)	(7)
Share in income of associates	20	(3)	(3)
Other non-cash changes		(3)	(0)
Change in net working capital[1]		(66)	(48)
(Gain)/loss on disposal of non-current assets incl. investments		(8)	(8)
Financial income	10	(2)	(2)
Financial expenses	10	10	9
Cash flow from operating activities[2]		88	135
Capital expenditures for plant and equipment	17	(59)	(56)
Capital expenditures for property incl. investment properties	17, 18	(49)	(33)
Capital expenditures for intangible assets	19	(5)	(6)
Acquisition of subsidiaries less cash and cash equivalents acquired	4	(49)	(2)
Disposal of plant and equipment		1	1
Disposal of property incl. investment properties		12	2
Disposal of intangible assets		—	—
Disposal of investments less cash and cash equivalents disposed of	4	(1)	13
Dividends received from associates	20	3	3
Cash flow from investing activities		(146)	(79)
Free cash flow		(58)	56
Increase in financial liabilities to third parties		(1)	—
Increase in third-party financial assets		122	0
Repayment of financial liabilities to third parties		(49)	(0)
Finance lease payments		(0)	(1)
Financial income received		2	2
Financial expenses paid		(4)	(3)
Dividends paid to shareholders		(47)	(47)
Cash flow from financing activities		22	(49)
Change in cash and cash equivalents before foreign currency translation adjustments		(36)	7
Cash and cash equivalents at beginning of period		239	233
Foreign currency translation adjustments in respect of cash and cash equivalents		(2)	(1)
Cash and cash equivalents at end of period		201	239

[1] Excludes current financial assets, current financial liabilities and other non-current liabilities.
[2] Including income taxes of CHF 19 million paid in the year under review (previous year: CHF 22 million).

The notes to the consolidated financial statements on pages 36 to 74 form an integral part of the consolidated financial statements.

Consolidated statement of changes in equity

in CHF m	Share capital	Capital reserves	Retained earnings	Offsetting of goodwill	Other reserves	Foreign currency translation adjustments	Attributable to the RUAG shareholder	Attributable to non-controlling interests	Total equity
Balance as at 1 January 2016	340	10	727	(83)	(6)	(39)	949	2	951
Net profit	—	—	114	—	—	—	114	2	116
Goodwill offset against equity	—	—	—	(1)	—	—	(1)	—	(1)
Change in fair value of cash flow hedges	—	—	—	—	(8)	—	(8)	—	(8)
Gains and losses from cash flow hedges transferred to profit or loss	—	—	—	—	2	—	2	—	2
Foreign currency translation adjustments of foreign subsidiaries	—	—	—	—	—	(4)	(4)	(0)	(4)
Dividends paid	—	—	(47)	—	—	—	(47)	—	(47)
Balance as at 31 December 2016	340	10	795	(84)	(12)	(43)	1 005	3	1 009
Balance as at 1 January 2017	340	10	795	(84)	(12)	(43)	1 005	3	1 009
Net profit	—	—	89	—	—	—	89	0	89
Goodwill offset against equity	—	—	—	(72)	—	—	(72)	—	(72)
Change in fair value of cash flow hedges	—	—	—	—	5	—	5	—	5
Gains and losses from cash flow hedges transferred to profit or loss	—	—	—	—	(1)	—	(1)	—	(1)
Foreign currency translation adjustments of foreign subsidiaries	—	—	—	—	—	29	29	0	29
Dividends paid	—	—	(47)	—	—	—	(47)	—	(47)
Balance as at 31 December 2017	340	10	837	(156)	(9)	(14)	1 007	4	1 011

As at 31 December 2017, the amount of non-distributable statutory reserves was CHF 47 million (previous year: CHF 42 million).

In the year under review, a dividend of CHF 47 million (previous year: CHF 47 million) was paid to the shareholder from the previous year's result. This is equivalent to a dividend per share of CHF 138.24 (previous year: CHF 138.24).

The notes to the consolidated financial statements on pages 36 to 74 form an integral part of the consolidated financial statements.

This financial report is a translation of the original German version. In case of any inconsistency the German version shall prevail.

1 General information: Business activities and relationship with the Swiss Confederation

RUAG Holding Ltd is a Swiss joint-stock company headquartered in Bern. It is wholly owned by the Swiss Confederation. RUAG Holding Ltd and its subsidiary companies (hereinafter referred to as "RUAG") focus on their core aerospace and defence businesses with goods and services in the military and civilian sectors and on the development of international growth markets. RUAG is bound by the owner's strategy of the Swiss Federal Council and its fundamental mission is to equip and maintain the technical systems of the Swiss Armed Forces.

Relationship with the Swiss Confederation

The Swiss Confederation is the sole shareholder of RUAG Holding Ltd. Under the terms of the Federal Act on State-Owned Defence Companies, any disposal of the capital or voting majority of the Swiss Confederation to third parties requires the approval of the Federal Assembly. As sole shareholder, the Confederation exercises control over all decisions taken at the General Meeting, including the election and remuneration of members of the Board of Directors and dividend resolutions. Details of transactions with the Swiss Confederation are given in Note 33.

2 Summary of significant accounting policies

2.1 Basis of preparation

RUAG's consolidated financial statements have been prepared in accordance with the guidelines of the Swiss Accounting and Reporting Recommendations (Swiss GAAP FER). Certain provisions of Swiss GAAP FER 31 "Additional recommendations for listed companies" have also been applied. These provisions contain recommendations regarding discontinued operations, income tax, financial liabilities and segment reporting. Furthermore, the provisions of Swiss company law have been fulfilled. The reporting period covers twelve months. The consolidated financial statements are presented in Swiss francs (CHF). The balance sheet is structured according to maturities.

Current assets include assets that

- are realized within 12 months after the balance-sheet date, or are sold, consumed or realized as part of operational activities, or that
- are held for trading purposes, as well as
- cash and cash equivalents.

All other assets are non-current assets.

Current liabilities include liabilities that must be settled

- within 12 months after the balance-sheet date, or for which a
- cash outflow is probable within the scope of operational activities, or
- if they are held for trading purposes.

All other liabilities are non-current liabilities.

The income statement is prepared using the total cost method.

Items are measured at historical cost, unless a recommendation requires a different valuation basis for a line item.

Preparation of the consolidated financial statements in accordance with the Swiss GAAP FER recommendations to some extent requires the use of estimates and assumptions. These have an impact on the recognized assets and liabilities, the application of accounting policies, the disclosure of contingent assets and liabilities at the end of the reporting period and the reporting of income and expenses during the reporting period. Even though these estimates and assumptions are based on the most recent knowledge of the management regarding current developments and events, the actual results may differ. Exceptionally complex areas, or areas where more extensive use of estimates and assumptions is necessary or where assumptions and estimates have a material impact on the consolidated financial statements, are presented in Note 3.

Unless otherwise indicated, all amounts are in millions of Swiss francs. Please note that the use of rounded figures and percentages may result in differences due to commercial rounding.

2.2 Definition of non-Swiss GAAP FER-compliant figures

The operating income sub-total shown separately on the income statement contains all operating income, own work capitalized less changes in inventories and work in progress.

The free cash flow comprises the cash flow from operating activities and the cash flow from investing activities and is shown separately in the statement of cash flows.

Both figures are key performance indicators for RUAG and are therefore shown separately.

2.3 Principles and scope of consolidation

RUAG's annual consolidated financial statements include subsidiaries where RUAG Holding Ltd is effectively able to control the financial and operating policies. For control to exist, the investor must have power, exposure or rights to variable returns and the ability to combine those requirements, that is the ability to use its power to affect the variable returns. This is usually the case if RUAG directly or indirectly holds the majority of the voting power or the potential voting rights of the entity. The assets, liabilities, equity, income and expenses of fully consolidated subsidiary companies are included in their entirety in the consolidated financial statements. Non-controlling interests in equity and net profit are stated separately. Subsidiaries and associates are consolidated with effect from the date of their acquisition, and eliminated from the consolidated financial statements in the event of a loss of control. Changes to investments in subsidiary companies are recognized as equity transactions insofar as these subsidiary companies were previously controlled and continue to be controlled. All intra-Group receivables, liabilities, expenses and income, as well as unrealized intercompany profits, are fully eliminated on consolidation.

All subsidiaries included in the consolidated financial statements have 31 December as their reporting date.

Associates where RUAG exerts a significant influence (normally 20–50 % of the voting rights are held directly or indirectly), but which the Group does not control, are recognized using the equity method. An equity investment is initially recorded at fair value. When measured subsequently, the carrying amount of the investment is adjusted to take account of the share of profit or loss less the share of the profit distribution. These investments are reported under "Associates".

Investments where RUAG does not exercise significant influence (less than 20 % of the voting rights are held directly or indirectly) are stated at historical cost less any valuation allowances and shown under "Non-current financial assets".

An overview of all significant subsidiaries, associates and non-controlling interests is provided in Note 37.

2.4 Foreign currency translation
RUAG Holding Ltd's consolidated financial statements are presented in Swiss francs (CHF), the functional currency of RUAG Holding Ltd.

Transactions in foreign currencies are translated into the functional currency of the Group companies at the exchange rate at the transaction date. At the end of the reporting period, foreign-currency receivables and liabilities (monetary items) are translated at the exchange rate at the end of the reporting period, while non-monetary items measured at fair value or cost in a foreign currency are translated into the functional currency at the rate at the date of the fair value measurement or the rate at the transaction date. The resulting exchange differences are recognized in profit or loss, with the exception of exchange differences arising from effective cash flow hedges or net investments in foreign subsidiaries, which are recognized directly in equity.

The assets and liabilities of subsidiaries and associates recognized using the equity method whose functional currency is not the Swiss franc are translated into Swiss francs on consolidation at the exchange rate applicable at the end of the reporting period. The income statement, cash flow statements and other fluctuating items are translated at the average exchange rate for the reporting period. Exchange differences arising from the conversion of the annual statements of subsidiaries or affiliates are recognized directly in consolidated equity and reported separately as cumulative foreign currency translation adjustments. In the event of the disposal (to the extent that this leads to the loss of control or significant influence) of a foreign subsidiary or associate, the cumulative foreign currency translation adjustments previously recognized in equity are transferred to the income statement as a component of the gain or loss on disposals.

Differences arising in the reporting period on translation of equity and non-current intra-Group financial transactions related to net investments in foreign operations, in addition to retained earnings and other equity items, are recognized immediately in the cumulative foreign currency translation adjustments in equity.

In these consolidated financial statements, the significant currencies were translated at the following rates in the reporting periods:

Exchange rates

Currency		Annual average 2017	End-of-year rate 2017	Annual average 2016	End-of-year rate 2016	Annual average 2015	End-of-year rate 2015
Euro	EUR	1.11	1.17	1.09	1.07	1.07	1.08
Swedish krona	SEK	11.53	11.89	11.52	11.22	11.42	11.79
US dollar	USD	0.98	0.98	0.99	1.02	0.96	0.99
Pound sterling	GBP	1.27	1.32	1.34	1.25	1.47	1.47
Hungarian forint	HUF	0.36	0.38	0.35	0.35	0.34	0.34

2.5 Cash and cash equivalents
Cash and cash equivalents comprise cash and the balances in postal checking and demand deposit accounts with financial institutions. They also include term deposits held with financial institutions and short-term money market investments that have a remaining term of no more than three months on initial recognition. This definition is also used for the statement of cash flows. Cash and cash equivalents are recognized at amortized cost.

2.6 Current financial assets
Current financial assets comprise term deposits held with financial institutions and short-term money market investments that are held for trading or due within one year.

2.7 Receivables and prepayments
Trade receivables and prepayments are recognized at amortized cost less valuation allowances for doubtful receivables. The valuation allowances are estimated on the basis of an analysis of the actual exposure to losses from receivables outstanding at the end of the reporting period. The valuation allowances comprise specific valuation allowances for specifically identified items where there is objective evidence that the outstanding amount will not be received in full, and global valuation allowances. The global valuation allowances are based on historical experience. Receivables and prepayments judged to be recoverable are charged to profit or loss as "Other operating expenses".

2.8 Inventories and work in progress
Inventories and work in progress are measured at the lower of cost and net realizable value. Cost comprises all costs of purchase and conversion, including pro rata production overheads. All foreseeable exposures to loss from work in progress are accounted for by recognizing economically reasonable valuation allowances. Inventories are valued using the weighted average method or standard cost accounting. The standard costs that are determined are regularly monitored and, if any major discrepancies are observed, adjusted to the latest conditions. Impairment losses are reported for hard-to-sell or slow-moving inventories. Non-saleable inventories are written off in full.

Long-term construction and service contracts are measured according to the percentage of completion method. When the conditions are satisfied, work in progress and sales are recognized by reference to the stage of completion. Long-term construction contracts are defined as manufacturing or service orders where completion of the order extends over a longer period, calculated from the time the order is awarded to the time it is essentially completed.

The stage of completion is derived from the relationship between the costs incurred by the order and the overall estimated cost of the order (cost-to-cost method). Losses from long-term construction and service contracts are recognized immediately and in full in the financial year in which the losses are identified, irrespective of the stage of completion. Order costs and pro rata profits from long-term construction and service contracts which are measured using the percentage of completion method are shown as work in progress (percentage of completion) as a component of inventories and work in progress. They are stated at cost plus a pro rata profit that corresponds to the stage of completion achieved.

In the Space segment, mainly the milestone method is applied. Here, project milestones are defined on the basis of individual customer contracts; upon reaching these milestones, services performed are invoiced to the customer and sales and income are realized on a pro rata basis.

If the outcome of long-term construction and service contracts cannot be estimated reliably, sales are only recognized to the extent of contract costs incurred that are likely to be recoverable (recoverable cost method). Contract costs are recognized when incurred unless they give rise to an asset that is linked to the future activity on the contract. Any expected loss on a contract is expensed immediately.

Semi-finished products and services in progress are stated under "Inventories and work in progress".

Sales from services provided are recognized in the income statement on the basis of the stage of completion at the end of the reporting period.

2.9 Property, plant and equipment
Property, plant and equipment is recognized at cost less accumulated depreciation and impairment. Repair and maintenance costs are stated as an expense. Major renovations and other value enhancing costs are capitalized and depreciated over their estimated useful life. The carrying amount of the replaced parts is derecognized. Items are depreciated on a straight-line basis, with the exception of land, which is not depreciated and is recognized at cost.

The estimated useful lives for the main classes of property, plant and equipment are:

Class	Useful life in years
Plant and equipment	5 to 12
Fixtures and fittings	10
Information technology	3 to 5
Motor vehicles	5 to 10
Aircraft	10 to 15
Buildings (operating properties)	20 to 60

The useful lives are reviewed at least once a year at the end of the reporting period and adjusted where necessary.

2.10 Government grants
Government grants related to assets are recognized in the balance sheet at fair value as deferred income. Government grants are then recognized in profit or loss as other income on a straight-line basis over the useful life of the assets.

2.11 Leases
Leased assets where the benefits and risk arising from ownership are essentially transferred to RUAG are recognized at the lower of fair value of the leased asset and present value of the minimum lease payments on inception of the lease. Correspondingly, the estimated net present value of future, non-cancellable lease payments is carried under liabilities from finance leases. Assets under finance leases are amortized on a straight-line basis over the shorter of their estimated useful life or the duration of the lease. All other lease transactions are classified as operating leases.

2.12 Investment property
Investment properties are measured at cost minus accumulated depreciation and impairment calculated on a straight-line basis. Repair and maintenance costs are stated as an expense. Major renovations and other value enhancing costs are capitalized and depreciated over their estimated useful life. Investment properties are depreciated on a straight-line basis over a useful life of 40 to 60 years with the exception of land, which is not depreciated and is recognized at cost.

Sites that are majority-leased to third parties are classified as investment properties. The fair value of the properties is calculated solely for disclosure reasons and was measured using the discounted cash flow (DCF) method. No expert market appraisal was carried out in the reporting period.

2.13 Intangible assets and goodwill
Intangible assets have a finite useful life and are recognized at cost less accumulated amortization and impairment. Intangible assets acquired separately in business combinations are recognized at their acquisition-date fair value less amortization and impairment.

Items are amortized on a straight-line basis over the following estimated useful lives:

Class	Useful life in years
Patents and developments	5 to 15
Trademarks and prototypes	3 to 8
ERP systems	3 to 5
Licences and rights	1 to 10
Order backlog and customer relationships	1 to 10

The useful lives are reviewed at least once a year at the end of the reporting period and adjusted where necessary.

Business combinations are accounted for using the acquisition method. The cost is recognized at the fair value of the consideration at the transaction date. Identifiable assets acquired and liabilities and contingent liabilities assumed are recognized in the balance sheet at their acquisition-date fair value, irrespective of the extent of any non-controlling interest. Transaction costs are recognized as expenses in profit or loss. The acquisition costs exceeding the net assets recognized at fair value (goodwill) are offset against equity at the time of acquisition. If the purchase price contains elements that depend on future events, these are estimated and recognized as accurately as possible at the time of acquisition. If, when the purchase price is definitively calculated at a later date, there are any differences, the effect is recognized in the income statement under “Other operating expenses, net”. The impact of the goodwill being theoretically capitalized (acquisition cost, residual value, useful life, amortization) and any potential impairment are shown in the notes. Any negative difference is recognized directly in profit or loss after being reviewed. In the event of a company being sold, the goodwill previously recorded under equity will be booked out and then recognized in the income statement as a component of the gain or loss on disposals.

2.14 Research and development expenses
Research expenses are not capitalized and are expensed as incurred. RUAG examines the capitalization of development costs on a case-by-case basis. Development costs are only recognized as intangible assets if an intangible asset is identifiable, the entity believes it can demonstrate the technical feasibility and ability to complete and use the asset, the asset is expected to generate future economic benefits and the cost of the asset can be reliably determined. Capitalized development costs are measured at cost less accumulated amortization and accumulated impairment losses.

2.15 Impairment

Impairment of property, plant and equipment and intangible assets The recoverable amount of property, plant and equipment, intangible assets and the goodwill recognized and disclosed in the notes is reviewed whenever changes in circumstances or events indicate that the carrying amount may be overestimated. Where there is an indication of a possible overestimate, the Group measures fair value on the basis of expected future cash flows from use and eventual sale, minus any cost of disposal. Where the carrying amount exceeds the higher of fair value less costs to sell and value in use, an impairment loss equivalent to the difference is recorded (this does not apply to goodwill). As goodwill is offset against equity at the time of acquisition, any impairment of the goodwill is not charged to the income statement, but is only disclosed in the notes. The impairment assessment is based on the smallest group of assets for which independent cash generating units are identifiable. The estimation of future discounted cash flows is based on the forecasts and assumptions of the management. Accordingly, the actual cash flows generated may differ significantly from these estimates.

2.16 Financial liabilities
Financial liabilities are initially recognized at fair value less direct transaction costs and subsequently measured at amortized cost using the effective interest method.

2.17 Trade accounts payable and prepayments
Trade accounts payable are recognized at amortized cost. Prepayments are measured at amortized cost using the effective interest method.

2.18 Deferred income and accrued expenses
Deferred income and accrued expenses contain expenses incurred during the reporting period for which supplier invoices are yet to be received. They also include income and bonuses received in advance that relate to future periods.

2.19 Provisions
Provisions are recognized where:
- RUAG has a present legal or constructive obligation due to a past event;
- it is likely that an outflow of resources embodying economic benefits will be required to settle the liability; and
- a reliable estimate can be made of the amount of the liability.

Provisions are discounted if the effect of discounting is material.

Provisions for restructuring Costs arising in connection with restructurings are treated as an expense when management has decided on a programme from which a probable liability has arisen and the amount of this liability can be estimated reliably. So that provisions can be made for the cost of redundancy plans, the applicable terms and the number of employees affected must be defined and the employees or their representatives must be given sufficiently detailed information about the redundancy plans.

Provisions for contract losses Losses arising from long-term construction and service contracts are recorded immediately and in full in the financial year in which the losses are identified.

Provisions for warranties Provisions for warranties are recognized based on the sales revenue to which warranty obligations relate and the goods and services provided in the past.

Provisions for leave and overtime credits Employees' entitlements to leave and overtime credits are calculated at the end of the reporting period and accounted for on an accrual basis.

2.20 Employee benefit obligations
In accordance with the corresponding national provisions, RUAG offers pension plans for its employees. These are primarily institutions and foundations that are financially independent from the Group. They are usually financed via employee and employer contributions.

The economic impacts of the pension plans are assessed on an annual basis. Any excesses/shortfalls are determined on the basis of the annual financial statements of the corresponding pension funds; such calculations are based on Swiss GAAP FER 26 (Swiss plans) and the applicable country-specific methods (foreign plans).

An economic benefit is only capitalized if this is permitted and where the intention is
- to use the excess to reduce employer contributions;
- to refund it to the employer in line with local legislation; or
- to use it in another way that would economically benefit the employer outside of the benefits in line with the regulations.

An economic liability is recognized if the conditions for creating a provision are met under Swiss GAAP FER 23. This is recognized under employee benefit obligations.

Changes to an economic benefit or liability are recognized in the income statement in the same way as for the contributions made for the period. Any impact on income of foreign pension plans resulting from a change in the discount rate that is reflected in the pension fund's liabilities being discounted/compounded is recognized and shown in net interest/financial result. Changes to pension entitlements additionally earned during the period in question (service costs), impacts on income resulting from changes in commitments (benefits defined in the regulations) and effects from actual changes in the insured group or from changed assumptions regarding salary/pension trends as well as biometric assumptions are recorded in the operating result under personnel expenses.

2.21 Other long-term employee benefits
Other long-term employee benefits include long-service awards. These are calculated using the projected unit credit method and are reported in the item "Provisions for loyalty bonuses and anniversary benefits".

2.22 Current and deferred income taxes
Income taxes include all current and deferred taxes which are based on income. They are recognized in profit or loss except to the extent that they relate to a business combination or to an item recognized directly in equity. Taxes which are not based on income, such as taxes on real estate and capital, are recognized under "Other operating expenses".

Current income taxes comprise the taxes expected to be payable in respect of taxable income, calculated at the tax rates that are applicable or are announced as at the balance-sheet date, and any adjustments to the tax liability in respect of prior periods.

Deferred taxes are recognized for temporary differences between the carrying amounts of assets and liabilities in the consolidated financial statements and their tax base. Deferred taxes are not recognized for:
- temporary differences when recognizing assets and liabilities for the first time in relation to transactions that do not impact net profit or taxable income; and
- temporary differences in relation to stakes in subsidiaries and associates, provided the Group is able to control the period of time over which these differences will be reversed and it is likely that they will not be reversed in the foreseeable future.

Deferred taxes are measured taking into account when and how the assets concerned are expected to be realized or settled. In this regard, tax rates apply that are applicable or are announced as at the balance-sheet date. Deferred taxes are included in non-current assets (deferred tax assets) or non-current liabilities (deferred tax liabilities) and are offset if certain conditions are met. Deferred tax assets for unused tax losses and deductible temporary differences are recognized to the extent that there are likely to be future profits against which they can be used. The tax rates are based on the actual tax rates and the tax rates expected to apply at the legal entities in question.

2.23 Equity

Share capital The share capital is the nominal capital comprising all registered shares that have been issued.

Capital reserves This item consists of the capital paid in over and above the par value (less transaction costs).

Retained earnings Retained earnings primarily include the subsidiaries' accumulated earnings that were not distributed to shareholders. The appropriation of available earnings is subject to local legal restrictions.

Offsetting of goodwill This item consists of the goodwill from acquisitions that is offset directly against equity at the time of acquisition.

Other reserves Other reserves primarily comprise the effective portion of the cumulative net changes in the fair value of hedging instruments used to hedge cash flows.

Foreign currency translation adjustments This item consists of the difference that arises when assets, liabilities, income and expenses of subsidiaries whose functional currency is not the Swiss franc are translated into Swiss francs.

2.24 Net sales

Net sales include the fair value of the consideration received from the sale of goods and the rendering of services by RUAG in its ordinary business operations. The amount is shown after any deductions for value added tax, price reductions, rebates and discounts and intra-Group sales. RUAG records its sales when the amounts can be measured reliably, future cash flows are likely and the specific criteria described below have been fulfilled.

Long-term contracts Net sales for the period comprise "invoiced sales" plus "change in contracts under the percentage of completion method". "Invoiced sales" comprise accrued or invoiced amounts for goods and services already provided in the period, while "change in contracts under the percentage of completion method" includes the goods and services already provided under current construction and service contracts and measured using the percentage of completion method.

Sale of goods Sales from the sale of goods are stated at the time of delivery or performance, i.e. when the relevant significant risks and rewards of ownership are transferred to the buyer.

Rendering of services Sales from the rendering of services are determined on the basis of either time and material or a fixed price contract.

Sales from fixed price agreements are measured using the percentage of completion method when both the full costs incurred up to completion of the order and the stage of completion at the end of the reporting period can be reliably determined. The stage of completion is derived from the relationship between contract costs incurred and the total estimated cost of the order (cost-to-cost method) or using the milestone method (Space segment). If the proceeds of a construction contract cannot be reliably measured, sales are recognized only to the extent of the potentially recoverable costs incurred by the contract recognized as an expense in the relevant period. Contributions from third parties arising from contract development work are recognized as sales and assigned to the period in which the corresponding development costs are incurred.

Other income Other income, such as rental income and interest income, is stated on a time-proportionate basis. Dividend income is recognized once legal entitlement to payment has arisen.

Advance payments received Advance payments received are deferred and then recognized as sales when the corresponding services are provided.

2.25 Segment information

Reportable operating segments are determined on the basis of the management approach. External segment reporting is then carried out in accordance with RUAG's organizational and management structure as well as internal financial reporting to RUAG's Chief Operating Decision Maker, the CEO. Reporting is broken down according to the "Space", "Aerostructures", "Aviation", "Ammotec" and "Defence" segments. In addition, "Services" – comprising central services such as IT and real estate management, as well as RUAG's corporate units – is presented as a separate segment. Unrealized gains or losses may be incurred as a result of services or disposal of assets between the individual segments. They are eliminated and stated in segment information, in the "Elimination" column. The segment assets contain all the assets required for operations that can be assigned to a specific operating segment. The segment assets primarily comprise receivables, inventories, property, plant and equipment and intangible assets. The segment investments contain additions to property, plant and equipment and other intangible assets.

Space segment RUAG Space is the largest independent aerospace supplier in Europe and is also on track for growth in the USA. With 14 production sites in six countries, the division specializes in components for use aboard satellites and launch vehicles. It is split into three areas, which also represent the most important sources of income: electronics for all space applications, mechanical products for satellites, and structures and separation systems for launch vehicles.

Aerostructures segment RUAG Aerostructures is a globally active tier 1 supplier manufacturing aircraft for civilian and military customers. Key activities include the development, production and final assembly of complete fuselage sections, wing and control surface components as well as sophisticated component assemblies and parts for civil and military aircraft. One of the division's strengths lies in managing complex supply chain networks. Among other things, it is responsible for the complete global fuselage section supply chains for Airbus and Bombardier. The main sources of earnings are the sale of aerostructures and of complex assemblies and components.

Aviation segment RUAG Aviation is a leading supplier, support provider and integrator of systems and components for civil and military aviation. Servicing aircraft and helicopters throughout their entire life cycle, the company's core competencies include maintenance, repair and overhaul services, upgrades, and the development, manufacturing and integration of subsystems. The main sources of earnings are maintenance and life extension services as well as the sale of systems and subsystems.

Ammotec segment With its Hunting & Sports and Armed Forces & Law Enforcement business units, RUAG Ammotec is the European market leader in small-calibre ammunition, pyrotechnic elements and components. Its precision ammunition for special forces is in high demand worldwide. The division is also the leader in heavy-metal-free primer technologies as used in actuator cartridges in the construction industry and automotive safety system applications. The product range also includes large-calibre training systems, hand grenades and environmentally safe disposal of pyrotechnic products. The main sources of earnings are the sale of ammunition as well as the components business for industrial purposes.

Defence segment RUAG Defence develops internationally sought-after technologies for armed forces, law enforcement and rescue and security organizations. Its core business includes products and services for tracked and wheeled vehicles, realistic military training, and reliable command, information and communication infrastructures. The division supports operators of critical ICT infrastructures with state-of-the-art cyber-security solutions. Its comprehensive portfolio also includes protection systems to counter ballistic threats and integration, maintenance, operation and innovative upgrades to relevant systems. The main sources of earnings are the sale of corresponding products as well as servicing and maintenance services.

2.26 Related party transactions

RUAG provides maintenance services and produces defence equipment for the Swiss Federal Department of Defence, Civil Protection and Sport (DDPS), and procures services from the same. The DDPS is RUAG's largest customer. The procurement contracts awarded by the DDPS for defence products and services are subject to civil law. The process of awarding such contracts is subject to the Swiss Confederation's provisions regarding public procurement. These provisions apply to all suppliers of goods and services, and are based on the principle of free competition.

2.27 Derivative financial and hedging instruments

Derivative financial instruments are measured at fair value. The way in which the gain or loss is measured depends on whether the instrument is used for the purpose of hedging a specific risk and the conditions for hedge accounting are met. The objective of hedge accounting is to ensure the change in value of the hedged item and hedge instrument is included in the income statement at the same time.

When concluding a hedge transaction, the Group documents the relationship between hedging instruments and hedged items, as well as the purpose and strategy of the hedge. The process also involves linking all hedging derivatives with specific assets and liabilities, or firm commitments and forecasted transactions. At inception as well as during the life of the hedge, the Group documents the extent to which the derivatives used for the hedge offset the change in fair value of the hedged item. When a contract is concluded, a derivative instrument is defined as

- a hedge on the change in the fair value of a recorded asset or a liability (fair value hedge), or as
- a hedge on cash flows from a forecasted transaction or firm commitment (cash flow hedge), or as
- a hedge on a net investment in a foreign operation.

Changes in the fair value of foreign exchange hedging instruments that are used to hedge the cash flows from a forecasted transaction or firm commitment and that offer an effective hedge are recognized as cash flow hedges. These instruments are measured at fair value; the effective portion of the change in fair value of the foreign exchange hedging instrument is recognized in equity and separately disclosed under "Other reserves". The ineffective portion is recognized in profit or loss in the income statement under "Other operating expenses". Upon occurrence of the underlying transaction, the relevant hedging instrument is reclassified from equity to the income statement. Commodity price hedging instruments are disclosed in the notes but are not recognized in the balance sheet.

Currently, RUAG has only hedges on cash flows from forecasted transactions or firm commitments (cash flow hedge).

3 Significant judgements and sources of estimation uncertainty in the application of the accounting policies

The preparation of the consolidated financial statements depends on assumptions and estimates associated with the accounting policies where there is a certain amount of scope for the use of management judgement. The application of accounting policies in the consolidated financial statements requires certain forward-looking estimates and assumptions to be made that may have a significant effect on the reported amounts of assets, liabilities, income and expenses and the related disclosures. The estimates and assumptions used in recognition and measurement are based on historical experience and other factors that are believed to be reasonable under the circumstances. The following items involve significant estimates and assumptions:

Inventories and work in progress The current value of inventories and work in progress is reassessed periodically. This involves classifying the individual items in terms of inventory sales ratios and valuing them accordingly. The carrying amount of inventories and work in progress as well as valuation allowances are explained in Note 15 "Inventories and work in progress".

Long-term construction and service contracts and manufacturing agreements Estimates with a significant effect are used as the basis for the measurement of long-term construction and service contracts using the percentage of completion method. Although the estimates, such as the projects' stage of completion and estimated contract costs, are made to the best of management's knowledge about current events and possible future measures, actual outcomes may ultimately differ from these estimates. Please also refer to the explanations in Note 16 "Percentage of completion" and Note 26 "Provisions".

Property, plant and equipment and intangible assets Property, plant and equipment and intangible assets are reviewed annually for indications of impairment. If there are indications that these assets are overvalued, an estimate is made of the future cash flows expected to result from the utilization of these assets or their possible disposal. Actual cash flows may differ from the discounted future cash flows based on these estimates. Factors such as changes in the planned use of property, plant and equipment, site closures, technical obsolescence or lower-than-forecasted sales of products, the rights to which have been recognized, may shorten the estimated useful life or result in impairment. The carrying values of property, plant and equipment and intangible assets are disclosed in Note 17 "Property, plant and equipment", Note 18 "Investment properties" and Note 19 "Intangible assets".

Provisions As part of their ordinary business operations, Group companies are exposed to various risks. These are continuously assessed and provisions are set aside accordingly in light of the available information on the basis of the cash flows that can realistically be expected. For example, provisions for warranties are determined on the basis of empirical values and provisions for litigation by means of a legal assessment. The carrying values of such provisions are disclosed in Note 26 "Provisions".

Deferred income taxes Deferred tax assets are recognized based on management's judgement. Deferred tax assets are only recognized for tax loss carryforwards if it is probable that they can be used. Their use depends on the ability to generate future taxable profits that can be offset against existing loss carryforwards. An assessment as to the probability of their future use requires estimates of various factors such as future earnings. If actual amounts differ from the estimates, this may result in a change in the assessment of the deferred tax assets' recoverability. The carrying values of current and deferred tax assets and liabilities are disclosed in the consolidated balance sheet and Note 11 "Income taxes".

4 Acquisitions, mergers, formations and disposals of companies

Acquisitions, mergers and formations of subsidiaries

RUAG Ammotec Italia s.r.l. (previously Turfer di Turelli Luca & C. SRL) As of 1 January 2017, RUAG Ammotec Deutschland GmbH acquired 100 % of the shares of Turfer di Turelli Luca & C. SRL, domiciled in Brescia (Italy). The company operates in Italy as a wholesaler of hunting and sports weapons, ammunition and accessories. This acquisition will help RUAG strengthen and further consolidate its own European wholesale business. RUAG Ammotec Italia s.r.l. was fully consolidated as of 1 January 2017.

Clearswift As of 20 January 2017, RUAG Holding Ltd acquired 100 % of the shares of Clearswift, headquartered in Reading (UK). The cyber-security company provides proprietary solutions in the areas of data loss prevention and deep content inspection. Clearswift has a high-performance research and development department, a global service organization and internationally established sales channels. This acquisition will help accelerate the expansion of RUAG's Cyber Security business unit. Clearswift was fully consolidated as of 1 February 2017.

Gyttorp As of 31 March 2017, Norma Precision AB acquired the remaining 60 % of the outstanding shares of Gyttorp AB, headquartered in Ingelstad (Sweden). Gyttorp AB combines the wholesale activities of Gyttorp Jakt AB (Sweden) and Gyttorp Finland Oy (Finland), while Gyttorp Cartridge Company AB (Sweden) manufactures market-leading shotgun cartridges under the Gyttorp brand for the Swedish, Norwegian and Finnish market. The complete acquisition of Gyttorp represents another step towards strengthening RUAG's wholesale activities and supplementing the product portfolio with market-leading brands. Gyttorp's activities were fully consolidated as of the acquisition date (1 April 2017). The non-controlling interest in Gyttorp AB was recognized at cost until 31 March 2017.

HTS Hoch Technologie Systeme GmbH As at 31 May 2016, RUAG Deutschland GmbH acquired the remaining 75.4 % of the outstanding shares of HTS Hoch Technologie Systeme GmbH, headquartered in Coswig (Germany). The purpose of the company is the development and manufacture of customer-specific mechanical products for the aerospace industry. This full takeover will ensure RUAG Space has better access to the German aerospace market.

Acquisitions of non-controlling interests On 4 February 2016, RUAG Switzerland Ltd, together with the Netherlands-based VDL Group, founded a joint venture called VDL-RUAG Shelters B.V., headquartered in Eindhoven, for the production and subsequent maintenance of command and control containers for the Netherlands army. This involved forming a private limited company (B.V.), of which RUAG owns 40 %. Production is set to take place between 2018 and 2022, with the joint venture then ensuring the equipment will be maintained after this date. In the year under review, the joint venture did not have any significant activities.

Mergers On 14 August 2017, Glückauf-Logistik GmbH, headquartered in Kassel (Germany), was merged retroactively as of 1 January 2017 with RUAG Defence Deutschland GmbH, headquartered in Wedel (Germany). This merger has no impact on RUAG's consolidated financial statements.

On 19 August 2016, Herkules Fahrzeuglogistik GmbH was retroactively merged with Glückauf-Logistik GmbH, headquartered in Kassel (Germany), with effect from 1 January 2016. This merger had no impact on the consolidated financial statements of RUAG.

Formations On 5 March 2016, RUAG Aerostructures Hungary Zrt., headquartered in Eger (Hungary), was founded. The company will be used as an extended workbench for the Aerostructures division. The Eger site manufactures subassemblies, which are then delivered to RUAG Aerospace Structures GmbH in Germany for further processing. A shared-service approach is being implemented in the areas of payroll, financial accounting and indirect material purchasing across the existing company of the Ammotec division and the newly founded company in Eger.

Effects of acquisitions of companies
in CHF m

	2017		2016
	Clearswift	Other acquisitions	HTS Hoch Technologie Systeme GmbH
Purchase price, paid in cash	55	1	1
Escrow account	3	—	—
Contingent consideration	4	0	—
Total consideration	62	1	1

Clearswift Under the agreements concerning the contingent consideration, the Group is obliged to pay an additional amount of up to CHF 7.5 million depending on the operating result achieved for the four financial years following the acquisition. At the time of acquisition, the fair value of this liability was estimated to be CHF 4.5 million.

Other acquisitions Under the agreement concerning the contingent consideration, the Group is obliged to pay an additional amount of up to CHF 0.1 million depending on defined revenue targets. At the time of acquisition, the liability was recognized at the nominal value.

Acquired assets and liabilities recognized at the time of acquisition
in CHF m

	2017		2016
	Clearswift	Other acquisitions	HTS Hoch Technologie Systeme GmbH
Current assets	17	12	0
Property, plant and equipment	1	0	1
Intangible assets	43	1	—
Deferred tax assets	2	0	—
Current and non-current liabilities	(62)	(13)	(1)
Deferred tax liabilities	(9)	0	0
Total acquired assets and liabilities	(8)	1	0

Calculation of fair value The valuation methods used to calculate the fair value of the material assets and liabilities acquired were as follows:

Inventories and work in progress The fair values were determined based on the estimated selling price under normal business conditions, less the estimated finishing and sales costs as well as an appropriate profit margin based on the work required to finish and sell the inventories and work in progress.

Property, plant and equipment The fair value of property, plant and equipment was measured based on the updated replacement values, taking into account the newly estimated useful life.

Deferred income Clearswift provides its products to customers for subscription fees that must be paid in advance. These advance payments are recorded as liabilities and the revenues are recognized over the term of the contract. The acquisition-date fair value is derived from the costs for the provision of the specific contractual liabilities as well as a standard market margin. The fair value calculated is significantly lower than the book value of the advance payments received.

Intangible assets and goodwill The fair value of material intangible assets is calculated using the "Multi Period Excess Earnings" and "Relief from Royalty" methods, based on the available market data and management estimates. A positive goodwill amount of CHF 71.8 million resulted from the acquisition of Clearswift. The other acquisitions gave rise to a goodwill amount of CHF 0.3 million and a badwill amount of CHF 0.1 million. Goodwill is offset against equity at the time of acquisition, while badwill is recognized as a loss on the income statement.

Net cash outflow
in CHF m

	2017		2016
	Clearswift	Other acquisitions	HTS Hoch Technologie Systeme GmbH
Cash consideration	59	1	1
Take-over of financial liabilities	39	6	—
Cash and cash equivalents acquired	(11)	(0)	0
Total net cash outflow	87	7	1

The considerations paid with regard to Clearswift already include the first tranche of the contingent consideration, which amounted to CHF 0.6 million.

The costs associated with the transactions amounted to approximately CHF 2.9 million, with the costs related to Clearswift accounting for CHF 2.8 million and other acquisitions CHF 0.1 million. In particular, these amounts include legal and consulting costs. The costs were recognized under "Other operating expenses, net", with the majority having already been incurred in the 2016 financial year.

Impact of the acquisitions on the Group result

The acquisitions had a positive impact of around CHF 35 million on the Group's consolidated sales (of which around CHF 24 million came from Clearswift and around CHF 11 million from the other acquisitions). They had an overall negative impact of about CHF 1.3 million on the Group's consolidated result. Clearswift contributed a loss of approximately CHF 1.7 million, which was caused by the effects of the purchase price allocation (writedowns of the recognized intangible assets and the negative effect of deferred income). The other acquisitions made a positive contribution of approximately CHF 0.4 million to the Group's result. The 2017 results also include one-time integration and set-up costs.

Had the acquisitions taken effect as of 1 January 2017, they would have contributed approximately CHF 40 million to net sales. Of this, Clearswift would have accounted for around CHF 26 million, while CHF 14 million would have come from the other acquisitions. This would have resulted in a consolidated loss of around CHF 2 million for the financial year as a whole. Clearswift would have made a loss of around CHF 2.5 million, while the other acquisitions would have turned a profit of approximately CHF 0.4 million.

Disposals of subsidiaries and business areas

No entities or business areas were disposed of during the financial year.

On 2 November 2016, OEI Opto AG was sold to the aerospace group Thales Alenia Space. OEI Opto AG was founded in the 2016 financial year as a vehicle for the sale of RUAG Space's Opto-Electronics & Instruments product unit. Thales Alenia Space has taken over all the unit's activities and employees. Up to the date of the sale, OEI Opto AG had generated sales of CHF 11.3 million and a loss of CHF 0.2 million.

During the reporting period, OEI Opto AG made a settlement payment of CHF 0.8 million to the buyer, with a negative impact of CHF 0.4 million on the Group's result.

Assets and liabilities disposed
in CHF m

	2017	2016
Current assets	—	12
Property, plant and equipment	—	2
Intangible assets	—	—
Current and non-current liabilities	—	(6)
Deferred tax liabilities	—	0
Assets and liabilities disposed	—	7

5 Segment information

in CHF m

	2017 Space	2016 Space	2017 Aerostructures	2016 Aerostructures	2017 Aviation	2016 Aviation
Net sales with third parties	365	344	255	235	506	460
Net sales with other segments	0	1	2	1	9	9
Total net sales	365	345	256	236	515	469
Earnings before interest, taxes, depreciation and amortization (EBITDA)	46	48	11	15	46	52
Depreciation, amortization and impairment	(12)	(17)	(3)	(3)	(7)	(8)
Earnings before interest and taxes (EBIT)	34	32	8	12	39	44
Net financial result						
Share in income of associates						
Earnings before taxes						
Income taxes						
Net profit						
Net operating assets by region[2]	81	41	140	103	123	95
Net operating assets Switzerland	9	12	57	54	46	37
Net operating assets Rest of Europe	68	46	83	49	61	43
Net operating assets Rest of world	4	(17)	—	—	16	14
Property, plant and equipment and intangible assets (incl. investment properties)	72	56	38	26	59	70
Property, plant and equipment and intangible assets Switzerland (incl. investment properties)	36	38	26	20	25	41
Property, plant and equipment and intangible assets Rest of Europe	22	17	12	6	18	14
Property, plant and equipment and intangible assets Rest of world	13	0	—	—	16	15
Capital expenditures for property, plant and equipment and intangible assets (incl. investment properties)	(29)	(12)	(14)	(14)	(11)	(16)
Disposal of property, plant and equipment and intangible assets (incl. investment properties)	0	0	0	0	0	0

[1] The profitability of the Defence division was seriously impacted by a number of factors in the year under review. Delays to projects gave rise to various revaluations and, in some cases, resulted in penalties having to be paid. One-off corrections to the valuation of inventories and other assets also had a negative effect on the results.

[2] Net assets comprise trade receivables, prepayments to suppliers, other current receivables, tax assets, prepaid expenses and accrued income, inventories and work in progress, property, plant and equipment, investment property and intangible assets less trade accounts payable, prepayments from customers, other current liabilities, tax liabilities, deferred income and accrued expenses as well as current and non-current provisions.

Further information on sales and customers is provided in Note 6 "Net sales".

Products and services of the individual segments are described in Note 2.25, "Segment information".

2017 Ammotec	2016 Ammotec	2017 Defence[1]	2016 Defence	2017 Services	2016 Services	2017 Total Segments	2016 Total Segments	2017 Eliminations	2016 Eliminations	2017 Group total	2016 Group total
397	385	385	384	47	51	1 955	1 858	—	—	1 955	1 858
0	0	5	5	134	128	150	144	(150)	(144)	—	—
397	385	389	388	182	179	2 105	2 002	(150)	(144)	1 955	1 858
43	46	9	35	40	36	196	232	—	—	196	232
(15)	(14)	(13)	(11)	(28)	(28)	(77)	(81)	—	—	(77)	(81)
28	31	(3)	24	12	8	119	151	—	—	119	151
										(8)	(7)
				3	3	3	3			3	3
										114	147
										(25)	(31)
										89	116
304	265	87	45	261	273	995	822	(0)	(0)	995	822
42	63	36	25	257	277	448	469	2	(1)	450	468
239	174	51	19	4	(4)	506	328	(2)	1	504	329
22	28	(0)	0	(0)	(0)	41	26	0	0	42	26
129	107	69	25	283	293	650	577	—	—	650	577
31	28	15	15	283	293	416	434	—	—	416	434
95	76	55	11	0	0	202	125	—	—	202	125
2	3	0	—	—	—	31	18	—	—	31	18
(29)	(25)	(9)	(7)	(22)	(21)	(113)	(96)	—	—	(113)	(96)
0	0	0	0	13	2	13	2	—	—	13	2

6 Net sales

in CHF m	2017	2016
Invoiced sales	1 920	1 817
Change in contracts under the percentage of completion (PoC) method	35	41
Total net sales	1 955	1 858

DDPS	590	568
Third parties	1 330	1 249
Invoiced sales by customer group	1 920	1 817

Aside from the DDPS and Airbus, RUAG has no other customer relationships that account for more than 10 % of net sales. Net sales from transactions with the DDPS are primarily attributable to the Aviation, Defence and Ammotec segments, while those from transactions with Airbus mainly relate to the Aerostructures and Space segments.

Defence	846	774
Civil	1 075	1 044
Invoiced sales by type of use	1 920	1 817

Switzerland	722	679
Rest of Europe	907	838
Middle East	23	16
North America	187	200
South America	9	11
Asia/Pacific	62	64
Africa	11	11
Invoiced sales by region	1 920	1 817

Invoiced sales in “rest of Europe” primarily concern Germany, France, the UK, Italy, Sweden and the Netherlands.

7 Personnel expenses

in CHF m	2017	2016
Salaries and wages	(681)	(640)
Expense of benefit plans	(51)	(49)
Other social security expenses	(89)	(82)
Contract personnel	(57)	(50)
Other personnel expenses	(36)	(38)
Total personnel expenses	(914)	(859)

The increase in personnel expenses is attributable to the year-on-year rise in the average headcount. The higher headcount was due in turn to the acquisitions effected in the reporting year and to the ongoing addition of two new sites – i.e. those in Hungary (Eger, Aerostructures division) and the USA (Decatur, Space division). Higher capacity utilization at Aviation also led to an increase in staff numbers.

8 Other operating expenses, net

in CHF m	2017	2016
Premises costs	(27)	(22)
Maintenance and repairs of property, plant and equipment	(55)	(53)
Cost of energy and waste disposal	(13)	(12)
Insurance and duties	(7)	(7)
Administration and IT costs	(60)	(55)
Advertising costs	(31)	(29)
Other operating expenses	(41)	(21)
Other operating income	41	29
Total other operating expenses, net	(193)	(171)

The increase in "Other operating expenses, net" during the year under review was due among other things to the various acquisitions of companies. Additional information on this can be found in Note 4 "Acquisitions, mergers, formations and disposals of companies".

In addition, higher capacity utilization rates and capacity expansions compared to the previous year across various segments resulted in additional costs for maintaining and repairing property, plant and equipment.

Furthermore, various adjustments and revaluations of provisions (guarantee provisions, follow-up costs etc.) combined with the effect of the newly acquired companies resulted in an increase in "Other operating expenses" in particular. For more information, see Note 26 "Provisions".

"Other operating income" contains net exchange gains of CHF 9 million (previous year: net exchange gains of CHF 2 million). Sales of property also had a positive impact on the result.

9 Research and development expenses

in CHF m	2017	2016
Total research and development expenses	181	171
of which third party-financed research and development	127	122
of which self-financed research and development costs	53	49

Research and development expenses include all own work and work assigned to third parties or services required from third parties that were recognized as an expense during the year under review. Self-financed research and development costs amounted to CHF 53 million (previous year: CHF 49 million). The increase in third party-financed research and development expenses of around CHF 6 million is primarily a result of the increased project volume in the Space division related to the development of a new payload fairing and additional composite structural components for ULA's Vulcan launch vehicle, and portfolio expansions in the currently disruptive space market. By contrast, self-financed and third party-financed research and development expenses in the Defence division declined from the previous year by around CHF 8 million.

10 Financial income/financial expenses

in CHF m	2017	2016
Interest income	2	2
Realized exchange gains	0	—
Realized gains from securities	—	—
Total financial income	2	2
Interest expense	(10)	(9)
Realized exchange losses	—	—
Realized losses from securities	—	—
Impairment of financial assets	—	—
Total financial expenses	(10)	(9)

In addition to conventional interest income/expenses, any impact on income resulting from a change in the discount rate that is reflected in the pension fund's liabilities being discounted/compounded is recognized and shown in net interest/financial result. In financial year 2017, such interest expenses amounted to CHF 5 million (previous year: CHF 5 million).

11 Income taxes

in CHF m	2017	2016
Current income tax expense of the reporting period	(25)	(32)
Adjustments to current income taxes from prior periods	(2)	0
Current income tax expense	(27)	(32)
Origination (reversal) of temporary differences	1	(0)
Effect of tax rate changes	(0)	1
Recognition of previously unrecognized tax losses	4	0
Use of recognized tax loss carryforwards	(2)	(1)
Deferred tax income	2	0
Income tax expense in profit or loss	(25)	(31)

In addition, the following deferred taxes are recognized in equity:

in CHF m	2017 Before tax	2017 Tax (expense)/ income	2017 Net (after tax)	2016 Before tax	2016 Tax (expense)/ income	2016 Net (after tax)
Change in fair value of cash flow hedges	8	(3)	5	(10)	2	(8)
Gains and losses from cash flow hedges transferred to profit or loss	(2)	1	(1)	3	(1)	2
Foreign currency translation adjustments of foreign subsidiaries	28	—	28	(4)	0	(4)
Changes in equity	34	(2)	32	(11)	2	(10)

Analysis of income tax expense

The following table shows the reconciliation of expected to effective income tax expense. The applicable income tax rate for the purposes of the following analysis is the average income tax rate of the Group companies weighted by profit or loss; it is 19.3 % (previous year: 23.2 %).

in CHF m	2017	2016
Earnings before taxes	114	147
Expected weighted tax rate in %	19.3 %	23.2 %
Expected income tax expense	(22)	(34)
Reconciliation of effective income tax expense		
Effect of (valuation allowances)/recognizing of tax loss carryforwards from prior years	0	(1)
Effect of using unrecognized tax loss carryforwards from prior years	0	0
Effect of current losses for which tax loss carryforwards are not recognized	(1)	(0)
Effect of non-deductible expenses	(1)	(1)
Effect of tax-free income	3	4
Effect of income taxed at lower rates	—	—
Effect of tax rate changes	(0)	1
Effect of tax credits (losses) from prior periods	(2)	0
Other effects (including effect of share in profit or loss of associates)	(3)	(0)
Effective income tax expense	(25)	(31)
Effective income tax rate	21.8 %	21.3 %

Individual countries (cantons in the case of Switzerland) operate different tax laws and different rates of tax. For this reason, the weighted average of the expected tax rate may vary between periods, which is attributable to the profits or losses generated in each individual country or canton.

Deferred tax assets and liabilities

Recognized deferred tax assets and liabilities break down as follows:

in CHF m	2017 Deferred tax assets	2017 Deferred tax liabilities	2016 Deferred tax assets	2016 Deferred tax liabilities
Assets				
Receivables and prepayments	0	2	0	3
Inventories and work in progress	4	13	2	11
Property, plant and equipment and investment property	2	16	3	14
Intangible assets	0	11	0	3
Tax loss carryforwards	7	—	4	—
Employee benefit assets	—	—	—	—
Other asset items	3	3	1	2
Liabilities				
Deferred income and accrued expenses	4	1	2	0
Current and non-current provisions	2	9	3	8
Employee benefit obligations	8	—	6	—
Other liability items	2	8	4	7
Deferred taxes before offsetting	33	64	25	49
Offsetting of deferred tax assets and liabilities	(16)	(16)	(13)	(13)
Total deferred taxes	17	47	13	36

Deferred tax assets and liabilities changed as follows:

in CHF m	2017	2016
Total deferred taxes at 1 January	(23)	(26)
Changes recognized in profit or loss	2	0
Changes in equity with no impact on profit or loss	(2)	2
Changes in the scope of consolidation	(7)	0
Foreign currency translation adjustments	(0)	0
Total deferred taxes at 31 December	(30)	(23)
of which deferred tax assets	17	13
of which deferred tax liabilities	(47)	(36)

Deferred taxes are calculated on the basis of the expected tax rates applicable at the individual companies for the relevant assets and liabilities.

Deferred tax assets for unused tax loss carryforwards are only recognized if it is probable that they will be offset against future taxable profits.

The tax loss carryforwards are due to expire as follows:

in CHF m	2017	2016
Expiring within 1 year	—	—
Expiring in 1 to 2 years	—	1
Expiring in 2 to 3 years	1	—
Expiring in 3 to 4 years	0	3
Expiring in 4 to 5 years	2	2
Expiring in 5 to 6 years	0	1
Expiring in 6 to 7 years	1	0
Expiring in more than 7 years	60	8
Total tax loss carryforwards	64	15

Potential tax effect of tax loss carryforwards	14	4
of which recognized as deferred tax assets	7	4
of which not recognized	7	1

12 Cash and cash equivalents

in CHF m	2017	2016
Cash on hand	0	3
Demand deposits with financial institutions	200	197
Money market investments	0	39
Total cash and cash equivalents	201	239

Currencies of cash and cash equivalents

in CHF m	2017	2016
CHF	105	139
EUR	42	55
USD	20	27
SEK	10	10
GBP	14	2
Other	11	6
Total cash and cash equivalents	201	239

13 Financial assets

Current financial assets

in CHF m	2017	2016
Derivative financial instruments	6	4
Other current financial assets	1	0
Total current financial assets	7	4

Current financial assets primarily comprise the fair value of open foreign currency hedging transactions (see also the information on financial instruments in Note 35, “Risk management process, financial risk management and capital management”).

Non-current financial assets

in CHF m	2017	2016
Money market investments	0	0
Other receivables from third parties	2	3
Valuation allowances	(0)	(0)
Total non-current financial assets	3	3

Currencies of current and non-current financial assets

in CHF m	2017	2016
CHF	1	1
EUR	3	1
USD	4	3
SEK	1	1
GBP	—	0
Other	0	0
Total financial assets	9	6

The carrying amounts of the non-current financial assets are a reasonable approximation of their fair value.

14 Trade receivables, other current receivables and prepayments

in CHF m	2017	2016
Trade receivables	271	273
Trade receivables and receivables from associates	0	0
Valuation allowances	(8)	(8)
Total trade receivables	263	266
Prepayments to suppliers	17	30
Prepayments to associates	0	0
Total prepayments to suppliers	17	30
Current receivables from government bodies	10	11
Other current receivables	11	12
Total other current receivables	21	23
Total trade receivables, other current receivables and prepayments	301	319

Maturity profile of trade receivables, other current receivables and prepayments

in CHF m	2017	2016
Not past due	217	232
Past due 1–30 days	38	42
Past due 31–60 days	14	5
Past due 61–90 days	4	5
Past due 91–180 days	8	8
Past due over 180 days	21	27
Total trade receivables, other current receivables and prepayments	301	319

Currencies of trade receivables, other current receivables and prepayments

in CHF m	2017	2016
CHF	60	101
EUR	129	117
USD	93	86
SEK	7	9
GBP	7	2
Other	5	4
Total trade receivables, other current receivables and prepayments	301	319

Valuation allowances for doubtful receivables comprise specific valuation allowances for specifically identified items where there is a high risk of non-payment and global valuation allowances based on historical experience.

The allowance for receivables changed as follows:

Valuation allowances for doubtful receivables

in CHF m	2017	2016
Balance at 1 January	(8)	(10)
Increase in allowance	(2)	(3)
Utilization of allowance	1	2
Reversal of allowance	0	3
Currency differences	(0)	0
Carrying amount at 31 December	(8)	(8)

Allowances for doubtful receivables are recorded in an allowance account. Changes are recognized in other operating expenses. No valuation allowances were required for financial instruments in categories other than loans and receivables at the end of the reporting period. Receivables judged to be unrecoverable are written off as realized losses.

15 Inventories and work in progress

in CHF m	2017	2016
Raw materials and supplies	360	304
Work in progress at cost of conversion	142	114
Work in progress (percentage of completion)[1]	135	101
Semi-finished goods	104	105
Finished goods	95	82
Valuation allowances	(120)	(102)
Total inventories and work in progress	717	603

[1] The key figures for work in progress, which is measured using the percentage of completion method, are explained in further detail below.

In the reporting period, a total of CHF 501 million (previous year: CHF 442 million) in raw materials and supplies, semi-finished and finished goods, and work in progress was charged to cost of materials.

In the reporting period, inventories amounting to CHF 5 million (previous year: CHF 2 million) were written down to net realizable value.

In both the reporting period and the previous year, there were no significant reversals of inventory write-downs effected in prior periods.

Write-downs and reversals of inventory write-downs are recorded as cost of materials.

16 Percentage of Completion (PoC)

Long-term construction and service contracts

in CHF m	2017	2016
Contract sales and costs of ongoing projects at the end of the reporting period		
Aggregated contract sales at the end of the reporting period	2 108	1 804
Aggregated contract costs at the end of the reporting period	(1 510)	(1 295)
Realized margin at the end of the reporting period	598	509
Cumulative balance of ongoing projects at the end of the reporting period		
Gross amount due from customers for contract work	135	101
Gross amount due to customers for contract work	(100)	(101)
Net position	35	0
Advances received from customers relating to PoC contracts	33	25

17 Property, plant and equipment

in CHF m

	Plant and equipment	Other[1]	Land	Buildings	Assets under construction	Property, plant and equipment
At cost						
As at 1 January 2016	488	230	75	477	42	1 311
Business combination	0	0	0	1	—	1
Eliminations from the scope of consolidation	(2)	(8)	—	(1)	—	(10)
Additions	20	28	0	2	37	87
Disposals	(5)	(12)	(0)	(1)	(0)	(18)
Reclassifications	10	8	—	2	(18)	2
Foreign currency translation adjustments	(3)	(1)	0	(0)	(0)	(4)
As at 31 December 2016	509	245	75	479	60	1 369
Accumulated depreciation and impairment losses						
As at 1 January 2016	364	167	0	343	—	874
Business combination	—	—	—	—	—	—
Eliminations from the scope of consolidation	(2)	(5)	—	(1)	—	(8)
Depreciation	21	21	0	17	—	58
Impairment	—	—	—	—	—	—
Disposals	(4)	(12)	—	(1)	—	(17)
Reclassifications	(0)	1	—	—	—	1
Foreign currency translation adjustments	(2)	(1)	(0)	(0)	—	(3)
As at 31 December 2016	376	171	0	358	—	905
At cost						
As at 1 January 2017	509	245	75	479	60	1 369
Business combination	1	4	—	—	—	5
Eliminations from the scope of consolidation	—	—	—	—	—	—
Additions	22	26	1	6	50	105
Disposals	(12)	(14)	(1)	(3)	(2)	(33)
Reclassifications	14	(10)	0	11	(35)	(21)[2]
Foreign currency translation adjustments	14	7	0	2	2	25
As at 31 December 2017	547	258	75	495	74	1 450
Accumulated depreciation and impairment losses						
As at 1 January 2017	376	171	0	358	—	905
Business combination	1	3	—	—	—	4
Eliminations from the scope of consolidation	—	—	—	—	—	—
Depreciation	22	22	0	16	0	60
Impairment	—	0	—	—	—	0
Disposals	(12)	(15)	—	(3)	—	(30)
Reclassifications	(1)	(1)	—	1	—	(2)[2]
Foreign currency translation adjustments	9	5	0	1	0	15
As at 31 December 2017	394	185	0	373	0	953
Net carrying amount						
As at 1 January 2016	124	63	75	134	42	438
As at 31 December 2016	132	74	75	122	60	464
As at 31 December 2017	153	73	75	123	74	497

[1] Fixtures and fittings, information technology, motor vehicles and aircrafts.
[2] Aircraft that were previously leased, but are now for sale, were moved to inventories during the reporting year.

The total amount of property, plant and equipment pledged as collateral is listed in Note 32 "Assets pledged as collateral".

Leased property, plant and equipment

in CHF m	2017	2016
At cost	5	5
Accumulated depreciation and impairment losses	(4)	(5)
Carrying amount at 31 December	0	1

Leased assets are items of property, plant and equipment that satisfy the criteria of finance leases. The net carrying amounts break down among the different classes of property, plant and equipment as follows:

in CHF m	2017	2016
Plant and equipment	0	0
Other	0	1
Carrying amount at 31 December	0	1

Fire insurance values

in CHF m	2017	2016
Plant and equipment	1 278	1 288
Property	951	930
Total fire insurance values	2 229	2 217

18 Investment properties

in CHF m	2017	2016
At cost		
As at 1 January	353	351
Business combination	—	—
Eliminations from the scope of consolidation	—	—
Additions	3	2
Disposals	(6)	(0)
Reclassifications	(0)	(0)
Foreign currency translation adjustments	—	—
As at 31 December	351	353
Accumulated depreciation and impairment losses		
As at 1 January	264	258
Business combination	—	—
Eliminations from the scope of consolidation	—	—
Depreciation	6	6
Disposals	(4)	—
Depreciation of net carrying amount	—	—
Reclassifications	—	—
Foreign currency translation adjustments	—	—
As at 31 December	266	264
Net carrying amount		
As at 1 January	88	93
As at 31 December	84	88

Fire insurance values

in CHF m	2017	2016
Investment property	441	477
Total fire insurance values	441	477

Investment property is measured at cost minus accumulated depreciation. The fair value of the properties set out below is calculated solely for disclosure reasons and was measured using the discounted cash flow (DCF) method.

in CHF m	2017	2016
Fair value (DCF calculation)	244	235
Rental income from investment property	21	20
Real estate expenses	8	11
of which on let property	7	9
of which on vacant property	1	2
Agreed capital commitments and commitments in respect of maintenance work	1	1
Future minimum rental income from ongoing rental contracts	86	55

Majority leased sites to third parties are classified as investment properties. In 2017 as in the previous year, there were six such sites: Bern, Altdorf, Zwieselberg (Thun-Boden), Aigle, Unterseen and Wimmis.

In the current year, the construction rights for the Bern and Altdorf sites were included in the DCF calculation for the first time. The increase in the fair value as well as the minimal future rental income compared to the previous year are in particular a result of these rights being considered for the first time.

Valuation techniques As was the case in the previous year, no fair value measurement was carried out by an external expert during the year under review. RUAG Real Estate Ltd calculates the fair value of investment property using the discounted cash flow (DCF) method.

The valuations carried out across the period under review using the DCF method are based on the current rental income. After the binding tenancy agreements have expired, both the vacancy risk, on the one hand, together with the additional/reduced rental income and inflation, on the other, are taken into account. The expected net cash flow is discounted at risk-adjusted discount rates on the valuation date. The discount rate also takes into account the location, development potential and building strategy of the investment property in question.

19 Intangible assets

in CHF m

	Patents and developments	Trademarks and prototypes	Licences and rights	Order backlog and customer relationships	ERP systems	Intangible assets in progress	Intangible assets
At cost							
As at 1 January 2016	2	9	24	143	—	—	179
Business combination	—	—	—	—	—	—	—
Eliminations from the scope of consolidation	(0)	—	(0)	(0)	—	—	(0)
Additions	—	—	6	—	—	—	6
Disposals	—	—	—	—	—	—	—
Reclassifications	—	—	—	—	—	—	—
Foreign currency translation adjustments	(0)	(0)	(0)	(1)	—	—	(1)
As at 31 December 2016	2	9	31	142	—	—	185
Accumulated amortization and impairment losses							
As at 1 January 2016	2	9	17	116	—	—	144
Business combination	—	—	—	—	—	—	—
Eliminations from the scope of consolidation	—	—	(0)	(0)	—	—	(0)
Amortization	0	—	1	16	—	—	17
Impairment	—	—	—	—	—	—	—
Disposals	—	—	—	—	—	—	—
Reclassifications	—	—	—	—	—	—	—
Foreign currency translation adjustments	(0)	(0)	(0)	(1)	—	—	(1)
As at 31 December 2016	2	9	18	131	—	—	160
At cost							
As at 1 January 2017	2	9	31	142	—	—	185
Business combination	22	2	1	21	—	—	46
Eliminations from the scope of consolidation	—	—	—	—	—	—	—
Additions	—	—	0	—	2	3	5
Disposals	—	—	(1)	—	—	—	(1)
Reclassifications	—	—	—	—	1	1	2
Foreign currency translation adjustments	1	1	2	3	0	0	7
As at 31 December 2017	25	12	33	167	3	4	244
Accumulated amortization and impairment losses							
As at 1 January 2017	2	9	18	131	—	—	160
Business combination	—	—	0	—	—	—	0
Eliminations from the scope of consolidation	—	—	—	—	—	—	—
Amortization	1	1	1	7	0	—	10
Impairment	—	—	1	—	—	—	1
Disposals	—	—	(1)	—	—	—	(1)
Reclassifications	—	—	—	—	—	—	—
Foreign currency translation adjustments	0	1	1	2	0	—	4
As at 31 December 2017	4	11	21	140	0	—	175
Net carrying amounts							
As at 1 January 2016	0	—	8	27	—	—	35
As at 31 December 2016	0	—	13	11	—	—	24
As at 31 December 2017	22	2	13	27	2	4	69

Amortization and impairment of intangible assets are reported in the consolidated income statement under “Amortization and impairment of intangible assets”.

Goodwill The goodwill from acquisitions is offset directly against the equity at the time of acquisition. The theoretical capitalization, based on a useful life of five years, would have the following impact on the consolidated financial statements:

Theoretical movement schedule for goodwill

in CHF m	Space	Aerostructures	Aviation	Ammotec	Defence	Total
At cost						
As at 1 January 2016	60	—	0	12	8	79
Business combination	1	—	—	—	—	1
Adjustments	—	—	—	—	—	—
Foreign currency translation adjustments	(0)	—	0	(0)	(0)	(0)
As at 31 December 2016	61	—	0	12	8	80
Accumulated amortization						
As at 1 January 2016	60	—	0	12	6	77
Theoretical ordinary amortization	0	—	—	—	1	1
Foreign currency translation adjustments	(0)	—	0	(0)	(0)	(0)
As at 31 December 2016	60	—	0	12	6	78
At cost						
As at 1 January 2017	61	—	0	12	8	80
Business combination	—	—	—	0	72	72
Adjustments	—	—	—	—	—	—
Foreign currency translation adjustments	1	—	(0)	1	5	7
As at 31 December 2017	62	—	0	13	85	159
Accumulated amortization						
As at 1 January 2017	60	—	0	12	6	78
Theoretical ordinary amortization	0	—	—	0	14	15
Foreign currency translation adjustments	1	—	(0)	1	1	2
As at 31 December 2017	61	—	0	13	21	95
Theoretical net book value						
As at 1 January 2016	—	—	—	—	2	2
As at 31 December 2016	1	—	—	—	1	2
As at 31 December 2017	1	—	—	0	63	64

Capitalizing the goodwill and amortizing it over five years would have the following theoretical impact on the consolidated income statement and consolidated balance sheet:

Impact on consolidated income statement

in CHF m	2017	2016
Earnings before interest and taxes (EBIT)	119	151
Theoretical amortization of goodwill	(15)	(1)
Theoretical EBIT incl. amortization of goodwill	104	150
Net profit	89	116
Theoretical amortization of goodwill	(15)	(1)
Theoretical net profit incl. amortization of goodwill	75	115

Impact on consolidated balance sheet

in CHF m	2017	2016
Equity according to the balance sheet	1 011	1 009
Theoretical capitalization of net book value of goodwill	64	2
Theoretical equity incl. net book value of goodwill	1 076	1 011

20 Associates

in CHF m	2017	2016
Carrying amount of interests in associates as at 1 January	39	39
Acquisitions	—	—
Business combination	—	—
Share in profit/loss of associates from discontinued operations	—	—
Share in profit/loss of associates from continued operations	3	3
Dividends	(3)	(3)
Reclassifications	—	(0)
Foreign currency translation adjustments	1	(0)
Carrying amount of interests in associates as at 31 December	40	39

RUAG does not hold any individually significant investments in associates. The following table shows the aggregate values of the investments in associates attributable to RUAG:

Aggregate investments of RUAG in associates

in CHF m	2017	2016
Share in result of associates from continued operations	3	3

Aggregate financial information for associates (100 %) is as follows:

Aggregate financial information for associates

in CHF m	2017	2016
Total assets	195	207
Total liabilities	112	121
Net assets	83	86
Net sales	138	152
Profit from continued operations	5	10

There are no contingent liabilities for RUAG relating to associates.

21 Financial liabilities

Current financial liabilities

in CHF m	Note	2017	2016
Due to financial institutions		50	0
Financial liabilities to third parties[1]		6	12
Liabilities to associates		—	—
Financial liabilities to employee benefit funds		—	0
Lease liabilities	31	0	0
Current portion of non-current financial liabilities		—	—
Total current financial liabilities		56	13

[1] This item primarily contains the negative replacement values of foreign currency forward transactions.

Non-current financial liabilities

in CHF m	Note	2017	2016
Due to financial institutions		75	—
Financial liabilities towards third parties		1	—
Lease liabilities	31	0	0
Loans secured by property		—	—
Bond issues		—	—
Liabilities to associates		—	—
Total non-current financial liabilities		76	0

The carrying amounts of the non-current financial liabilities are a reasonable approximation of the fair value. The average rate of interest on non-current financial liabilities in the year under review was 0.6 % (previous year: 3.3 %).

Maturity structure of current and non-current financial liabilities

in CHF m	2017	2016
Up to 1 year	56	13
Up to 2 years	30	0
Up to 3 years	30	0
Up to 4 years	15	0
Over 4 years	1	—
Total financial liabilities	133	13

The current and non-current financial liabilities due to financial institutions contain a covenant in relation to the debt factor, expressed as a ratio of the net financial liabilities as of the reporting date (comprising all interest-bearing financial liabilities less cash and cash equivalents) to EBITDA (on a rolling basis for the previous 12 months). In addition, there are a few negative and positive covenants in line with standard market practice. If these covenants cannot be met, the financial institution would have the right to terminate the loan at short notice. Both during the reporting period and as of 31 December 2017, all covenants were met.

Currencies of financial liabilities

in CHF m	2017	2016
CHF	53	1
EUR	35	4
USD	0	7
SEK	0	0
GBP	43	0
Other	1	0
Total financial liabilities	133	13

22 Trade accounts payable and prepayments

in CHF m	2017	2016
Trade accounts payable	93	118
Trade accounts payable to associates	0	0
Total trade accounts payable	93	118
Prepayments from customers	213	182
Trade accounts payable to associates	—	—
Total prepayments from customers	213	182
Total trade accounts payable and prepayments	306	300

Currencies of trade accounts payable and prepayments

in CHF m	2017	2016
CHF	129	121
EUR	126	112
USD	37	54
SEK	10	9
GBP	1	1
Other	3	2
Total trade accounts payable and prepayments	306	300

23 Other current liabilities

in CHF m	2017	2016
Due to third parties	12	21
Due to associates	—	—
Due to government bodies	26	30
Due to shareholders	—	—
Due to employee benefit funds	2	3
Total current liabilities	40	55

24 Other non-current liabilities

in CHF m	2017	2016
Due to third parties	1	4
Due to associates	—	—
Due to shareholders	—	—
Due to employee benefit funds	—	—
Total other non-current liabilities	1	4

25 Deferred income and accrued expenses

in CHF m	2017	2016
Deferred income and accrued expenses for PoC orders	100	101
Income relating to future periods	32	7
Outstanding trade accounts payable	53	45
Personnel-related accrued expenses	21	22
Other deferred income and accrued expenses	14	24
Total deferred income and accrued expenses	220	199

26 Provisions

in CHF m

	Restructuring	Contract losses	Warranties	Holiday and overtime	Loyalty bonuses and anniversary benefits	Other	Total
Balance at 1 January 2016	15	16	18	31	23	29	132
Business combination	—	—	—	—	—	0	0
Eliminations from the scope of consolidation	—	(2)	—	(0)	(0)	0	(2)
Additions	—	10	3	24	1	8	46
Release of unused provisions	(3)	(5)	(7)	(0)	(2)	(5)	(22)
Use of provisions	(2)	(6)	(2)	(18)	(2)	(7)	(37)
Reclassifications	—	—	(0)	—	—	0	—
Foreign currency translation adjustments	0	(0)	(0)	(0)	(0)	(0)	(1)
Balance at 31 December 2016	11	13	12	36	19	25	116
Current provisions	—	11	11	36	1	16	75
Non-current provisions	11	2	1	—	18	9	41
Balance at 1 January 2017	11	13	12	36	19	25	116
Business combination	—	—	—	0	—	4	5
Eliminations from the scope of consolidation	—	—	—	—	—	—	—
Additions	1	11	3	21	1	8	45
Release of unused provisions	(4)	(4)	(3)	—	(3)	(2)	(16)
Use of provisions	(0)	(5)	(1)	(23)	(2)	(7)	(38)
Reclassifications	—	—	—	—	—	—	—
Foreign currency translation adjustments	—	1	0	1	0	1	4
Balance at 31 December 2017	7	16	12	35	15	30	115
Current provisions	—	14	11	35	1	15	76
Non-current provisions	7	2	1	—	15	15	39

The development of provisions in the reporting year was shaped by the following material events:

As at the end of the reporting period, the restructuring provisions created in the Space division in 2015 relating to the transfer of business activities were revalued, which led to the release of CHF 4 million. The provisions were recognized in relation to the gradual transfer of the production of payload fairings and other structures from Zurich-Seebach to Emmen and the USA (Decatur, Alabama) and the associated restructuring costs. The associated cash outflows will mainly occur as of 2019. The releases of unused provisions are primarily related to the fact that, due to the increased requirement for space in the structures area, some of the structures no longer need to be transferred to Emmen.

In the Defence division provisions of around CHF 4 million had to be created for anticipated contract losses due to extraordinary adjustments to planned costs for projects. In the Aviation division, provisions for anticipated contract losses also had to be increased by CHF 3 million in Germany. On the other hand, provisions for contract losses resulting from a reduction in project risks in the Swiss Aviation area were released.

The warranty provision adjustments come within the scope of ordinary fluctuations in day-to-day business. The non-current portion of the provisions is likely to be used in the period 2019–21.

The reduction in provisions for loyalty bonuses and anniversary benefits is mainly due to the change in the likelihood of staff leaving the company, partly offset by a slight fall in the discount rate. As at 31 December 2017, a discount rate of 0.7 % (previous year: 0.8 %) was used to calculate the long company service provision for employees in Switzerland. Other actuarial assumptions, such as the probability of employees retiring and salary increases did not differ materially from the assumptions in the previous year. Payment of the on-current portion of the provisions will take place as of 2019.

The increase in other provisions is primarily due to the acquisition of Clearswift in January 2017. Under the agreements concerning contingent considerations, the Group is obliged to pay additional amounts depending on the operating result achieved for the four financial years following the acquisition.

In relation to the acquisitions of companies carried out in 2009 (GEKE Schutztechnik GmbH) and 2013 (RUAG Defence France SAS), as at the end of 2016 the other provisions contained provisions for potential liabilities to former owners (outstanding purchase price payments). During the reporting period, agreements were reached which resulted in a payment of around CHF 2 million.

The other provision of CHF 1 million created during the previous year in the Aerostructures division resulting from the termination of a supplier contract was used in full during the reporting period.

27 Employee benefit obligations

The RUAG Group maintains various defined benefit plans for employees. The main employee benefit plans are in Switzerland, Germany and Sweden, the plan in Switzerland being administered by a legally autonomous organization.

Employee benefit plan in Switzerland All RUAG employees in Switzerland have been insured against the risks of old age, death and disability with the Group employee benefit fund VORSORGE RUAG. VORSORGE RUAG is a fully autonomous employee benefit fund set up in line with the Swiss defined contribution system. It has the legal status of a foundation. In addition to the compulsory benefits, the employee benefit fund also provides benefits over and above the compulsory minimum under the Swiss Federal Act on Occupational Retirement, Survivors' and Disability Pension Schemes (BVG). It is registered with and regulated by the Bern supervisory authority for occupational retirement schemes and foundations. VORSORGE RUAG is subject to the provisions of the BVG. Under those provisions, the management body of the employee benefit fund is also responsible for ensuring that, in the event of a deficit, restructuring measures are decided and implemented so as to restore the funding level of future employee benefits to 100 % within a reasonable period. These measures include making additional contributions to rehabilitate the fund. Key decisions concerning the benefits offered by VORSORGE RUAG are taken by the Foundation Board, which is made up of four employee and four employer representatives.

Management staff at RUAG Switzerland are also insured under the KADERVORSORGE RUAG plan. KADERVORSORGE RUAG is an addition to VORSORGE RUAG and exclusively provides benefits over and above the compulsory minimum. As part of the management insurance, the bonuses of the management staff are insured. It is conceived as a defined contribution plan and only provides lump-sum payments (no pensions). In the event of death or disability, a risk capital payment is made in addition to the saved capital which is financed by risk contributions.

Employee benefit plan in Germany There are pension commitments in Germany with respect to active and retired employees which cover old-age, loss of income and survivors' pensions. Benefits are essentially divided into a basic pension scheme, which – except for a few transitional arrangements – was managed by the Dynamit Nobel VVaG pension fund until 31 March 2016 and since 1 April 2016 has been managed as a defined benefit scheme of RUAG Ammotec GmbH, and a supplementary pension scheme which is run directly via RUAG Ammotec GmbH as a defined benefit scheme. The basic pension is determined by salary components up to the contribution assessment ceiling in the statutory pension insurance scheme. The supplementary pension is made up of salary-dependent contributions for remuneration components above the contribution assessment ceiling.

A three-part pension commitment has been put in place for certain management staff. This is composed of a basic pension primarily based on final salary, and two defined contribution components. The annual increment of the pension entitlement in this case is based on the bonus awarded or on a conversion of earnings into pension contributions (whereby the employees decide, within predefined limits, on the percentage to be converted) and is topped up by an additional contribution from the employer.

Employee benefit plan in Sweden The existing ITP plan was renegotiated with effect from 1 January 2007, and became a defined contribution plan (ITP 1) from that point onwards. However, all staff born before 1979 are still insured under the ITP 2 defined benefit plan. Alongside a final salary retirement pension, the plan also includes surviving dependants' and disability pension cover provided by Alecta.

In addition to the defined benefit obligations, the Group provides other long-term employee benefits comprising loyalty bonuses and anniversary benefits (see Note 26, "Provisions").

The following table shows the economic benefit and economic liability at the end of the reporting year and the previous year, and the corresponding development of benefit plan expenses:

in CHF m	Surplus/deficit in accordance with FER 26	2017 Group's economic share	2016 Group's economic share	Foreign currency translation adjustments	Year-on-year changes/expenses for reporting period	Contributions accrued for the period	2017 Expense of benefit plans in personnel expenses	Year-on-year changes/expenses for reporting period	2017 Expense of benefit plans in financial result	2016 Expense of benefit plans in personnel expenses	2016 Expense of benefit plans in financial result
Patronal financing foundation	161	—	—	—	—	—	—	—	—	—	—
Benefit plans without surplus/deficit	—	(2)	(1)	0	1	48	49	0	0	46	0
Benefit plans with surplus	—	—	—	—	—	—	—	—	—	2	—
Benefit plans with deficit	—	—	—	—	—	—	—	—	—	—	—
Benefit plans without plan assets	—	(69)	(57)	4	2	—	2	5	5	0	5
Total	161	(70)	(58)	5	3	48	51	5	5	49	5

The free reserves of the patronal financing foundation are not designated for economic use by the Group. The benefit plans without surplus/deficit include the VORSORGE RUAG defined benefit plan and the defined benefit basic pension scheme in Germany. Unlike in the previous year, the KADERVORSORGE RUAG management plan no longer showed a surplus. The recognized economic liabilities for benefit plans without plan assets, i.e. unfunded plans, amount to CHF 69 million (previous year: CHF 57 million) and mainly relate to the pension plans in Germany and Sweden.

The following table contains a summary of the benefit and contribution plan expenses for the reporting year and the previous year:

in CHF m	2017 Switzerland	2017 Abroad	2017 Total	2016 Switzerland	2016 Abroad	2016 Total
Contributions to benefit and contribution plans at expense of Group companies	39	10	48	39	9	48
Contributions to benefit and contribution plans from employer contribution reserves	—	—	—	—	—	—
Total contributions	39	10	48	39	9	48
+/– change in ECR from portfolio performance, impairment etc.	—	—	—	—	—	—
Contributions and change in employer contribution reserves	39	10	48	39	9	48
Decrease/Increase in economic liability of Group from benefit plans without surplus/deficit	—	1	1	—	0	0
Decrease/Increase in economic liability of Group (plans without plan assets)	—	2	2	—	0	0
Total change in economic impact from surpluses/deficits	—	3	3	—	1	1
Expense of benefit and contribution plans in personnel expenses for period	39	13	51	39	10	49
Decrease/Increase in economic liability of Group from benefit and contribution plans without surplus/deficit	—	0	0	—	0	0
Decrease/Increase in economic liability of Group (plans without plan assets)	—	5	5	—	5	5
Total change in economic impact from surpluses/deficits	—	5	5	—	5	5
Expense of benefit and contribution plans in financial result for period	—	5	5	—	5	5
Total expense of benefit and contribution plans for period	39	17	56	39	14	54

The change in recognized economic liabilities from benefit plans and paid-in employer contributions for the reporting year amount to CHF 56 million (previous year: CHF 54 million) and are included in personnel expenses/financial result.

28 Share capital

The share capital comprises a total of 340,000 fully paid-up shares with a par value of CHF 1,000 each. There is no conditional share capital. All shares in RUAG Holding Ltd are owned by the Swiss Confederation.

29 Contingent liabilities towards third parties

in CHF m	2017	2016
Group guarantees	29	29
Total contingent liabilities towards third parties	29	29

Group guarantees are primarily performance and bid guarantees from operational business.

30 Additional contingent liabilities not stated on the balance sheet

in CHF m	2017	2016
Agreed contractual penalties (fines and premiums)	6	2
Legal proceedings	0	0
Bill commitments	—	—
Capital commitments for property, plant and equipment (incl. investment properties)	21	22
Other liabilities not stated on the balance sheet	2	2
Total contingent liabilities not stated on the balance sheet	29	25

Contractual penalties By the nature of its operations, RUAG has to deal with contractual penalties. The amounts reported reflect all agreed contractual penalties as at the end of the reporting period. These obligations are regularly reassessed. As soon as it is probable that a cash outflow will arise, a provision is recognized for it. The possibility of a cash outflow over and above the recognized provisions is currently considered improbable.

Legal proceedings Open or potential legal proceedings are handled by Corporate Legal & Secretary General and regularly monitored as to the probability of a future cash outflow. As soon as it is probable that a cash outflow will arise, a provision is recognized for it. The possibility of a cash outflow over and above the recognized provisions is currently considered improbable.

Capital commitments Capital commitments include the value of investments to which RUAG has committed as at the end of the reporting period.

31 Future minimum commitments from leasing transactions

Finance leases

in CHF m	2017	2016
Within 1 year	0	0
Later than 1 year, within 5 years	0	0
After 5 years	—	—
Total	0	1
Less future interest costs	(0)	(0)
Total lease liabilities recognized	0	1

Operating leases

in CHF m	2017	2016
Within 1 year	22	21
Later than 1 year, within 5 years	47	54
After 5 years	13	13
Total	83	88

These comprise unrecognized obligations under operating leases (including rental agreements).

32 Assets pledged as collateral

in CHF m	2017	2016
Cash and cash equivalents	—	—
Receivables and inventories	—	—
Plant and equipment	0	0
Property	3	2
Total assets pledged as collateral	3	2

33 Related party transactions

in CHF m	2017	2016
Receivables from related parties	30	53
Liabilities to related parties	(0)	(0)
Prepayments from related parties	(65)	(47)
Current liabilities to employee benefit funds	—	—
Non-current liabilities to employee benefit funds	—	—

In the year under review, CHF 30 million of receivables from related parties (previous year: CHF 53 million) and CHF 0.0 million of liabilities to related parties (previous year: CHF 0.1 million) were attributable to the DDPS. Invoiced sales to the DDPS totalled CHF 590 million (previous year: CHF 568 million) as stated in Note 6, “Net sales”. In return, the DDPS supplied materials and services totalling CHF 6 million (previous year: CHF 18 million). There were no loans between the Group companies and members of the Board of Directors. CHF 0.3 million (previous year: CHF 0.3 million) was generated with associates, and services with a value of CHF 3.0 million (previous year: CHF 3.0 million) purchased.

34 Compensation of key management personnel

in CHF thousands	2017	2016
Highest overall compensation in the Executive Board according to executive pay reporting (Arts. 3 and 5 of the Management Salaries Ordinance)[1]	795	912

The overall emoluments paid to non-executive members of the Board of Directors for the 2017 financial year amounted to CHF 730,000 (previous year: CHF 804,000). The overall emoluments paid to the CEO and the Management Board for the 2017 financial year amounted to CHF 6,058,000 (previous year: CHF 6,374,000).[2] The total remuneration for the CEO amounted to CHF 892,000 in the year under review (previous year: 1,022,000).[2]

Overview of compensation paid to members of the Board of Directors and the Group Executive Board:

	Total		Maximum overall compensation	
in CHF thousands	2017	2016	2017	2016
Basic salary of Board of Directors[3]				
Cash compensation	730	804	198	198
Total compensation paid to members of the Board of Directors[3]	730	804	198	198
Basic salary of Group Executive Board[4]				
Cash compensation	4 069	3 596	585	549
Benefits in kind	95	91	9	9
Employer contributions to pension funds	447	428	80	75
Performance-based component, Group Executive Board				
Cash compensation[5]	1 334	2 065	201	354
Employer contributions to pension funds	113	194	17	35
Other long-term employee benefits	—	—	—	—
Total compensation paid to members of the Group Executive Board[4]	6 058	6 374	892	1 022
of which cash compensation	5 403	5 661	786	903
of which benefits in kind	95	91	9	9
of which employer contributions to pension funds	560	622	97	110
of which other long-term employee benefits	—	—	—	—
Relation between performance-related component and cash compensation	33 %	57 %	34 %	64 %
Total compensation paid to members of the Board of Directors and Group Executive Board[3, 4]	6 788	7 178		
of which short-term employee benefits[6]	6 228	6 556		
of which employer contributions to pension funds	560	622		
of which other long-term employee benefits	—	—		

[1] Other than disclosures under international standards, the federal government's Management Salaries Ordinance stipulates that the employer’s pension fund contributions should not be included in the figure for overall compensation.
[2] The overall emoluments are exclusive of the employer's social insurance contributions.
[3] In the year under review, one member of the Board of Directors stepped down as of 27 April 2017; this position subsequently remained vacant.
[4] Changes within the Executive Board during the year under review resulted in temporary incumbent overlaps, which in turn gave rise to higher costs.
[5] Incl. LTI entitlements from the 2015–2017 LTI Plan (previous year: 2014–2016).
[6] Includes cash compensation and benefits in kind.

35 Risk management process, financial risk management and capital management

Risk management process

The risk management system of RUAG differentiates between strategic and operational risks and focuses on relevant topics from the perspective of the Group and the divisions. Risks are identified, assessed and monitored in the individual divisions using a structured, bottom-up risk assessment. In order to prevent or reduce the individual risks, the appropriate measures are defined and implemented. At Group level, the aggregate risks relevant for the Group are monitored and managed by the Group Executive Board.

The risks identified are assessed in terms of probability of occurrence and impact, and are entered on the Group's risk map. This risk map is periodically discussed with the Group Executive Board, the Audit Committee and the entire Board of Directors. Depending on the way responsibilities are defined, the Group Executive Board or divisional management are responsible for the ongoing monitoring, control and management of risks. As part of this, the management is supported by the Risk Manager in training sessions or moderating workshops.

Financial risk management
RUAG is exposed to various financial risks as a result of its business activities. The most significant financial risks arise from changes in exchange rates, interest rates and commodity prices. A further risk is the ability to secure adequate liquidity.

Financial risk management is a corporate function and is carried out at Group level by the Treasury department in compliance with the directives issued by the Board of Directors. The Treasury identifies, evaluates and hedges financial risks in close cooperation with the operating units (divisions).

a. Market risks
RUAG is exposed to market risks that largely relate to changes in exchange and interest rates and would therefore impact the value of the financial instruments held or the income/expenses associated with these. The Group monitors these risks continuously. It employs a number of derivative financial instruments to manage the volatility associated with these risks. The Group's objective is to reduce – where appropriate – fluctuations in earnings and cash flows associated with changes in interest rates, exchange rates and the value of financial assets.

In compliance with Group policy, RUAG employs derivative financial instruments (e.g. foreign currency forward transactions) to manage risk. RUAG avoids any financial transaction in which the risk cannot be gauged at the time the transaction is concluded. The Group does not sell any assets that it does not own or does not know that it will own. RUAG sells only existing assets and hedges only existing transactions and (in the case of forward hedges) forecasted transactions that can be expected to materialize on the basis of past experience.

Exchange rate risk The consolidated financial statements are presented in Swiss francs (CHF). The Group is mainly subject to changes in the exchange rates of the euro, US dollar, Swedish krona and pound sterling. In the case of transaction risk, it faces the risk of fluctuations in the value of foreign currencies between the date of a contractual agreement and the actual date of payment. Accordingly, RUAG employs different contracts to compensate for exchange rate-induced changes in asset values, firm commitments and forecasted transactions. RUAG also employs forward transactions and currency options to hedge certain cash flows anticipated in foreign currency.

At the end of the reporting period and of the previous year, the following foreign currency positions were recognized in the balance sheet in relation to financial assets and liabilities:

as at 31 December 2017

in CHF m	EUR	USD	SEK	GBP	Other
Cash and cash equivalents	42	20	10	14	11
Trade receivables/other receivables	123	83	7	7	4
Other financial assets	3	4	1	—	0
Financial liabilities	(35)	(0)	(0)	(43)	(1)
Trade accounts payable/other liabilities	(48)	(15)	(13)	(3)	(5)
Other financial liabilities	—	—	(1)	—	—
Total foreign currency positions as at balance-sheet date from financial assets and liabilities	85	92	3	(25)	9

as at 31 December 2016

in CHF m	EUR	USD	SEK	GBP	Other
Cash and cash equivalents	55	27	10	2	6
Trade receivables/other receivables	106	70	9	2	3
Other financial assets	1	3	1	0	0
Financial liabilities	(4)	(7)	(0)	(0)	(0)
Trade accounts payable/other liabilities	(61)	(27)	(13)	(1)	(2)
Other financial liabilities	—	—	(1)	—	—
Total foreign currency positions as at balance-sheet date from financial assets and liabilities	97	65	6	3	6

The following currency hedging transactions existed as at 31 December:

Volume of contracts

in CHF m	2017	2016
Currency hedging contracts banks	303	288
Currency hedging contracts banks	(95)	(89)

Carrying amount

in CHF m	2017	2016
Current financial assets	6	4
Current financial liabilities	(6)	(12)

The carrying amounts only contain the positive and negative replacement values from foreign currency forward transactions that are recognized at fair value. The following tables show the contractual due dates of the foreign currency forward transactions held by RUAG at the end of the reporting and the previous year:

as at 31 December 2017

in CHF m	Up to 1 year	Up to 2 years	Up to 3 years	Over 3 years	Total
Foreign currency forward transactions used for hedging purposes:					
Outflows	(5)	(1)	(0)	(0)	(6)
Inflows	6	0	0	0	6
	1	(1)	(0)	(0)	0

as at 31 December 2016

in CHF m	Up to 1 year	Up to 2 years	Up to 3 years	Over 3 years	Total
Foreign currency forward transactions used for hedging purposes:					
Outflows	(10)	(1)	(1)	(0)	(12)
Inflows	3	1	—	—	4
	(7)	(1)	(1)	(0)	(8)

Hedge accounting RUAG carries out foreign currency forward transactions to hedge future transactions in relation to its operational business (hedging future revenues or purchases of goods and services in the corresponding currencies); these hedging transactions have been designated for hedge accounting. The hedging reserve under shareholders' equity (other reserves) included the following as at 31 December:

in CHF m	2017	2016
Other reserves	(2)	(8)

Due to the occurrence of the underlying transactions, CHF 2 million was booked out of other reserves under shareholders' equity in the reporting year and shown under other operating income (previous year: CHF 3 million in other operating expenses).

RUAG Holding Ltd provides certain foreign Group companies with loans in EUR and AUD. These loans are not hedged. As at 31 December 2017, there were loans totalling EUR 176 million (previous year: EUR 175 million) and AUD 15 million (previous year: AUD 15 million). As these loans are equity-like loans (because they are not scheduled or likely to be repaid in the foreseeable future), any foreign currency gains or losses are recognized directly in equity. The cumulative foreign exchange losses booked to equity that relate to these loans was CHF 25 million as at 31 December 2017 (previous year: CHF 25 million).

Interest rate risk RUAG is exposed to interest rate risks arising from the volatility of market interest rates. Demand deposits and money market investments are subject to an interest rate risk that can impact on net profit. Interest-bearing financial liabilities largely comprise loans from financial institutions with variable interest rates. Due to the negative interest rate policy introduced by the Swiss National Bank and the positive net financial position as at 31 December 2017, RUAG is also exposed to the risk of negative interest rates.

Interest-bearing financial liabilities

as at 31 December, in CHF m	2017	2016
Current financial liabilities	50	1
Non-current financial liabilities	76	0
Total interest-bearing financial liabilities	127	1
Of which variable interest-bearing	127	0
Fixed through interest rate swap	—	—
Variable interest-bearing, net	127	0

Interest expense for interest-bearing financial liabilities in the year under review amounted to CHF 1 million (previous year: CHF 0 million).

Commodity price risk In buying commodities (particularly copper, lead, zinc, aluminium, etc.) to be used as raw materials in production, the company is subject to a price risk. Commodity price changes can affect the gross profit margins of the operations concerned. Therefore, RUAG uses primarily lead swaps to minimize the price fluctuation risk of planned purchases.

The following hedging transactions existed as at 31 December:

Volume of contracts

in CHF m	2017	2016
Lead price hedging contracts banks	9	13

Replacement values

in CHF m	2017	2016
Positive replacement value banks	1	2
Negative replacement value banks	—	(0)

The following table shows an overview of the annual consumption of commodities.

Consumption

in CHF m	2017	2016
Aluminium	2	3
Lead	15	12
Copper	17	26
Steel	3	3
Zinc	3	4
Other	0	0
Total	40	50

b. Credit risk

Credit risks arise in particular when customers are not in a position to fulfil their contractual commitments. To manage this risk, the Group periodically evaluates customers' solvency. Around 31 % (previous year: 31 %) of the Group's sales are attributable to the DDPS. No other customer accounts for more than 10% of the Group's sales, with the exception of Airbus.

Trade and other receivables from the DDPS account for around 12 % (previous year: 20 %) of total trade and other receivables as at 31 December 2017. As at the balance-sheet date, there are no heavily concentrated default risks with regard to the recognized trade receivables.

The carrying amount of financial assets corresponds to the maximum credit risk and is composed as follows:

in CHF m	2017	2016
Cash and cash equivalents	201	239
Current financial assets	7	4
Trade receivables/other receivables		
Other current receivables	284	288
Non-current financial assets	3	3
Total credit risk	494	534

Counterparty risk comprises the risk of default on derivative financial instruments and money market transactions and the credit risk on current account balances and time deposits. Default risk and credit risk are minimized by choosing as counterparties only banks and financial institutions that have an optimum credit rating when the transaction is concluded. These risks are regularly monitored to ensure that they remain within the prescribed parameters. Group guidelines ensure that the credit risk in respect of financial institutions is limited. At present, the Group does not expect any losses arising from counterparties' non-fulfilment of their contractual obligations.

c. Liquidity risk

Liquidity risk describes the risk that arises if the Group is not in a position to fulfil its obligations when due or at a reasonable price. Group Treasury is responsible for monitoring liquidity, financing and repayment. In addition, management controls processes and guidelines in this connection. To maintain flexibility, RUAG manages its liquidity risk on a consolidated basis, drawing on business policy, tax and financial considerations and, if necessary, various funding sources. A rolling liquidity plan is drawn up on the basis of expected cash flows and is regularly updated.

The net financial position is a key measure of liquidity management. The table below provides an analysis of the Group's net financial position by due date from the end of the reporting period to the contractual expiry date.

As at 31 December 2017

in CHF m	Up to 1 year	Up to 2 years	Up to 3 years	Up to 4 years	Over 4 years	Total
Cash and cash equivalents	201	—	—	—	—	201
Current financial assets[1]	1	—	—	—	—	1
Non-current financial assets	—	0	0	0	2	3
Current financial liabilities[1]	(50)	—	—	—	—	(50)
Non-current financial liabilities	—	(30)	(30)	(15)	(1)	(76)
Other non-current financial liabilities	—	(0)	(0)	(0)	(0)	(1)
Net financial position	152	(30)	(30)	(15)	0	77
Prepayments from customers						213
Net financial position excl. customer prepayments						(136)

As at 31 December 2016

in CHF m	Up to 1 year	Up to 2 years	Up to 3 years	Up to 4 years	Over 4 years	Total
Cash and cash equivalents	239	—	—	—	—	239
Current financial assets[1]	0	—	—	—	—	0
Non-current financial assets	—	0	0	0	2	3
Current financial liabilities[1]	(1)	—	—	—	—	(1)
Non-current financial liabilities	—	(0)	(0)	(0)	—	(0)
Other non-current financial liabilities	—	(1)	(0)	(0)	(3)	(4)
Net financial position	239	(1)	(0)	(0)	(1)	237
Prepayments from customers						182
Net financial position excl. customer prepayments						55

[1] Cash flow hedges recognized in current financial assets and liabilities are not part of the net financial position as they are not interest-bearing.

Capital management

In managing capital, RUAG's aims to ensure that the Group can continue its operating activities, that the owner receives an adequate return and that the balance sheet structure is optimized with regard to the cost of capital. In order to meet these objectives, RUAG can apply for higher or lower dividend payments, repay capital to the shareholder, issue new shares, or dispose of assets in order to reduce debt. RUAG monitors its capital structure on the basis of net financial position and equity. The net financial position is the sum of cash and cash equivalents, current and non-current financial assets minus current and non-current financial liabilities and other non-current liabilities.

36 Events after the reporting period

On 28 February 2018, the Board of Directors of RUAG Holding Ltd approved the consolidated financial statements for publication. As at this time, no significant events had occurred after the reporting period. In particular, no events had transpired that would have required the carrying values of the Group's assets and liabilities to be adjusted or that would have to be disclosed at this point. The right to approve the consolidated financial statements rests with the annual shareholders' meeting.

37 Consolidated companies, associates and non-controlling interests (as at 31 December 2017)

Company	Head office	Country	Equity capital (100 %)		Shareholding	Consolidation method
RUAG Holding Ltd[1]	Bern	Switzerland	CHF	340 000 000		Full
Consolidated companies						
RUAG Switzerland Ltd	Emmen	Switzerland	CHF	112 200 000	100.0 %	Full
RUAG Ammotec AG	Thun	Switzerland	CHF	12 000 000	100.0 %	Full
RUAG Real Estate Ltd	Bern	Switzerland	CHF	8 000 000	100.0 %	Full
RUAG Ammotec Schweiz AG	Winterthur	Switzerland	CHF	300 000	100.0 %	Full
RUAG Environment Ltd	Schattdorf	Switzerland	CHF	100 000	100.0 %	Full
RUAG Corporate Services Ltd	Bern	Switzerland	CHF	100 000	100.0 %	Full
RUVEX Ltd	Bern	Switzerland	CHF	100 000	100.0 %	Full
brings! AG	Schattdorf	Switzerland	CHF	100 000	55.0 %	Full
RUAG Deutschland GmbH	Wessling	Germany	EUR	1 000 000	100.0 %	Full
RUAG Aerospace Services GmbH	Wessling	Germany	EUR	1 000 000	100.0 %	Full
RUAG Aerospace Structures GmbH	Wessling	Germany	EUR	25 000	100.0 %	Full
RUAG Defence Deutschland GmbH	Wedel	Germany	EUR	260 000	100.0 %	Full
HTS Hoch Technologie Systeme GmbH	Coswig	Germany	EUR	26 000	100.0 %	Full
GEKE Schutztechnik GmbH	Lichtenau	Germany	EUR	25 000	51.0 %	Full
RUAG Ammotec Deutschland GmbH	Fürth	Germany	EUR	100 000	100.0 %	Full
RUAG Ammotec GmbH	Fürth	Germany	EUR	25 000	100.0 %	Full
Clearswift GmbH	Cologne	Germany	EUR	27 892	100.0 %	Full[5]
RUAG Sweden AB	Gothenburg	Sweden	SEK	100 000	100.0 %	Full
RUAG Space AB	Gothenburg	Sweden	SEK	15 000 000	100.0 %	Full
Norma Precision AB	Amotfors	Sweden	SEK	2 500 000	100.0 %	Full
Gyttorp AB	Ingelstad	Sweden	SEK	701 400	100.0 %	Full[4]
Gyttorp Cartridge Company AB	Nora	Sweden	SEK	1 000 000	100.0 %	Full[4]
Gyttorp Jakt AB	Karlskoga	Sweden	SEK	300 000	100.0 %	Full[4]
RUAG Australia PTY Ltd.	Bayswater	Australia	AUD	10 000	100.0 %	Full
Clearswift (Asia/Pacific) Pty Ltd	North Sydney	Australia	AUD	1 720 000	100.0 %	Full[5]
RUAG Ammotec Benelux BVBA	Boechout	Belgium	EUR	25 000	100.0 %	Full
RUAG Ammotec UK Ltd.	Liskeard	UK	GBP	15 000	100.0 %	Full
Clearswift Holding Ltd	Reading	UK	GBP	1	100.0 %	Full[5]
Clearswift Ltd	Reading	UK	GBP	15 114 616	100.0 %	Full[5]
Content Technologies Holdings Ltd	Reading	UK	GBP	52 148	100.0 %	Full[5]
Newincco 1130 Ltd	Reading	UK	GBP	0.1	100.0 %	Full[5]
Clearswift Group Ltd	Reading	UK	GBP	0	100.0 %	Full[5]
Clearswift Systems Ltd	Reading	UK	GBP	0	100.0 %	Full[5]
RUAG Space Finland Oy AB	Tampere	Finland	EUR	2 500	100.0 %	Full
Gyttorp Finland Oy	Malax	Finland	EUR	33 638	100.0 %	Full[4]
RUAG Holding France SAS	Terssac	France	EUR	100 000	100.0 %	Full
RUAG Defence France SAS	Terssac	France	EUR	400 000	100.0 %	Full
RUAG Ammotec France SAS	Paris	France	EUR	1 000 000	100.0 %	Full
RUAG Ammotec Italia s.r.l.	Brescia	Italy	EUR	100 000	100.0 %	Full[5]
Clearswift KK	Tokyo	Japan	JPY	20 000 000	100.0 %	Full[5]
RUAG Aviation Malaysia SDN BHD	Kuala Lumpur	Malaysia	MYR	1 500 100	65.0 %	Full
RUAG Ammotec Austria GmbH	Vienna	Austria	EUR	297 959	100.0 %	Full
RUAG Space GmbH	Vienna	Austria	EUR	1 500 000	100.0 %	Full
Clearswift Espana SL	Madrid	Spain	EUR	3 100	100.0 %	Full[5]
RUAG Hungarian Ammotec Inc.	Sirok	Hungary	HUF	280 000 000	100.0 %	Full
RUAG Aerostructures Hungary Zrt	Eger	Hungary	HUF	600 000 000	100.0 %	Full

1 RUAG Holding Ltd, Stauffacherstrasse 65, P.O. Box, CH-3000 Bern 22.

2 Investments of between 20 % and 50 % are measured using the equity method.

3 Non-material investments are valued at cost minus a valuation allowance.

4 As of 31 March 2017, Norma Precision AB acquired the remaining 60 % of the outstanding shares of Gyttorp AB (incl. the investments in Gyttorp Cartridge Company AB, Gyttorp Jakt AB and Gyttorp Finland OY), headquartered in Ingelstad (Sweden) and fully consolidated it from this date. In the previous year, these investments were valued at cost minus a valuation allowance.

5 As of 20 January 2017, RUAG Holding Ltd acquired 100 % of the shares of Clearswift, headquartered in Reading (UK) and fully consolidated it from 1 February 2017. As of 1 January 2017, RUAG Ammotec Deutschland GmbH acquired 100 % of the shares of RUAG Ammotec Italia s.r.l. (previously Turfer di Turelli Luca & C. SRL), domiciled in Brescia (Italy) and fully consolidated it from this date.

Company	Head office	Country	Equity capital (100 %)		Shareholding	Consolidation method
RUAG Ammotec USA Inc.	Tampa, FL	USA	USD	6 500 000	100.0 %	Full
Mecanex USA Inc.	Berlin, CT	USA	USD	1 500	100.0 %	Full
RUAG Holding USA Inc.	Huntsville, AL	USA	USD	0.1	100.0 %	Full
RUAG Space USA Inc.	El Segundo, CA	USA	USD	1 000	100.0 %	Full
Clearswift Corporation	Mount Laurel, NJ	USA	USD	12 000 000	100.0 %	Full [5]
RUAG Simulation Company LLC	Abu Dhabi	UAE	AED	150 000	49.0 %	Full
RUAG Space LLC in liquidation	Zurich	Switzerland	CHF	20 000	100.0 %	[3]
Stadeln Genehmigungshaltergesellschaft mbH	Fürth	Germany	EUR	25 000	78.6 %	[3]
RUAG Industria e Comercio de Municoes Ltda	São Francisco	Brazil	BRL	200 000	100.0 %	[3]
RUAG do Brasil Serviços Aeronáuticos Ltda	Rio de Janeiro	Brazil	BRL	10 000	90.0 %	[3]
NET-TEL Computer Systems Limited	Reading	UK	GBP	1	100.0 %	[3]
Associates[2]						
Nitrochemie AG	Wimmis	Switzerland	CHF	1 000 000	49.0 %	Equity
Nitrochemie Wimmis AG	Wimmis	Switzerland	CHF	25 000 000	45.0 %	Equity
Nidwalden AirPark Ltd	Stans	Switzerland	CHF	1 000 000	40.0 %	Equity
Nitrochemie Aschau GmbH	Aschau	Germany	EUR	7 700 000	45.0 %	Equity
Other investments						
Visier Medien Holding AG	Zug	Switzerland	CHF	400 000	49.5 %	[3]
CFS Engineering SA	Ecublens	Switzerland	CHF	150 000	40.0 %	[3]
AIONAV Systems Ltd	Muri bei Bern	Switzerland	CHF	100 000	12.0 %	[3]
Switzerland Innovation Park Biel/Bienne Ltd	Biel/Bienne	Switzerland	CHF	1 540 000	6.50 %	[3]
Flughafen Bern AG	Bern	Switzerland	CHF	14 310 000	1.4 %	[3]
Brünig Indoor Aktiengesellschaft	Lungern	Switzerland	CHF	3 400 000	0.3 %	[3]
Arianespace Participation	Evry	France	EUR	3 937 983	3.5 %	[3]
VDL-RUAG Shelters B.V.	Eindhoven	Netherlands	EUR	50 000	40.0 %	[3]

1 RUAG Holding Ltd, Stauffacherstrasse 65, P.O. Box, CH-3000 Bern 22.

2 Investments of between 20 % and 50 % are measured using the equity method.

3 Non-material investments are valued at cost minus a valuation allowance.

4 As of 31 March 2017, Norma Precision AB acquired the remaining 60 % of the outstanding shares of Gyttorp AB (incl. the investments in Gyttorp Cartridge Company AB, Gyttorp Jakt AB and Gyttorp Finland OY), headquartered in Ingelstad (Sweden) and fully consolidated it from this date. In the previous year, these investments were valued at cost minus a valuation allowance.

5 As of 20 January 2017, RUAG Holding Ltd acquired 100 % of the shares of Clearswift, headquartered in Reading (UK) and fully consolidated it from 1 February 2017. As of 1 January 2017, RUAG Ammotec Deutschland GmbH acquired 100 % of the shares of RUAG Ammotec Italia s.r.l. (previously Turfer di Turelli Luca & C. SRL), domiciled in Brescia (Italy) and fully consolidated it from this date.

KPMG AG
Audit
Hofgut
CH-3073 Gümligen-Bern
PO Box 112
CH-3000 Bern 15
Telephone +41 58 249 76 00
Fax +41 58 249 76 17
www.kpmg.ch

Report of the Statutory Auditor to the General Meeting of Shareholders of

RUAG Holding Ltd, Bern

Report of the Statutory Auditor on the Consolidated Financial Statements

As statutory auditor, we have audited the accompanying consolidated financial statements of RUAG Holding Ltd, which comprise the income statement, balance sheet, statement of cash flows, statement of changes in equity and notes (pages 32 to 74), for the year ended 31 December 2017.

Board of Directors' Responsibility
The board of directors is responsible for the preparation of the consolidated financial statements in accordance with Swiss GAAP FER and the requirements of Swiss law. This responsibility includes designing, implementing and maintaining an internal control system relevant to the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error. The board of directors is further responsible for selecting and applying appropriate accounting policies and making accounting estimates that are reasonable in the circumstances.

Auditor's Responsibility
Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with Swiss law and Swiss Auditing Standards. Those standards require that we plan and perform the audit to obtain reasonable assurance whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers the internal control system relevant to the entity's preparation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control system. An audit also includes evaluating the appropriateness of the accounting policies used and the reasonableness of accounting estimates made, as well as evaluating the overall presentation of the consolidated financial statements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion
In our opinion, the consolidated financial statements for the year ended 31 December 2017 give a true and fair view of the financial position, the results of operations and the cash flows in accordance with Swiss GAAP FER and comply with Swiss law.

KPMG

RUAG Holding Ltd, Bern
Report of the Statutory Auditor
on the Consolidated Financial Statements
to the General Meeting of Shareholders

Report on Other Legal Requirements

We confirm that we meet the legal requirements on licensing according to the Auditor Oversight Act (AOA) and independence (article 728 CO) and that there are no circumstances incompatible with our independence.

In accordance with article 728a paragraph 1 item 3 CO and Swiss Auditing Standard 890, we confirm that an internal control system exists, which has been designed for the preparation of consolidated financial statements according to the instructions of the board of directors.

We recommend that the consolidated financial statements submitted to you be approved.

KPMG AG

Herbert Bussmann
Licensed Audit Expert
Auditor in Charge

Florin Janine Krapp
Licensed Audit Expert

Gümligen-Bern, 28 February 2018

Income statement for 1 January to 31 December

in CHF m	Note	2017	2016
Dividend income	2.5	75	110
Income from services		4	4
Total operating income		80	114
Personnel expenses		(0)	(0)
Other operating expenses	2.6	(9)	(8)
Total operating expenses		(9)	(8)
Operating profit/loss		70	106
Financial income			
Interest income		11	7
Currency gains		1	—
Financial expenses			
Interest expense		(1)	(0)
Currency losses		—	(2)
Pre-tax net profit		81	111
Income taxes		(1)	(1)
Net profit for the year		80	110

The notes to the financial statements on pages 79 to 81 form an integral part of the financial statements.

Balance sheet as at 31 December

in CHF m	Note	2017	2016
Cash and cash equivalents		123	160
Current financial assets			
Due to third parties		1	—
Due to companies in which the entity holds an investment		92	34
Other current receivables			
Due to third parties		0	0
Due to companies in which the entity holds an investment		18	6
Prepaid expenses and accrued income		2	—
Total current assets		236	200
in % of total assets		18%	17%
Financial assets			
Due to third parties		0	0
Due to companies in which the entity holds an investment		390	364
Investments	2.1	709	646
Intangible assets		0	0
Total non-current assets		1 100	1 009
in % of total assets		82%	83%
Total assets		1 335	1 209
Current interest-bearing liabilities			
Due to third parties		50	—
Due to companies in which the entity holds an investment		154	131
Other current interest-bearing liabilities			
Due to companies in which the entity holds an investment		13	73
Other current liabilities			
Due to third parties		1	1
Current provisions		1	—
Deferred income and accrued expenses			
Due to third parties		0	1
Due to companies in which the entity holds an investment		1	—
Total current liabilities		220	205
Non-current interest-bearing liabilities			
Due to third parties		75	—
Non-current provisions		3	—
Total non-current liabilities		79	—
Total liabilities		298	205
in % of total liabilities and equity		22%	17%
Share capital	2.3	340	340
Legal capital reserve			
Reserves from capital contributions	2.4	10	10
Legal retained earnings			
General legal retained earnings		47	42
Voluntary retained earnings			
Balance sheet profit			
Net profit brought forward		560	503
Net profit for the year		80	110
Total equity		1 037	1 004
in % of total liabilities and equity		78%	83%
Total liabilities and equity		1 335	1 209

The notes to the financial statements on pages 79 to 81 form an integral part of the financial statements.

1 Principles

1.1 General
The key applied accounting principles that are not stipulated by law are described below. Here it must be noted that in order to ensure its long-term success, the company has made use of the option to create and release hidden reserves.

1.2 Financial assets
The financial assets include long-term loans. Loans provided in foreign currencies are valued using the closing rates on the balance-sheet date; in this regard, unrealized losses are recognized, while unrealized profits are not (imparity principle).

1.3 Investments
Investments are measured at cost minus the required impairment. The carrying amounts are reviewed on an annual basis with regard to their value and, if necessary, written down. The valuations are checked in accordance with the individual valuation principle.

1.4 Foreign currency forward transactions
Positive and negative replacement values of foreign currency forward transactions are not measured during their life because the net principle is applied. The contract volumes and replacement values of current transactions are listed in the notes under section 2.2.

1.5 Foreign currency valuation
Current assets and liabilities in foreign currencies are valued using the closing rates on the balance-sheet date. Profits or losses are recognized on a "realized" basis. For non-current assets and liabilities, the lowest value principle applies; any unrealized foreign exchange losses are treated as an expense, while unrealized profits are not recognized in the income statement.

1.6 Non-preparation of statement of cash flows and additional details in the notes
As RUAG Holding Ltd prepares its consolidated financial statements in line with recognized accounting standards (Swiss GAAP FER), in accordance with the statutory provisions it has not provided details in the notes to the financial statements concerning interest-bearing liabilities and audit fees, and has not prepared a statement of cash flows.

2 Information on balance sheet and income statement items

2.1 Investments
a) Direct investments

Company	Head office	Country	Share of capital and voting rights 2017 in %	Share of capital and voting rights 2016 in %		Capital
RUAG Switzerland Ltd	Emmen	Switzerland	100	100	CHF	112 200 000
RUAG Ammotec AG	Thun	Switzerland	100	100	CHF	12 000 000
RUAG Real Estate Ltd	Bern	Switzerland	100	100	CHF	8 000 000
RUAG Corporate Services Ltd	Bern	Switzerland	100	100	CHF	100 000
RUAG Ammotec Schweiz AG	Winterthur	Switzerland	100	100	CHF	300 000
RUAG Deutschland GmbH	Wessling	Germany	100	100	EUR	1 000 000
RUAG Sweden AB	Gothenburg	Sweden	100	100	SEK	100 000
Clearswift Holding Ltd	Reading	UK	100	0	GBP	1
RUAG Holding France SAS	Terssac	France	100	100	EUR	100 000
RUAG Australia PTY Ltd.	Bayswater	Australia	100	100	AUD	10 000
RUAG Aerostructures Hungary Zrt.	Eger	Hungary	100	100	HUF	600 000 000
Nitrochemie AG	Wimmis	Switzerland	49	49	CHF	1 000 000
Nitrochemie Wimmis AG	Wimmis	Switzerland	45	45	CHF	25 000 000
Nitrochemie Aschau GmbH	Aschau	Germany	45	45	EUR	7 700 000

b) Material indirect investments

Company	Head office	Country	Share of capital and voting rights 2017 in %	Share of capital and voting rights 2016 in %		Capital
RUAG Aerospace Services GmbH	Wessling	Germany	100	100	EUR	1 000 000
RUAG Aerospace Structures GmbH	Wessling	Germany	100	100	EUR	25 000
RUAG Ammotec GmbH	Fürth	Germany	100	100	EUR	25 000
RUAG Space AB	Gothenburg	Sweden	100	100	SEK	15 000 000
Clearswift Ltd	Reading	UK	100	0	GBP	15 114 616

2.2 Foreign currency forward transactions

in CHF m	2017	2016
Volume of foreign currency hedging contracts with banks	303	288
Volume of foreign currency hedging contracts with banks	(95)	(89)
Volume of foreign currency hedging contracts with Group companies	93	89
Volume of foreign currency hedging contracts with Group companies	(229)	(273)
Positive replacement value banks	6	4
Negative replacement value banks	(6)	(12)
Positive replacement value Group companies	6	12
Negative replacement value Group companies	(6)	(4)
Total replacement values	(0)	(0)

The contract volumes represent the volume of open foreign currency forward transactions as at the year-end. The replacement values only contain the positive and negative replacement values from open foreign currency forward transactions as at the year-end that are recognized at fair value.

2.3 Share capital
The share capital of CHF 340 million comprises 340,000 registered shares, each with a nominal value of CHF 1,000.

2.4 Reserves from capital contributions
The reserves from capital contributions contain the premium from the non-cash contribution from the former state-owned defence company to RUAG Holding Ltd as at 1 January 1999.

2.5 Dividend income
Dividend income primarily contains the dividends from RUAG Switzerland Ltd and other investments. In the previous year, a gain of CHF 8.4 million was also recognized from the disposal of the investment in OEI Opto AG. OEI Opto AG was founded in the 2016 financial year as a vehicle for the sale of RUAG Space's Opto-Electronics & Instruments product unit (part of RUAG Switzerland Ltd).

2.6 Other operating expenses

in CHF m	2017	2016
Advertising costs	(3)	(4)
Administration costs	(2)	(1)
Management fees (cost attributed to holding company)	(4)	(3)
Total other operating expenses	(9)	(8)

3 Further information

3.1 Full-time positions
RUAG Holding Ltd does not employ any staff.

3.2 Collateral provided for third-party liabilities

in CHF m	2017	2016
Group guarantees	129	120
Total contingent liabilities	129	120

Guarantee liabilities are primarily performance and advance payment guarantees issued as part of operational business, as well as guarantees to secure bank credit limits vis-à-vis the subsidiaries. This includes a letter of support issued by RUAG Holding Ltd on 22 December 2017 with a maximum amount of AUD 16.0 million in favour of RUAG Australia PTY Ltd.

3.3 Events after the reporting period

No material events have taken place since the end of the reporting period that would have an impact on the carrying values of the assets or liabilities or would have to be disclosed here.

Proposal by the Board of Directors for the appropriation of available earnings

in CHF m	2017	2016
Balance sheet profit at the start of the financial year	560	503
Net profit for the year	80	110
Balance sheet profit at the disposal of the Annual General Meeting	640	613
The Board of Directors proposes to the Annual General Meeting the following appropriation of available earnings:		
Dividends	40	47
Allocation to general legal retained earnings	4	6
Balance to be brought forward	596	560

KPMG

KPMG AG
Audit
Hofgut
CH-3073 Gümligen-Bern

PO Box 112
CH-3000 Bern 15

Telephone +41 58 249 76 00
Fax +41 58 249 76 17
www.kpmg.ch

Report of the Statutory Auditor to the General Meeting of Shareholders of

RUAG Holding Ltd, Bern

Report of the Statutory Auditor on the Financial Statements

As statutory auditor, we have audited the accompanying financial statements of RUAG Holding Ltd, which comprise the income statement, balance sheet and notes (pages 77 to 81), for the year ended 31 December 2017.

Board of Directors' Responsibility
The board of directors is responsible for the preparation of the financial statements in accordance with the requirements of Swiss law and the company's articles of incorporation. This responsibility includes designing, implementing and maintaining an internal control system relevant to the preparation of financial statements that are free from material misstatement, whether due to fraud or error. The board of directors is further responsible for selecting and applying appropriate accounting policies and making accounting estimates that are reasonable in the circumstances.

Auditor's Responsibility
Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with Swiss law and Swiss Auditing Standards. Those standards require that we plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers the internal control system relevant to the entity's preparation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control system. An audit also includes evaluating the appropriateness of the accounting policies used and the reasonableness of accounting estimates made, as well as evaluating the overall presentation of the financial statements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion
In our opinion, the financial statements for the year ended 31 December 2017 comply with Swiss law and the company's articles of incorporation.

KPMG

RUAG Holding Ltd, Bern
Report of the Statutory Auditor
on the Financial Statements
to the General Meeting of Shareholders

Report on Other Legal Requirements

We confirm that we meet the legal requirements on licensing according to the Auditor Oversight Act (AOA) and independence (article 728 CO) and that there are no circumstances incompatible with our independence.

In accordance with article 728a paragraph 1 item 3 CO and Swiss Auditing Standard 890, we confirm that an internal control system exists, which has been designed for the preparation of financial statements according to the instructions of the board of directors.

We further confirm that the proposed appropriation of available earnings complies with Swiss law and the company's articles of incorporation. We recommend that the financial statements submitted to you be approved.

KPMG AG

Herbert Bussmann
Licensed Audit Expert
Auditor in Charge

Florin Jamne Krapp
Licensed Audit Expert

Gümligen-Bern, 28 February 2018

RUAG follows clear rules

Management and control functions at RUAG are based on the corporate governance guidelines of SIX Swiss Exchange.[1]

Board of Directors

The duties of the Board of Directors of RUAG Holding Ltd are governed by the Swiss Code of Obligations, the owner's strategy of the Swiss Federal Council, the Articles of Association and the Regulations Governing Organization and Operations. The Board of Directors of RUAG Holding Ltd currently consists of six members, none of whom performed executive functions in the year under review or in the three preceding years. In addition, the members of the Board of Directors have no material business relationship with the Group. Egon W. Behle resigned from the Board of Directors with effect from 27 April 2017. A successor is now being sought. Otherwise, no changes to the Board of Directors were made in the year under review. The list shown below provides information about the name, year of birth, function, date of joining and remaining term of office of each member of the Board of Directors. Details of nationality, education and career milestones can be found on the RUAG website.[2]

Election and term of office

The Board of Directors of RUAG Holding Ltd and its chairman are elected by the Annual General Meeting (AGM). In accordance with the Articles of Association, the Board of Directors consists of at least three individuals. The majority of the Board's members must be Swiss nationals who are resident in Switzerland. They are elected annually and individually, and may be re-elected. RUAG does not specify an age limit for members of the Board of Directors, nor does it limit their term of office.

Internal organization and tasks

The Board of Directors holds ultimate responsibility for the business strategy and overall management of the Group. Subject to the authority of the Annual General Meeting, it possesses supreme decision-making powers.

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

- The strategic orientation and management of the Group in accordance with the owner's strategy of the Swiss Federal Council
- The structuring of the accounting system, financial controlling and financial planning
- The appointment and dismissal of the CEO, other members of the Group Executive Board and other senior executives
- Supreme oversight of business activities
- Production of the Annual Report, preparation of the AGM and implementation of resolutions passed by the latter

Board of Directors

Name	Born	Function	Member since	Elected until AGM
Hans-Peter Schwald	1959	Chairman, non-executive	2002	2018
Dr. Remo Lütolf	1956	Vice-Chairman, non-executive	2014	2018
Egon W. Behle	1955	Non-executive member	2011	Resigned as of 27.4.2017
Paul Häring	1957	Non-executive member	2004	2018
Markus Hutter	1957	Non-executive member	2014	2018
Prof. Sibylle Minder Hochreutener	1973	Non-executive member	2014	2018
Jürg Oleas	1957	Non-executive member	2011	2018

[1] Unless otherwise specified, the information is applicable as at 31 December 2017.
[2] https://www.ruag.com/en/about-ruag/organisation/board-directors

Decisions are taken by the Board of Directors as a whole. To assist the Board in preparing and implementing its decisions, three committees have been formed: an Audit Committee, a Nomination & Compensation Committee, and a Strategy Committee. The Board of Directors has also formed an Advisory Board. Beside the usual six meetings, the Board of Directors met for a strategy meeting in summer 2017 and also held three extraordinary meetings. In addition, the members of the Board of Directors discussed matters by telephone as required. The agenda for meetings of the Board of Directors is set by the Chairman. Any member of the Board of Directors may request that an item be included on the agenda. The members are provided with documentation prior to each meeting to enable them to prepare for the items to be discussed.

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

Committees

The Board of Directors has formed an Audit Committee, a Nomination & Compensation Committee and a Strategy Committee, and has appointed Chairs for these committees. The committees meet regularly and prepare business for the full Board of Directors, draft related proposals and implement resolutions of the Board of Directors as required. The agenda of each committee's meetings is set by its Chairs. The members of the committees are provided with documentation prior to the meetings to enable them to prepare for the items on the agenda.

Audit Committee
The Audit Committee is composed of three members of the Board of Directors: Paul Häring (Chair), Hans-Peter Schwald and Jürg Oleas. The members of the Audit Committee are experienced in financial and accounting matters. The Audit Committee meets regularly and is convened by the Chair as often as business requires. Usually the meetings are also attended by the CEO, CFO, Vice President of Internal Audit, General Counsel and representatives of the statutory auditor.

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

- Assessing processes in the risk and control environment (internal control system)
- Monitoring financial reporting
- Assessing the internal and external auditors
- Defining and approving the focal points of the audits
- Accepting the audit report and any recommendations of the statutory auditor prior to submission of the annual financial statements (individual and consolidated) to the full Board of Directors for approval
- Submitting a proposal to the full Board of Directors as to which external auditor should be recommended to the AGM for appointment; assessing the performance, fees and independence of the external auditor and examining the compatibility of audit activities with any consultancy mandates.
- Regularly examining the Compliance Management System

The Audit Committee regulates, supervises and commissions the Internal Audit. It provides the full Board of Directors with a regular report on its activities and immediately informs the Board of any important matters.

Nomination & Compensation Committee
The Nomination & Compensation Committee (NCC) is composed of four members of the Board of Directors: Markus Hutter (Chair), Hans-Peter Schwald, Dr. Remo Lütolf and Prof. Sibylle Minder Hochreutener. The NCC meets regularly and is convened by the Chair as often as business requires. The meetings are usually also attended by the CEO and the Chief Human Resource Officer.

The main task of the NCC is to propose the outlines of human resource policies and planning to the full Board of Directors and to present proposals on the selection and compensation of Group Executive Board members. This also includes preparing necessary decisions for the full Board of Directors in the areas of management development, compensation system and policies, objective setting, pension fund matters and social partnership.

Finally, the NCC is tasked with proposing the compensation of members of the Board of Directors in conformity with the guidelines set forth by the Swiss Confederation.

Strategy Committee
The Strategy Committee comprises three members of the Board of Directors: Jürg Oleas (Chair) and Hans-Peter Schwald, plus Egon W. Behle, who was a member of this committee until 27 April 2017. A successor to Egon W. Behle is being sought. The Strategy Committee has four scheduled meetings a year, which are coordinated with the strategic and budgetary planning process.

The Strategy Committee assists the Board of Directors with its strategic duties. In particular, these include preparing for the Board's Strategy Workshop and clarifying important issues with the owner (e.g. owner's strategy of the Swiss Federal Council). The Strategy Committee prepares resolutions of the full Board of Directors relating to RUAG's strategy, its budget and multi-year plan. The meetings are usually also attended by the CEO and CFO and by the Vice President Strategy & Corporate Development.

Advisory Board
The Advisory Board helps the Board of Directors and Group Executive Board to better deliberate on, prepare, implement and communicate their decisions. The Advisory Board has no executive or supervisory functions, and is not an official organ of the company. The Advisory Board held two meetings in 2017. One of its members, Philip W. Erzinger, resigned after the first meeting. Thus at present the Board only has two members: Prof. Thomas Friedli and Prof. Alexandre J. Vautravers. A successor to Philip W. Erzinger is currently being sought.

Even though RUAG complies strictly with the law, its activities are subject to close scrutiny and in some cases are rejected, depending on political or social orientation. Moreover, it is inherent in the Group's highly international activities that it is obliged to take account of and evaluate diverse political, cultural and economic views. The Advisory Board regularly assesses reputational, economic and compliance risks – and with regard to the latter especially the risk of corruption – in those countries in which RUAG operates or wishes to operate. In this way it helps to ensure that the top management bodies of RUAG can better judge the social situation and the international challenges as well as the consequences of pending decisions.

Information and control instruments
The RUAG Management Information System (MIS) is structured as follows: The separate financial statements (balance sheet, income statement and statement of cash flows) of the individual subsidiaries/divisions are compiled on a monthly, quarterly, semi-annual and annual basis. These figures are consolidated for each division and for the Group as a whole and presented in comparison with the budget. The budget, which represents the first year of a rolling three-year plan, is examined in the form of a feasibility forecast based on monthly results. The CEO submits a written monthly report on budget compliance to the Board of Directors.

Compliance Board
The Compliance Board enforces the prohibition on corruption and is responsible for operating the whistleblower system (see below). It implements the Export Compliance policy for defence applications and enforces the ban on illicit price-fixing and market manipulation (antitrust and competition law) and the prohibition of money laundering. According to its charter, the Compliance Board is composed of the General Counsel (Chair), the Vice President Compliance & Risk Management, the Vice President Owner Relations, the Vice President Legal and one representative from each division. The Compliance Board meets at least twice a year. Statements and day-to-day business decisions are the responsibility of a committee composed of the General Counsel (Chair) and the Vice President for Risk Management.

The Vice President Compliance & Risk Management commenced work at the beginning of 2017. He is implementing the "Integrity@RUAG" Group project – commissioned by the Board of Directors and extending over a number of years – for the integrated expansion and strengthening of the compliance and risk management system. He sits on the Compliance Board as Vice President Compliance & Risk Management. As part of this project, the Compliance Board is also being scrutinized with regard to its composition, responsibilities and decision-making powers (especially to distinguish it from the newly created Compliance organization) and with regard to the frequency of meetings, etc., and is being given a new direction.

Whistleblower system
RUAG has an independent reporting office, which offers employees and third parties a way to report any abuses occurring at RUAG – anonymously if desired. The reporting tool, run by an external Swiss company, is intended to function as an early warning system and to help prevent, detect and remedy any irregularities. Incoming reports are seen and processed only by designated Compliance & Risk Management specialists.

Code of Conduct for Business Partners
The Code of Conduct for Business Partners has been integrated into RUAG's General Terms and Conditions. Ever since it was founded, RUAG has been committed to conducting business in accordance with ethical principles and applicable law and in a socially responsible fashion. RUAG also expects its customers, suppliers and service providers and their supply chains to conduct themselves correctly in every respect.

"Saying no to corruption" directive
By systematically implementing the "Saying no to corruption" directive, which forms part of every RUAG employment contract, RUAG is affirming its commitment to being a fair competitor and refraining from seeking unfair advantage by providing financial or other incentives to third parties. RUAG likewise does not accept financial or other incentives in expectation of or as a reward for granting an unfair advantage. See page 24.

Members of the Group Executive Board as at 31.12.2017

Name[1]	Born	Function	Member since
Urs Breitmeier	1963	CEO, RUAG Group	2006
Philipp M. Berner	1966	Member, RUAG Aviation	2010
Dr. Peter Guggenbach	1962	Member, RUAG Space	2009
Christoph Eisenhardt[2]	1968	Member, RUAG Ammotec	2017
Dr. Alexander Toussaint	1967	Member, RUAG Aerostructures	2015
Andreas Berger[3]	1968	Member (ad interim), RUAG Defence (ad interim)	2017
Urs Kiener	1965	Member, Corporate Finance & Controlling	2002
Dr. Christian Ferber	1965	Member, Corporate Human Resources	2012
Alexander Harte[4]	1961	Member (ad interim), General Counsel (ad interim)	2017

1 https://www.ruag.com/en/about-ruag/organisation/group-executive-board
2 Appointed as new Member of the Group Executive Board as of 1.10.2017 as successor to Cyril Kubelka
3 Appointed as new Member of the Group Executive Board ad interim as of 16.10.2017 as successor to Dr. Markus A. Zoller
4 Appointed as new Member of the Group Executive Board ad interim as of 1.8.2017 as successor to Dr. Patrick Grawehr

Group Executive Board

Management organization

The Board of Directors has appointed a Group Executive Board under the chairmanship of the CEO. Since 1 April 2013, CEO Urs Breitmeier has been responsible for the day-to-day business of the company. Throughout 2017, together with the Group Executive Board, he was responsible for the overall management of the Group and for all matters not delegated to another governing body of the company by law, the Articles of Association or the Regulations Governing Organization and Operations. The powers and duties of the Group Executive Board and CEO are set out in detail in the Organizational Regulations and in the job description of the CEO.

The members of the Group Executive Board report to the CEO.

The Group Executive Board comprises the Chief Executive Officer (CEO), the division heads, the Chief Financial Officer (CFO), the Chief Human Resource Officer (CHRO) and the General Counsel.

CEO

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

At the proposal of the CEO, the Board of Directors decides on the three-year corporate plan, annual budget, individual projects, divisional and consolidated financial statements and Group Executive Board-level human resource issues.

The CEO regularly submits reports to the Board of Directors on business performance, anticipated business matters and risks, as well as changes at the next management level.

The members of the Board of Directors may request and review further information on operations as provided by the law, the Articles of Association and the Regulations Governing Organization and Operations.

The CEO regularly assesses whether the Articles of Association and the regulations and other guidelines issued by the Board of Directors require amendment, and applies for such amendments to be made.

Group Executive Board

The list shown above provides information on the name, year of birth, function and date of joining of each member of the Group Executive Board.

Management contracts

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

RUAG management structure as at 31 December 2017

Board of Directors
Hans-Peter Schwald (Chairman), Dr. Remo Lütolf (Vice-Chairman),
Paul Häring, Markus Hutter, Prof. Sibylle Minder Hochreutener, Jürg Oleas

Advisory Board
Prof. Thomas Friedli
Prof. Alexandre J. Vautravers

Audit Committee
Paul Häring (Chair)
Hans-Peter Schwald
Jürg Oleas

Internal Audit

Nomination & Compensation Committee
Markus Hutter (Chair)
Hans-Peter Schwald
Dr. Remo Lütolf
Prof. Sibylle Minder Hochreutener

Strategy Committee
Jürg Oleas (Chair)
Hans-Peter Schwald

CEO RUAG Group/ Corporate Services Urs Breitmeier	**Space**[2] Dr. Peter Guggenbach	**Aerostructures** Dr. Alexander Toussaint	**Aviation** Philipp M. Berner	**Ammotec**[3] Christoph Eisenhardt	**Defence** Andreas Berger
Corporate Finance & Controlling[1] Urs Kiener	Space Switzerland	Aerostructures Germany	Military Aviation	Law Enforcement/ Armed Forces	Land Systems
Corporate Human Resources Dr. Christian Ferber	Space Sweden	Aerostructures Switzerland	Aviation International	Hunting & Sports/ Industry Application	Network Enabled Operations
Corporate Legal & Secretary General Alexander Harte	Space Austria		Subsystems & Products		Simulation & Training
			Business Aviation		Cyber Security[4]

— Group Executive Board
[1] Including Real Estate/Environment, Risk Management, Procurement
[2] As of 1 January 2018, the Space division is organized and managed in the product groups Electronics, Spacecraft and Launchers.
[3] As of 1 January 2018, the Ammotec division is organized and managed in the business units Defence & Law Enforcement, Hunting & Sports and Industry.
[4] As of 1 January 2018, the Cyber Security business unit was assigned to CEO RUAG Group/Corporate Services.

Compensation, profit-sharing and loans

Compensation report

The following details correspond to the guidelines of SIX Swiss Exchange concerning compensation paid to members of the Board of Directors and Group Executive Board, taking the transparency provisions of the Swiss Code of Obligations (Art. 663b*bis* and Art. 663c) into account. Compensation paid in accordance with these provisions of the Swiss Code of Obligations is listed in the financial statements in Note 34 “Compensation of key management personnel”, with further details provided.

Compensation policy

RUAG’s HR policy includes the principle that employee performance and company success are the main factors that determine compensation. The policy is aimed at implementing simple, clearly structured compensation systems that ensure fair pay and are transparent for employees. RUAG bases its compensation on current levels of remuneration in the applicable market environment and reviews it regularly. Individual compensation is based on job requirements, the employee’s skills and performance, and the company’s financial success. Wherever possible, RUAG applies success- and performance-based compensation systems with an additional success-based variable component. These principles also apply in setting the compensation policy for the Group Executive Board, which is determined by the Board of Directors at the request of the NCC. RUAG also prepares an annual report for submission to the Swiss Federal Department of Defence, Civil Protection and Sport (DDPS), the Swiss Federal Council and the Finance Delegation of the Federal Assembly on compliance with the Federal Council’s executive pay ordinance.

Board of Directors

The members of the Board of Directors receive compensation for their work that is determined annually by the AGM in accordance with the guidelines set forth by the Swiss Confederation. The criteria for determining compensation paid to the Board of Directors is based on the responsibility accorded to its members, the complexity of the task, the specialist and personal demands placed on the individual and the expected average time required to fulfil the task.

Compensation consists of the following:

- Fixed fee
- Other benefits

Each member of the Board of Directors receives a fixed fee as part of his or her basic compensation. Other benefits comprise the payment by RUAG Holding Ltd of contributions to social security funds and reimbursement of expenses and lump-sum allowances for expenses.

No compensation was paid to former Board members.

Further details of compensation paid in the year under review can be found in the financial statements in Note 34 “Compensation of key management personnel”.

Group Executive Board

The composition and amount of compensation are based on the industry and labour market environment and are regularly reviewed. To this end, publicly available information on companies of a similar size from Swiss industry and, where applicable, the results of surveys and external studies are taken into account. The performance-based component of compensation for members of the Group Executive Board depends on the extent to which individual performance objectives are reached, and on the company’s financial success. Compensation consists of the following:

- Fixed basic salary
- Performance-based component
- Employer contributions to pension funds
- Fringe benefits

The fixed basic salary is determined primarily by the task, responsibility, qualifications and experience of the Board members, as well as the market environment. The performance-based component consists of a one-year Short Term Incentive Plan (STI) and a three-year Long Term Incentive Plan (LTI). Targets are determined with reference to the extent to which individual performance objectives are reached, and to the company’s financial success. As part of the objective-setting process, measurable goals are set at the beginning of each year by the Board of Directors and the CEO for the members of the Group Executive Board. At the end of the financial year, the extent to which these objectives have been met is assessed.

Short Term Incentive Plan (STI) The financial success of the Group overall and of the individual divisions is measured based on five financial value drivers:

- Net sales
- Operating result (EBIT)
- Necessary net operating assets (NOA)
- Return on net operating assets (RONOA)
- Free cash flow

The target figures are set for one year and the targets are weighted according to strategic priorities. A lower and an upper threshold are defined for each of the five value drivers. If the lower threshold is not reached for the criterion concerned, the related portion of the performance-based component is omitted. However, exceeding the upper threshold does not lead to a further increase in the amount of the performance-based component. Goal attainment is weighted for the members of the Group Executive Board as follows: 20 % for the personal goals and 80 % for the financial goals. In the case of the divisional CEOs, the financial goals are defined per division. In the case of the CEO and the heads of the service units, the financial goals of the Group apply.

Long Term Incentive Plan (LTI) This remuneration component was introduced in 2013 with the aim of focusing the efforts of RUAG’s top managers on the long-term success of the business (cf. also the Swiss Federal Council’s executive pay ordinance, or “Kaderlohnverordnung”). The LTI is for members of the Group Executive Board only. The target figure used for the LTI is the Group’s cumulative net profit over the next three years (plan period), defined with a minimum value, a target value and a maximum value. Payment is made in April of the year following the plan period. Payments are conditional upon an employment relationship existing between the plan participant and RUAG at the end of the plan period.

The Board of Directors specifies the performance benchmark target for a three-year period each year on adoption of the corporate plan. At the same time it also sets the minimum and maximum values and specifies the individual amount payable to each plan participant if the target figure is achieved. If the minimum value is not achieved, no payment will be made. If the maximum value is exceeded, the maximum amount paid will be that stated in the current remuneration plan regulations, i.e. 150 % (LTI 2015–17) or 120 % (LTI 2016–18 and LTI 2017–19) of the specified amount. Payment will be made after the audited financial statements for the last financial year become available. A third of the LTI target value will be expensed each year depending on how the target value develops, with adjustments being made in the subsequent two years if necessary.

The total amount of the performance-based component is based on the extent to which the STI and LTI plan objectives are met. For the members of the Group Executive Board the performance-based component in 2017 ranged from 24 % (previous year: 23 %) to a maximum of 46 % (previous year: 74 %) of the annual cash remuneration.

Other benefits comprise employers' contributions paid to social security funds and for mandatory and extra-mandatory employee benefits. The same regulations on expenses apply for the members of the Group Executive Board as for all other employees of the Group. Additional regulations also apply to the members of the Group Executive Board and all members of management in Switzerland concerning a lump-sum allowance for representation and other incidental expenses. Both regulations have been approved by the cantonal tax authorities concerned. A company car is provided to each member of the Group Executive Board. No appreciable compensation was paid to former Group Executive Board members. Further details of compensation paid in the year under review can be found in the financial statements in Note 34 "Compensation of key management personnel".

Other compensation
Severance payments: Members of the Board of Directors did not receive any severance payments. A severance payment of CHF 316,500 was paid to one member of the Group Executive Board.

Shares and options: No shares and/or options are allocated to members of the Group Executive Board or Board of Directors.

Additional fees: During the 2017 financial year, the members of the Group Executive Board or Board of Directors received no appreciable fees or other compensation for additional services rendered to RUAG Holding Ltd or any of its subsidiaries.

RUAG and its subsidiaries have not provided any securities, loans, advances or credits to the members of the Group Executive Board or Board of Directors and related parties, nor waived any amounts receivable from them.

Capital structure
The share capital of RUAG Holding Ltd amounts to CHF 340 million, comprising 340,000 fully paid-up registered shares, each with a par value of CHF 1,000. As at 31 December 2017, RUAG Holding Ltd did not have any conditional or authorized capital, nor had it issued participation or dividend right certificates. The registered shares of RUAG Holding Ltd are not listed.

Changes in capital
No changes in capital were decided upon in the last three reporting periods.

Shares, share register
At the AGM of RUAG Holding Ltd, each registered share carries one vote. The voting right may only be exercised provided that the shareholder is recorded in the RUAG Holding Ltd share register as a shareholder with voting rights. The registered shares carry full entitlement to dividends.

In place of shares, the company may issue certificates. It may also elect to issue neither shares nor certificates. In this case, the shareholder is entitled at any time to demand issuance of a statement of shares held.

The Board of Directors keeps a register of shareholders.

Shareholder structure

Shareholder
The Swiss Confederation holds 100 % of shares and thus all voting rights of RUAG Holding Ltd. The Swiss Federal Department of Defence, Civil Protection and Sport (DDPS) exercises the Confederation's shareholder interests.

Owner's strategy of the Swiss Federal Council
In its owner's strategy, the Federal Council lays down strategic objectives for its shareholding in RUAG Holding Ltd, specifically strategic focal points, human resource policy and financial objectives, cooperation and investments and reporting to the Swiss Federal Council.

The 2016–19 owner's strategy of the Swiss Federal Council entered into force on 1 January 2016. It establishes the transparent, binding framework which enables RUAG Holding Ltd and its subsidiaries to fulfil their duties on a commercial basis while taking account of broader interests. The owner's strategy is enshrined in the Articles of Association of RUAG Holding Ltd.

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

Participation rights of shareholders

Voting right
At the AGM of RUAG Holding Ltd, each registered share carries one vote. A shareholder may be represented by another shareholder only by written proxy.

Statutory quorums
The following resolutions are subject to decision by qualified majority in accordance with the Swiss Code of Obligations (Art. 704 CO):

- Amendment of the company's objects
- Introduction of shares with preferential voting rights
- Restriction on the transferability of registered shares
- Authorized or contingent capital increase
- Capital increase funded by equity capital, against contributions in kind or to fund acquisitions in kind and the granting of special privileges
- Restriction or cancellation of subscription rights
- Relocation of the company's registered office
- Dissolution of the company or liquidation

Convening the AGM

The AGM is convened and its agenda set as governed by law and by the Articles of Association.

Change in control and defensive measures

Obligatory offer for sale

The Articles of Association contain no provisions concerning opting-out (Art. 125 paras. 3–4 of the Financial Market Infrastructure Act – FinMIA) or opting-up (Art. 135 para. 1 FinMIA).

Change of control clauses

Any disposal of the capital or voting majority of the Swiss Confederation in RUAG Holding Ltd to third parties requires the approval of the Federal Assembly (by simple federal decree, not subject to referendum, Art. 3 para. 3 of the Federal Act on Federal Armaments Companies). Existing agreements and plans do not contain any change-of-control clauses in favour of the members of the Board of Directors and/or of the Executive Board or other executives of RUAG Holding Ltd.

Pension fund

The VORSORGE RUAG pension fund cover ratio as at 31 December 2017 was 103.3 % (previous year: 101.1 %). The fund's financial situation has thus remained stable despite low interest rates in the financial markets.

Statutory auditor

Duration of mandate of auditor in charge

At the Annual General Meeting of 27 April 2017, KPMG Ltd, Bern was elected as RUAG's statutory auditor for a further year.

Auditor in charge Herbert Bussmann has been responsible for the audit mandate since the AGM of May 2014.

Audit fees and additional expenses

KPMG invoiced the Group CHF 1.1 million (previous year: CHF 1.0 million) during the 2017 financial year for services related to the audit of the financial statements of RUAG Holding Ltd and its subsidiaries and of RUAG's consolidated financial statements.

In addition, KPMG invoiced RUAG CHF 0.1 million (previous year: CHF 0.5 million) during the 2017 financial year for audit-related services, tax advice and due diligence services.

Supervisory and control instruments

The Audit Committee of the Board of Directors assesses the performance, fees and independence of the statutory auditor each year and submits a proposal to the Board of Directors as to which external auditor should be recommended to the AGM for appointment.
On 27 April 2017, the AGM reappointed KPMG as the statutory auditor. The Audit Committee annually reviews the scope of external auditing, the auditing plans and the relevant processes, and discusses the audit results with the external auditor in each case.

Information policy

The Group pursues an open information policy in relation to the public and to the financial markets. The published figures extend beyond the statutory requirements in terms of transparency. Quarterly discussions are held between the shareholder and the Board of Directors.

Fees paid to KPMG

in CHF 1 000	2017	2016
Audit fees	1 068	1 025
Tax advice	92	62
Due diligence services	—	274
All other services	16	117
Total fees	1 176	1 478

Key dates

End of financial year	31.12.2017
Annual press conference	23.03.2018
AGM	26.04.2018

The Annual Report containing the financial statements for the year ended 31 December 2017 is sent to the shareholder together with an invitation to the AGM.

RUAG Holding Ltd, Stauffacherstrasse 65, 3000 Bern 22, Switzerland, info@ruag.com, www.ruag.com, +41 31 376 64 50