QUARTERLY REPORT
AT 31 MARCH 2007
FINMECCANICA

CONTENTS

REPORT ON COMPANY ACTIVITIES AT 31 MARCH 2007 4

1. Results for the first quarter of the year 4

2. Significant events for the period and after the end of the quarter 15

3. Group financial statements 22

I. ACCOUNTING STATEMENTS 22

II. GENERAL INFORMATION 26

III. FORM, CONTENT AND APPLICABLE ACCOUNTING STANDARDS 26

IV. ACCOUNTING STANDARDS ADOPTED 27

V. SIGNIFICANT ISSUES 46

VI. SIGNIFICANT NON-RECURRING EVENTS OR TRANSACTIONS 49

VII. EFFECTS OF CHANGES IN THE ACCOUNTING STANDARDS ADOPTED 50

VIII. SEGEMENT INFORMATION 52

IX. NOTES TO THE QUARTERLY FINANCIAL STATEMENTS AT 31 MARCH 2007 55

X. FINANCIAL RISK MANAGEMENT 86

XI. TRANSACTIONS WITH RELATED PARTIES 90

4. Performance by division 97

- HELICOPTERS 97

- DEFENCE ELECTRONICS 101

- AERONAUTICS 105
- SPACE 109
- DEFENCE SYSTEMS 114
- ENERGY 117
- TRANSPORTATION 119
- OTHER ACTIVITIES 122

5. Outlook 125

Finmeccanica Group

Report on company activities at 31 March 2007

1. Results for the first quarter of the year

Highlights

€ millions	Mar-07	Mar-06	change	Dec-06
New orders	2,430	4,199	-42%	15,725
Order backlog	35,362	34,194		35,810
Revenues	2,740	2,583	6%	12,472
EBIT	101	100	1%	878
Net result	18	383	-95%	1,020
Net capital employed	7,327	6,444		6,188
Inet debt	1,970	1,481		858
FOCF	-1,107	-676	-64%	506
ROI	*14.9%*	*14.4%*	*0.5 p.p.*	*17.7%*
ROE	*12.6%*	*17.2%*	*-4.6 p.p.*	*20.5%*
EVA®	-90	-52	-73%	257
R&D costs	402	379	6%	1,783
Employees (no.)	58,685	56,970		58,059

Before looking at the results for the first quarter of 2007, it should be noted that, during 2006, changes have taken place in the recognition of development costs as a result of changes in the regulatory framework. As a result, beginning with the 2006 annual report, reference is now made to "revenues" rather than to "value of production". For further details on these changes, see the section concerning the "effects of changes in the accounting standards adopted" (Section 7).

Finmeccanica Group's consolidated results for the first quarter of 2007 are not entirely representative of the trend for the financial year as a whole since more than half of the

Group's business is concentrated in the second half of the year. Nonetheless, as at 31 March 2007, revenues increased by 6%, while EBIT was essentially stable even though the first quarter of 2006 benefited from a gain of some €mil. 18 on the sale of a property by the subsidiary Selex Communications Ltd. ROS is essentially in line with that of 31 March 2006, settling at 3.7% for the first quarter of 2007.

New orders for the period totalled €mil. 2,430, as compared with the €mil. 4,199 for the first quarter of 2006, which benefited from a number of non-recurring new orders, primarily in the helicopter division.

Regarding Group profitability indicators compared with the prior year (shown in brackets), return on investment (ROI) was 14.9% (14.4%), return on equity (ROE) stood at 12.6% (17.2% in 2006, which benefited from the non-recurring gains described below).

As regards EVA®[1] (a negative €mil. 90 for the first quarter of 2007, as compared with negative €mil. 52 at March 2006), it should be noted that, as a result of the change in cost of capital for the Group, it is difficult to compare the figures for the two periods concerned. In fact, as a result of the changing macroeconomic landscape, marked by high levels of volatility on the financial markets and increasing interest rates, Finmeccanica has recently taken steps to increase the Group's cost of capital by more than one percent over the rate used until 31 December 2006.

****

The first quarter of 2007 closed with consolidated net income of €mil. 18, as compared with €mil. 383 for the same period of the previous year, which, however, included the following two non-recurring events: the gain realized on the public tender for the 52.17% stake in Ansaldo STS S.p.A. in the amount of roughly €mil. 355 net of the effect of consolidated tax procedures and the aforementioned gain on the sale of a property by Selex Communications Ltd. in the amount of roughly €mil. 18. Excluding these effects, net income at 31 March 2006 would have been €mil. 10; therefore, on like-for-like terms, net income for the first quarter of 2007 is €mil. 8 higher than that of the same period of the previous year.

[1] **EVA® is a registered trademark of Stern Steward & Co.**

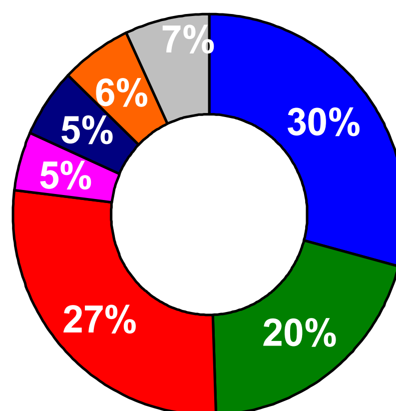
****

New orders for the first quarter of 2007 totalled €mil. 2,430, as compared with the €mil. 4,199 for the same period of the previous year. However, for the purposes of comparison, it is important to note that the first quarter of 2006 benefited from a number of significant non-recurring orders in the helicopter division totalling €mil. 1,190 (i.e. the IMOS contract for logistics support for the entire fleet of EH101's in service with the British Royal Air Force and Navy with a value of €mil. 640 and the MCSP contract to upgrade 30 EH101 Merlin MK1 helicopters in service with the Royal Navy with a value of €mil. 550).

The following are also of note (and are described in greater detail under section 4 of the report on operations): the announcement by the Turkish government of the start of negotiations with AgustaWestland for a helicopter programme (roughly €mil. 1,200) and the finalization by Selex Sistemi Integrati of a new order (more than €mil. 250) related to the extension of the homeland security system in use by the Algerian National Police Force.

Orders

€ millions	Mar-07	Mar-06	change
■ Helicopters	712	1,836	-61%
■ Defence Electronics	502	629	-20%
■ Aeronautics	667	431	55%
■ Space	121	218	-44%
■ Defence Systems	132	89	48%
■ Energy	145	576	-75%
■ Trasportation	170	484	-65%
Eliminations and other ac	-19	-64	
	2,430	4,199	



The main new orders for the first quarter of 2007 included the following:

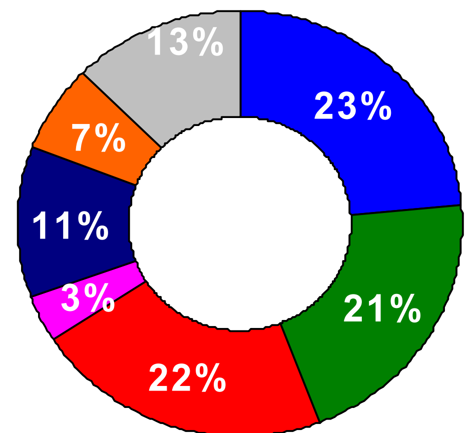
- Helicopters:
    - civil-public sector: orders for 28 AW139 helicopters for a total of €mil. 266;
    - commercial sector: orders for 64 helicopters (30 A109 Grand, 12 A109 Power, and 22 A119) for a total of €mil. 218;
- Defence Electronics:
    - further orders for avionics equipment and communication systems for the EFA;
    - further international orders for countermeasures and air-traffic control systems;
    - the definition of a framework agreement with CNIPA (National Centre for IT in the Government) for security and information technology activities;
- Aeronautics:
    - military segment: the EFA Future Enhancements order to further develop the weapons system in order to enhance the craft's performance and operating capacity;
    - civil sector: orders of the GIE-ATR consortium that received orders for 24 aircraft (of which 11 ordered by Spanish firms, 6 by the Philippine Cebu Air, and 3 by the Indian firm Jet Airways) and the additional lots of the B767, A321 and Falcon programmes; engine nacelles; and transformations of the MD11 aircraft;
- Space:
    - commercial segment: the renewal of the contracts for multi-year, high-value television services, particularly for Sky, and the collection of new orders for the supply of telecommunications satellite services;
    - Earth observation segment: the contract concerning the Cosmo programme for the completion of the fourth satellite;
    - navigation and infomobility segment: additional orders related to the Galileo (the in-orbit validation phase) and EGNOS programmes;
- Defence Systems:
    - orders to upgrade the battery of Aspide air-defence missiles;
    - orders for four 76/62SR cannons and for machine guns to Malaysia;

- Energy:
    - a gas turbine and related alternator for the Algeciras site (lot 2) and the Vlore site, respectively;
    - service segment: important orders in renewable energy related to the refurbishment of four hydroelectric assemblies, two hydroelectric generators, and a hydroelectric plant;
- Transportation:
    - signalling segment: two orders by the mining firm Rio Tinto;
    - systems segment: the order related to Alifana Inferiore to equip 15 Metrocampania Nordest electric trains with technological signalling systems;
    - vehicles segment: service orders.

At 31 March 2007, the **order backlog** stood at €mil. 35,362, as compared with €mil. 35,810 at 31 December 2006. These cover three years of Group production. The slight decrease of €mil. 448 is essentially due to ordinary order acquisition and customer invoicing activities.

Order backlog

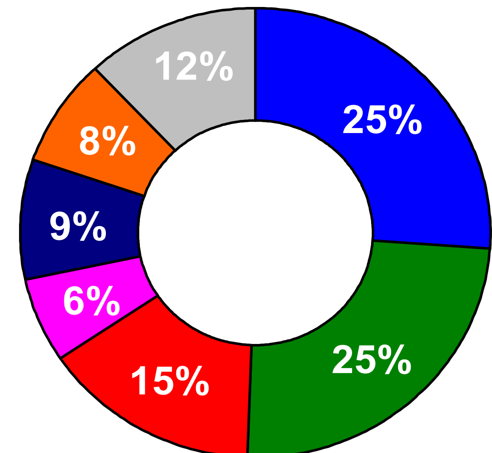
€ millions	Mar-07	Dec-06	change
Helicopters	8,496	8,572	-1%
Defence Electronics	7,418	7,676	-3%
Aeronautics	7,866	7,538	4%
Space	1,251	1,264	-1%
Defence Systems	4,133	4,252	-3%
Energy	2,396	2,468	-3%
Transportation	4,540	4,703	-3%
Eliminations and other activities	-738	-663	
	35,362	35,810	



At 31 March 2007, **revenues** totalled €mil. 2,740 for an increase of €mil. 157, or 6%, over the same period of the previous year. This internal growth confirms the Group's general growth targets.

Revenues

€ millions	Mar-07	Mar-06	change
Helicopters	720	578	25%
Defence Electronics	680	708	-4%
Aeronautics	412	408	1%
Space	166	140	19%
Defence Systems	238	214	11%
Energy	218	201	8%
Trasportation	330	340	-3%
Eliminations and other activities	-24	-6	
	2,740	2,583	



The increase in revenues was primarily due to the sharp increase for the helicopter division as a result of high production volumes in the commercial segment (A109s, AW139s, and A119s) for the beginning of full operations for the helicopter for the President of the United States of America and for product support activities.

The following sectors also contributed to this growth:

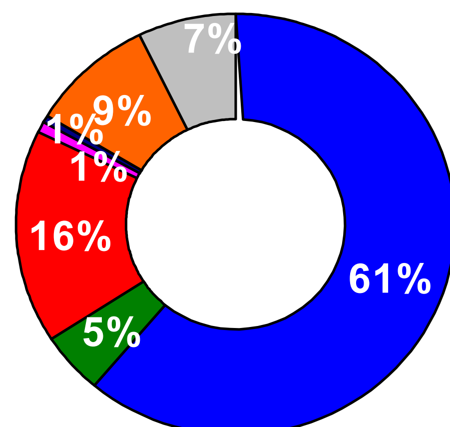
- Space, for production increases in the manufacturing segment;
- Defence Systems, for the production of Storm Shadow air-to-surface missile systems and SCALP EG and for customer support activities, as well as for production related to the PZH2000 for the Italian army and to Hitfist land-based turrets;
- Energy, for the execution of the Algeciras and Amman East orders.

Production volumes in the other segments were essentially in line with the performance of the first quarter of 2006.

EBIT for the first quarter of 2007 came to €mil. 101 and was essentially in line with that of the same period of the previous year, which benefited from the €mil. 18 gain on the sale of a property by the subsidiary Selex Communications Ltd.

EBIT

€ millions	Mar-07	Mar-06	change
■ Helicopters	75	44	70%
■ Defence Electronics	6	42	-86%
■ Aeronautics	20	15	33%
■ Space	1	9	-89%
■ Defence Systems	1	7	-86%
■ Energy	11	7	57%
■ Trasportation	9	16	-44%
Other activities	-22	-40	
	101	100	



Contributing to this level of EBIT was the solid performance of the Helicopter division, both in absolute terms and in terms of percentage growth, as a result of the aforementioned increase in production and the consolidation of efficiency gains related to the integration of the Italian and British businesses. The following segments posted positive performance:

- Aeronautics, for improvements by Alenia Aeronautica S.p.A., which offset the worsening of Alenia Aeronavali S.p.A. In that regard, it should be noted that, at the end of 2006, Alenia Aeronavali S.p.A. launched a plan for reorganization and efficiency improvements;
- Energy, for the aforementioned increase in production volumes related primarily to systems.

Conversely, the following segments posted declines in EBIT:

- Defence Electronics, due both to a contingent situation with a mix of less profitable activities than in the past in command and control systems and information technology and to lower volumes. It should also be noted that the

figures for the first quarter of 2006 benefited from the aforementioned gain on the sale of a property (€mil. 18);

- Space, due to an increase in costs on a number of programmes in France, as well as to an increase in the number of employees over the same period of the previous year;
- Defence Systems, due to an increase in costs associated with the reorganization of the missile segment;
- Transportation, due primarily to difficulties in the Vehicles segment, where losses were affected by the revision of estimates for a number of orders at the end of the previous year.

****

Group **net debt** (payables higher than financial receivables and cash and cash equivalents) at 31 March 2007 was €mil. 1,970 (€mil. 858 at 31 December 2006), a net increase of €mil. 1,112.

This debt level of 39% of consolidated shareholders' equity is lower than the amount achievable on a careful and prudent financial management and falls within the maximum limits set by the main rating companies.

Free Operating Cash Flow (FOCF) at 31 March 2007 was negative (use of cash) in the amount of €mil. 1,107 compared with a negative €mil. 676 at 31 March 2006. In analysing this FOCF, seasonal factors have to be taken into account. The balance between trade collections and payments reveals that payments are particularly higher than collections. The worsening of €mil. 431 was essentially affected by the increase in production volumes and, in the amount of roughly €mil. 140, by greater investments over the same period of the previous year related primarily to aeronautics programmes.

Consolidated net invested capital at 31 March 2007 came to €mil. 7,327, compared with the €mil. 6,188 of 31 December 2006. This increase of €mil. 1,139 was due to the €mil.

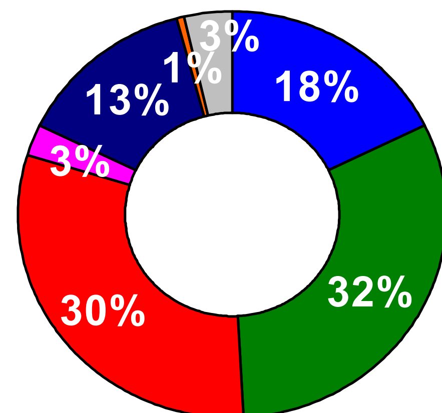
900 increase in working capital (€mil. 466 at 31 March 2007 compared to a negative €mil. 434 at 31 December 2006) due primarily to the aforementioned trend in FOCF and the increase in capital assets due to investments in non-current assets net of depreciation and amortization.

****

For the first quarter of 2007, **research and development** costs totalled €mil. 402, compared with the €mil. 379 of the first quarter of 2006, for an increase of 6% and representing approximately 15% of value of production.

R&D Costs

€ millions	Mar-07	Mar-06	change
■ Helicopters	71	97	-27%
■ Defence Electronics	127	117	9%
■ Aeronautics	122	103	18%
■ Space	11	9	22%
■ Defence Systems	54	40	35%
■ Energy	3	3	0%
■ Trasportation	14	10	40%
	402	379	



The main R&D activities regarded:

- Helicopters:
  - within the scope of the programmes funded by Italian law 808/85: the development of technologies, mainly for military purposes, for a new helicopter of the 6-7 ton class named the A149 and development of multi-role versions of the BA609 convertiplane for national security purposes;

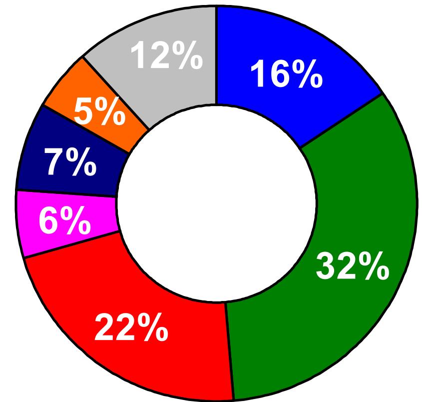
- Defence Electronics:
  - the continuation of development of the EFA programme;

    - the fine-tuning of the UAV FALCO prototypes;
    - the development of naval and land-based command and control systems;
    - the completion of development of air-traffic control radar systems;
    - the completion of the TETRA network;
- Aeronautics:
    - the development of civil programmes, including the B787;
    - in the military segment, the C27J, the EFA, and the M346 trainer;
    - activities related to the second lot, Tornado, AMX, JSF, Unmanned Air Vehicles (UAVs), A380, engine nacelles, and B767 Cargo;
- Space:
    - the study and development phases of the Syracuse 3 and Sicral 1B (SAR radar, altimeter, and radiometer) programmes, dual-use systems for security and civil protection (Cosmo);
    - the development of platforms and solutions for the provision of navigation and infomobility services, Galileo, GIS (Geodatabase), and LEO applications;
- Defence Systems:
    - the continuation of development related to: the Meteor air-to-air missile in the missile segment; the guided multiple launch rocket system as part of land and naval weapons; and the Black Shark heavy torpedo in the underwater system segment;
- Energy:
    - the continuation of the technological autonomy plan in the steam and gas turbine field;
- Transportation:
    - in the Signalling segment, the projects intended primarily for alignment to new requirements both in the rail and mass transit segments.

The **number of employees** at 31 March 2007 stood at 58,685 people, an increase of 626 from the 58,059 of 31 December 2006. This increase is primarily attributable to net new

hires, particularly in the Aeronautics, Helicopter, and Transportation divisions, as well as to changes in consolidated companies.

Employees (number)			
€ millions	Mar-07	Dec-06	change
■ Helicopters	8,999	8,899	1%
■ Defence Electronics	19,074	19,185	-1%
■ Aeronautics	12,687	12,135	5%
■ Space	3,252	3,221	1%
■ Defence Systems	4,213	4,275	-1%
■ Energy	2,864	2,856	0%
■ Trasportation	6,784	6,677	2%
Other activities	812	811	
	58,685	58,059	



2. Significant events for the period and after the end of the quarter

Industrial transactions

Within the ***Helicopters*** division, on 7 February 2007, AgustaWestland and Boeing signed a memorandum of understanding for the joint production of the next generation of Chinook transport helicopters for the Italian army and other future vertical take-off and landing (VTOL) craft both for the domestic market and for international opportunities.

In the ***Defence Electronics*** segment, activities were completed that have led to Finmeccanica holding the entirety of the share capital of **Datamat S.p.A.**, an Italian company which develops and builds avionics and naval mission systems, and integrated solutions in the defence, space, government, healthcare, banking, finance and telecommunications sectors.
Specifically, upon completion of the remaining purchase and consequent delisting of the company in the first part of 2007 and having reached the equity interest threshold of 98%, on 17 April 2007, Finmeccanica exercised its right to purchase the remaining Datamat shares in accordance with Article 111 of the Italian consolidated finance act (the so-called *squeeze-out* clause) at a price of €10.040 per share as established by an expert appointed by the Rome court, thereby becoming the sole shareholder in Datamat.

On 14 February 2007, **Selex Sistemi Integrati S.p.A.** and the Indian firm Bharat Heavy Electricals Ltd. (BHEL) signed a memorandum of understanding for a partnership in the field of radar and other industry technologies. The two firms will be studying trade opportunities and all other business aspects for the development and production of technologically advanced devices.

On 30 March 2007, Finmeccanica completed the acquisition of the remaining 25% stake from BAE Systems in the company **Selex Sensors and Airborne Systems S.p.A.** (Selex S&AS S.p.A.) for a total outlay of roughly €mil. 400. In the coming months, an additional payment currently estimated at €mil. 12 will be added to this amount. The

total price also includes the portion of undistributed earnings payable by Selex S&AS S.p.A. to BAE Systems for the entire period in which it held an interest in the company.

On 22 March 2007, **Finmeccanica** signed a memorandum of understanding with the Libyan government for the potential creation of a joint venture in the field of Security and Defence Electronics in order to create innovative solutions for the Libyan market and for the markets of other African nations. The goal is to use Finmeccanica's know-how together with local industry to develop integrated systems to monitor critical infrastructures, as well as communications and homeland security systems and integrated postal automation systems.

In the area of Security, on 14 March 2007, a decree of the Italian Ministry for the Economy and Finance was published in issue 61 of the Italian *Gazzetta Ufficiale*. This decree established the price of the **electronic ID card** and launched a national project aimed at creating a tool that will enable individuals to be recognized with certainty so as to certify one's identity and to be able to take advantage of value-added services. Through its subsidiary Selex Service Management S.p.A. and together with Istituto Poligrafico e Zecca dello Stato S.p.A. (79%) and Poste Italiane S.p.A. (15%), Finmeccanica has a 15% interest in the consortium Innovazione e Progetti, which will be responsible for developing the initiative, acting as a point of contact for business and technology, particularly as regards security-related aspects.

In ***Aeronautics*** on 5 April 2007, Alenia Aeronautica and TsAGI, the Russian central aero-hydrodynamics institute, signed a partnership agreement for the research, development, and design of aerostructures for civil craft, as well as for joint projects in the field of advanced aerodynamics and other design activities for next-generation aircraft.

On 20 February 2007, an inter-governmental agreement was signed by the Italian Ministry for Economic Development and the Russian Federation's Ministry of Industry and Energy concerning the trade agreements in effect between **Finmeccanica** and **Sukhoi Aviation Holding** and their respective subsidiaries, Alenia Aeronautica S.p.A.

and Sukhoi Civil Aircraft Company (SCAC), concerning programmes for the manufacture, distribution, and post-sale services for the “SuperJet 100” family of 75-100 seat regional jets.

In the ***Space*** segment, on 6 April 2007, following authorization by the European Commission, Thales replaced Alcatel-Lucent in the joint ventures Alcatel Alenia Space – which was then renamed Thales Alenia Space (67% Thales and 33% Finmeccanica) – and Telespazio (67% Finmeccanica and 33% Thales). This change, which completes the second phase of the partnership agreement between Thales and Alcatel-Lucent announced on 5 April 2006, opens the door for the creation of the new space alliance between Finmeccanica and Thales.

On 18 October 2006, as part of the broader efforts to develop the company’s civil businesses, **Finmeccanica** signed a memorandum of understanding with the **Russian railway** in order to begin a partnership concerning the manufacture, distribution, and technical support services for rolling stock and rail transport infrastructures.
In that regard, on 9 February 2007, the **Russian railway**, the **Ferrovie dello Stato group**, and **Finmeccanica** signed a memorandum of understanding aimed at developing commercial partnerships for international projects of mutual interest, particularly in the field of high-speed trains, which could also include the Moscow-St. Petersburg line. The first act of this partnership will involve Saudi Arabia with the Jedda-Mecca-Medina high-speed line with an estimated value of some USDbil. 6.
In March, during the latest Italy-Russia summit held in Bari, Finmeccanica also signed a new industrial cooperation agreement with the Russian railway, which defines the timing and procedures for implementing high-priority projects, such as: the development of a new regional train; the application of technology and capacity already available to Selex Sistemi Integrati S.p.A. in order to create safety and security systems; the development by Telespazio S.p.A. of a satellite observation system to monitor landslides near the Tuapse-Adler railway line.

On 5 February 2007, two conventions were also signed by **AnsaldoBreda S.p.A.**, the Province of Pistoia, the University of Florence, and Istituto Fedi aimed at created a

laboratory located in Pistoia for dynamic mechatronics simulations and applied research and innovation in the rail transport industry.

On 18 April 2007, Coinfra S.p.A., a member of the Tili group, also signed a preliminary purchase agreement for an 85% stake in **Ansaldo Trasmissione e Distribuzione S.p.A.**, whose capital is currently held by Fondo Athena (35.5%), Ezine S.A. (34.5%), and Sogepa S.p.A., a member of the Finmeccanica Group (30%). The agreement currently calls for Sogepa to maintain a 15% interest.

Financial transactions

In the first quarter of 2007, Finmeccanica carried out no transaction on the capital markets. As a result, there was no substantial change in the structure of medium to long-term debt, particularly with regard to bonds, which stood at around €mil. 1,734 (under IAS/IFRS). The average term of maturity is approximately 9 years.

On 16 January 2007, the bond issued in 1997 by the Luxembourg subsidiary Finmeccanica Finance S.A. on the Japanese market came to maturity and was redeemed in its entirety for an amount of roughly €mil. 6.

Below is a list of bonds outstanding at 31 March 2007, including the transactions placed on the market by Finmeccanica Finance S.A.:

Issuer		**Year of issue**	**Maturity**	**Amount (€mil)**	**Annual coupon**	**Type of offer**	**IAS recog. amts €mil. (5)**
Finmeccanica Finance S.A.	(1)	2002	30-Dec-08	297	Variable	Italian retail	297
Finmeccanica Finance S.A.	(2)	2003	8-Aug-10	501	0.375%	European institutional	437
Finmeccanica Finance S.A.	(3)	2003	12-Dec-18	500	5.75%	European institutional	504
Finmeccanica S.p.A.	(4)	2005	24-Mar-25	500	4.875%	European institutional	496

(1) Bonds exclusively offered to the public in Italy and listed on the TLX market, which is managed by Trading Lab Banca S.p.A. - Unicredito Italiano Group. Issued as part of the Euro Medium Term Notes (EMTN) programmes for a maximum €bil. 2, the bonds are governed by a specific Italian regulation. Transaction authorised pursuant to Article 129 of Legislative Decree no. 385/93. Prospectus filed with CONSOB on 4 December 2002 (authorisation notified with note no. 2079342/3.12.02)

(2) Exchangeable bonds with a maximum number of 20,000,000 shares in STMicroelectronics N.V. (STM) at a conversion price of €25.07 per share. Starting from the third anniversary of the issue, Finmeccanica Finance can ask for the loan to be converted if the average price recorded during the 30 working days prior to the date of notice to bond-holders exceeds 125% of the conversion price. At the maturity date Finmeccanica Finance can repay in cash or, upon prior notice to be given with at least 15 working days, through a combination of STM shares valued at the average prices recorded in the prior 5 working days. Transaction authorised pursuant to Article 129 of Legislative Decree no. 385/93. Bonds are listed on the Luxembourg Stock Exchange.

(3) Bonds issued as part of the EMTN programmes for a maximum of €bil. 2 The entire issue was converted from a fixed-rate issue to a floating-rate one for the first two years of the loan. The transaction was authorised pursuant to Article 129 of Legislative Decree no. 385/93. Bonds listed on the Luxembourg Stock Exchange.

Rate transactions were made on these bonds and led to benefit throughout 2005 from low floating rates with an effective cost of some 3.25%. During 2006, the effective cost of the loan returned to a fixed rate equal to an average value of some 5.92%.

(4) Bonds issued as part of the EMTN programmes for a maximum of €bil. 2 The transaction was authorised pursuant to Article 129 of Legislative Decree no. 385/93. Bonds listed on the Luxembourg Stock Exchange. Some rate transactions were made to optimise collection costs.

(5) The difference between the face value of bonds and book value is due to interest rates being classified as to increase debt and to discounts being recognised to decrease debt. Furthermore, as regards the issue of exchangeable bonds in (2) above, IAS 39 provides for the separation of the financial debt component and the call option sold. The debt component is measured by applying the market interest rate at the issue date in place of the nominal interest rate, while the option component, excluded from the financial position, is subject to periodic measurement at fair value. At 31 March 2007, this valuation method led to posting a debt €mil. 64 less than the face value of the bond. This differential will gradually come down as the maturity date draws near.

All the bond issues of Finmeccanica Finance S.A. are irrevocably and unconditionally secured by Finmeccanica S.p.A.

All the bonds above are governed by regulations with standard legal clauses for this type of company transactions. In the case of the Finmeccanica issues, these clauses do not

require any commitment for specific financial parameters (financial covenants) but require negative pledge and cross default clauses.

Based on negative pledge clauses, issuers Finmeccanica Finance S.A., Finmeccanica S.p.A. and their Material Subsidiaries (companies whose issuer or guarantor owns more than 50% of share capital or represent at least 10% of total revenues) are expressly and specifically prohibited from creating guarantees to secure financial transactions to the partial benefit of one or more creditors, without prejudice to the generalities of the foregoing. Exceptions to this prohibition are securitisation and, starting from July 2006, the creation of assets for the use indicated in Article 2447 bis *et seq*. of the Italian Civil Code.

The cross-default clauses give the bondholders the right to request early redemption of the loan (i.e. default) in the event that, for any loan or, more generally, any financial obligation of the Group, there should be a failure to make payment beyond preset limits or other default event.

All Finmeccanica S.p.A. and Finmeccanica Finance S.A. bonds were given a medium-term financial credit rating by the three international rating agencies: Moody's Investors Service, Fitch and Standard and Poor's. More specifically, at the reporting date these credit ratings were A3 (Moody’s) and BBB (Fitch and Standard and Poor’s), both with stable outlook. During 2005, Moody’s credit rating improved from Baa2 to A3, in part due to a review of the agency’s methods.

As part of the centralisation of its financial operations, Finmeccanica S.p.A. has cash loans and endorsement loans facilities sufficient to meet the Group needs. Specifically, it holds a medium-term revolving credit line of €mil. 1,200 agreed in 2004 with a pool of national and foreign banks, whose interest rates and maturity (current maturity 2012) were renegotiated in 2005, thanks in part to the improved credit rating as mentioned above. This transaction is also governed by negative pledge clauses, which have been illustrated above. At 31 March 2007, this credit line was not used. Finmeccanica also has additional short-term credit lines, for cash loans, amounting to around €mil. 1,200, of which €mil. 900 is unconfirmed and around €mil. 300 is confirmed; at 31 March 2007,

these credit lines were also unused. There are also unconfirmed endorsement loan lines of around €mil. 2,000.

3. Group financial statements

I. ACCOUNTING STATEMENTS

Income Statement

(€mil.)	For the three months ended 31 March 2007	For the three months ended 31 March 2006	For the twelve months ended 31 December 2006
Revenue	2,575	2,426	11,179
Revenues from related parties	165	157	1,293
Other operating revenue	78	83	487
Other operating revenue from related parties			7
Costs for goods	(1,076)	(942)	(4,788)
Costs for services	(774)	(774)	(3,543)
Costs (net of recoveries) from related parties	(11)	(16)	(118)
Personnel costs	(898)	(848)	(3,391)
Depreciation, amortisation and impairment	(109)	(88)	(505)
Other operating costs	(77)	(74)	(433)
Changes in inventories of work in progress, semi-finished and finished goods	14	165	(24)
(-) Capitalisation of internal construction costs	214	11	714
	101	**100**	**878**
Financial income	109	470	1,191
Financial income from related parties	1	-	3
Financial expense	(127)	(125)	(779)
Financial expense from related parties	(4)	(3)	(16)
Effect of accounting for equity investments with equity method	1	(4)	(5)
Profit before taxes and the effect of discontinued operations	**81**	**438**	**1,272**
Income taxes	(63)	(55)	(243)
(Loss) profit associated with discontinued operations	-	-	(9)
Net profit	**18**	**383**	**1,020**
. Group	*12*	*379*	*988*
. Minority interests	*6*	*4*	*32*
Earnings per share			
Basic	*0.028*	*0.896*	*2.333*
Diluted	*0.028*	*0.891*	*2.323*
Earnings per share net of discontinued operations			
Basic	*0.028*	*0.896*	*2.353*
Diluted	*0.028*	*0.891*	*2.344*

Balance Sheet

€mil.	*31 March 2007*	*31 December 2006*	*31 March 2006*
Non-current assets			
Intangible assets	5,430	5,317	3,689
Property, plant and equipment	2,774	2,660	2,512
Investment properties	1	2	3
Equity investments	141	140	132
Financial assets at fair value	862	857	914
Non-current receivables from related parties	18	16	12
Receivables	430	426	121
Deferred tax assets	447	470	395
Other assets	6	9	7
	10,109	9,897	7,785
Current assets			
Inventories	3,237	3,095	5,765
Contract work in progress	3,233	2,823	2,732
Receivables from related parties	440	438	387
Trade receivables	3,398	3,479	3,214
Financial assets at fair value	19	21	21
Tax receivables	500	469	358
Financial receivables	386	452	302
Other assets	576	594	463
Cash and cash equivalents	472	2,003	686
	12,261	13,374	13,929
Non-current assets held for sale	119	110	136
Total assets	22,489	23,381	21,849
Shareholders' equity			
Share capital	1,860	1,858	1,863
Other reserves	3,444	3,418	3,005
Group shareholders' equity	5,304	5,276	4,868
Shareholders' equity of minority interests	85	81	137
Total shareholders' equity	5,389	5,357	5,005
Non-current liabilities			
Borrowings	1,969	1,979	1,983
Severance pay and other employee liabilities	1,231	1,238	1,134
Provisions for risks and charges	355	365	434
Deferred tax assets	342	340	111
Other liabilities	1,320	1,332	365
	5,217	5,254	4,027
Current liabilities			
Advances from customers	5,546	5,529	4,425
Trade payables to related parties	470	594	366
Trade payables	3,145	3,486	3,004
Borrowings	508	881	235
Tax payables	301	322	258
Provisions for risks and charges	551	571	541
Other liabilities	1,275	1,304	3,894
	11,796	12,687	12,723
Liabilities directly correlated with assets held for sale	87	83	94
Total liabilities	17,100	18,024	16,844
Total liabilities and shareholders' equity	22,489	23,381	21,849

Cash flow statement

€mil.	For the three months ended 31 March	
	2007	**2006**
Cash flow from operating activities:		
Gross cash flow from operating activities	255	225
Changes in working capital	(839)	(706)
Changes in other operating assets and liabilities, income taxes and financial charges paid	(203)	(114)
Cash flow generate from (used for) operating activities	**(787)**	**(595)**
Cash flow from investing activities:		
Acquisitions of companies, net of cash acquired	(6)	(96)
Payment to BAE Systems for call option	(400)	-
Investments in property, plant and equipment and intangible assets	(322)	(120)
Disposals of property, plant and equipment and intangible assets	3	39
IPO Ansaldo STS	-	398
Other investing activities	43	124
Cash flow generated from (used in) investing activities	**(682)**	**345**
Cash flow from financing activities:		
Capital increase	5	15
Net change in other financial payables	(63)	(138)
Cash flow generate by (used for) financing activities	**(58)**	**(123)**
Net increase (decrease) in cash and cash equivalents	(1,527)	(373)
Translation differences	(4)	(2)
Cash and cash equivalents at 1 January	2,003	1,061
Cash and cash equivalents at 31 March 2007	**472**	**686**

Statement of change in shareholders' equity

€mil.	Share capital	Retained earnings and consolidation reserve	Other reserves	Group shareholders' equity	Minority interests	Total shareholders' equity
Shareholders' equity at 31 December 2005	1,858	2,173	413	4,444	154	4,598
Change in the fair value of assets available for sale			8	8		8
Change in the fair value of cash-flow hedge instruments and transfers to the income statement			26	26		26
Repurchase of treasury shares						
Allocations for stock grant plans			4	4		4
Translation differences			(22)	(22)	(3)	(25)
Dividends					(8)	(8)
Share capital increase	5	10		15	1	16
Change in the scope of the consolidation area and other minor changes			14	14	(11)	3
Net profit at 31 March 2006		379		379	4	383
Shareholders' equity at 31 March 2006	**1,863**	**2,562**	**443**	**4,868**	**137**	**5,005**
Shareholders' equity at 31 December 2006	1,858	2,933	485	5,276	81	5,357
Change in the fair value of assets available for sale			22	22		22
Change in the fair value of cash-flow hedge instruments and transfers to the income statement			4	4		4
Allocations for stock grant plans			6	6	1	7
Repurchase of treasury shares						
Translation differences			(21)	(21)	(1)	(22)
Dividends						
Share capital increase	2	3		5		5
Change in the scope of the consolidation area and other minor changes					(2)	(2)
Net profit at 31 March 2007		12		12	6	18
Shareholders' equity at 31 March 2007	**1,860**	**2,948**	**496**	**5,304**	**85**	**5,389**

II. GENERAL INFORMATION

The Finmeccanica Group is a major Italian high technology organisation. Finmeccanica S.p.A., the holding company responsible for guiding and controlling industrial and strategic operations, coordinates its subsidiaries (the Finmeccanica Group or, simply, the Group), which are especially concentrated in the fields of aeronautics and helicopters, space, defence, energy and transportation.
Finmeccanica is a company limited by shares based in Rome (Italy), at Piazza Monte Grappa 4, and is listed on the Milan stock market (S&P/MIB).

III. FORM, CONTENT AND APPLICABLE ACCOUNTING STANDARDS

In application of Regulation (EC) No. 1606/2002 of 9 July 2002, the consolidated quarterly report of the Finmeccanica Group at 31 March 2007 was prepared in accordance with the international accounting standards (IFRSs) endorsed by the European Commission, supplemented by the relevant interpretations (Standing Interpretations Committee - SIC and International Financial Reporting Interpretations Committee - IFRIC) issued by the International Accounting Standard Board (IASB).
The general principle used in preparing these consolidated financial statements is the cost method, except for the recognition of derivative instruments and some financial assets, which must or – to the extent of financial assets – can be recognised at fair value under IAS 39.

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

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

Preparation of the consolidated quarterly report required management to make certain estimates. The main areas affected by estimates or assumptions of particular importance or that have significant effects on the balances shown are described in Note 5.
The consolidated quarterly report at 31 March 2007, which was prepared in accordance with IFRS, was not audited.

IV. ACCOUNTING STANDARDS ADOPTED

IV.1 Standards and consolidation area

This quarterly report at 31 March 2007 includes the statements of the companies/entities included in the scope of consolidation ('consolidated entities'), which have been prepared in accordance with the IFRSs adopted by the Finmeccanica Group.

Subsidiaries and entities controlled jointly

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

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

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

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

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

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

The consolidated entities all close their financial years on 31 December. The quarterly report at 31 March 2007 was prepared based on the ending balances at 31 March.

Other equity investments

Investments in entities over which significant influence is exercised, which generally corresponds to a holding of between 20% and 50%, are accounted for either using the

equity method or at fair value. In the case of the equity method, the value of the investment is in line with shareholders' equity adjusted, when necessary, to reflect the application of IFRSs, and includes the recognition of goodwill (net of impairments) calculated at the time of purchase, and to account for the adjustments required by the standards governing the preparation of consolidated financial statements. Unrealised gains on transactions between the Group and its associates are eliminated to the extent of the Group's interest in the associates. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred.

Any value losses in excess of book value are recorded in the provision for risks on equity investments if there is an obligation to cover these losses.

The fair value of equity investments, in the event this method applies, is calculated based on the bid price of the last trading day of the month for which the consolidated IFRS report was prepared (in this case 30 March 2007).

IV.2 Segment information

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

IV.3 Currency translation

Identification of the functional currency

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

Translation of transactions denominated in a foreign currency

Items expressed in a currency other than the functional currency, whether monetary (cash and cash equivalents, receivables or payables due in pre-set or measurable amounts, etc.) or non-monetary (advances to suppliers of goods and services, goodwill,

intangible assets, etc.), are initially recognised at the exchange rate prevailing at the date on which the transaction takes place. Subsequently, the monetary items are translated into the functional currency based on the exchange rate at the reporting date, and any differences resulting from this conversion are recognised in the income statement. Non-monetary items continue to be carried at the exchange rate on the date of the transaction, except in situations where there is a persistent unfavourable trend in the exchange rate concerned. If this is the case, exchange differences are recognised in the income statement.

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

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

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

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

IV.4 Intangible assets

Intangible assets are non-monetary items without physical form, but which can be clearly identified and generate future economic benefits for the company. They are

carried at purchase and/or production cost, including directly related expenses allocated to them when preparing the asset for operations and net of accumulated amortisation (with the exception of intangibles with an indefinite useful life) and any permanent impairments of value. Amortisation begins when the asset is available for use and is recognised systematically over its remaining useful life. In the period in which the intangible asset is recognised for the first time, the amortisation rate applied takes into account the period of actual use of the asset.

Development costs

This account includes costs related to the application of the results of research or other knowledge in a plan or a project for the production of materials, devices, processes, systems or services that are new or significantly advanced, prior to the start of commercial production or use, for which the generation of future economic benefits can be demonstrated. These costs are amortised over the entire period in which the future earnings are expected to be realised for the project itself. If such costs fall within the scope of costs defined by Group standards as 'non-recurring costs', they are recognised in a special item within intangible assets (Section 5.1).
Research costs, on the other hand, are expensed in the period in which they are incurred.

Industrial patent and intellectual property rights

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

Concessions, licences and trademarks

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

can be capitalised after receiving title to the rights themselves and are amortised systematically over the shorter of the period of expected use and that of ownership of the rights.

Goodwill

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

Goodwill related to the acquisition of consolidated companies is recognised under intangible assets. Goodwill related to unconsolidated associated companies or subsidiaries is included in the value of investments.

IV.5 Property, plant and equipment

Property, plant and equipment is measured at purchase or production cost net of accumulated depreciation and any impairment losses. The cost includes all direct costs incurred to prepare the assets for use, as well as any charges for dismantlement and disposal that will be incurred to return the site to its original condition.

Charges incurred for routine and/or cyclical maintenance and repairs are expensed in full in the period in which they are incurred. Costs related to the expansion, modernisation or improvement of owned or leased structural assets are only capitalised to the extent that such costs meet the requirements for being classified separately as an asset or part of an asset. Any public capital grants related to property, plant and equipment are recognised as a direct deduction from the asset to which they refer.

The value of an asset is adjusted by systematic depreciation calculated based on the residual useful life of the asset itself. In the period in which the asset is recognised for the first time, the depreciation rate applied takes into account the period of actual use of the asset. The estimated useful lives adopted by the Group for the various asset classes are as follows:

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

In the event the asset to be depreciated is composed of distinct elements with useful lives that are significantly different from those of the other constituent parts, each individual part that makes up the asset is depreciated separately, in application of the component approach to depreciation.

This item also includes equipment intended for specific programmes (tooling), although it is depreciated, as with other non-recurring costs (see Section 5.1), on the basis of units manufactured in relation to those expected to be produced.

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

IV.6 Investment properties

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

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

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

IV.8 Equity investments

The Group classifies its equity investments as follows:

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

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

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

IV.9 Inventories

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

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

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

IV.10 Contract work in progress

Work in progress is recognised on the basis of progress (or percentage of completion), whereby costs, revenues and margins are recognised based on the progress of production. The state of completion is determined on the basis of the ratio between costs incurred at the measurement date and the total expected costs for the programme.
The valuation reflects the best estimate of the schedules prepared at the reporting date. The assumptions upon which the valuations are made are periodically updated. Any impact on profit or loss are recognised in the period in which the updates are made.
In the event the completion of a contract is expected to result in a loss at the gross margin level, the loss is recognised in its entirety in the period in which it becomes reasonably foreseeable.
Contract work in progress is recorded net of any write-downs, as well as pre-payments and advances related to the contract being performed.
This analysis is carried out contract by contract: in the event of positive differences (where the value of work in progress is greater than total pre-payments), the difference is recorded as an asset; negative differences, on the other hand, are recorded as a liability under 'due to customers for contract work'. If it has not been collected at the date of

preparation of the annual or interim accounts, the amount recorded among advance payments will have a directly contra-item in trade receivables.
Contracts with payments in a currency other than the functional currency (the euro for the Group) are measured by converting the portion of payments due, calculated using the percentage-of-completion method, at the exchange rate prevailing at the close of the period in question. However, the Group's policy for exchange-rate risk calls for all contracts in which cash inflows and outflows are significantly exposed to exchange rate fluctuations to be hedged specifically. In such cases, the recognition methods described in Section 5.3 below are applied.

IV.11 Receivables and financial assets

The Group classifies its financial assets into the following categories:

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

Management classifies assets at the time they are first recognised.

Financial assets at fair value through profit or loss

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

Loans and receivables

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

Financial assets held to maturity

These are non-derivative assets with fixed maturities that the Group has the intention and ability to hold to maturity. Those maturing within 12 months are carried as current assets. Should objective evidence of impairment emerge, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in profit or loss – is removed from equity and recognised in the income statement. If the reasons for the write-down should cease to obtain in future periods, the value of the asset is restored up to the amortised cost value it would have if no impairment had been recognised.

Financial assets available for sale

This category encompasses non-derivative financial assets specifically designated as available for sale or are not classified in any of the previous items. They are recognised at fair value, which is calculated with reference to their market price at the annual and/or interim reporting date or using financial valuation techniques and models. Changes in value are recognised in a specific equity item ('Reserve for assets available for sale'). The reserve is taken to the income statement only when the financial asset is effectively sold or, in cases of a loss of value, when it become evident that the impairment in value already recognised in equity is unrecoverable. Classification as current or non-current depends on the intentions of management and the effective marketability of the security

itself. Assets that are expected to be sold within 12 months are carried under current assets.

Should objective evidence of impairment emerge, the value of the asset is reduced to the value obtained by discounting the expected cash flows from the asset; reductions in value previously recognised in equity are reversed to profit or loss. If the reasons for the write-down should cease to obtain, the value of the asset is restored.

IV.12 Derivatives

Derivatives are still regarded as assets held for trading and stated at fair value through profit and loss unless they are deemed eligible for hedge accounting and effective in offsetting the risk in respect of underlying assets, liabilities or commitments undertaken by the Group.
In particular, the Group uses derivatives as part of its hedging strategies to offset the risk of changes in the fair value of assets or liabilities on its balance sheet or the risk associated with contractual commitments (fair value hedges) and the risk of changes in expected cash flows in contractually defined or highly probable operations (cash flow hedges). For details regarding the methodology for recognising hedges of the exchange rate risk on long-term contracts, see Section 5.3.

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

Fair value hedges

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

Cash flow hedges

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

Determining fair value

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

IV.13 Cash and cash equivalents

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

IV.14 Shareholders' equity

Share capital

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

Treasury shares

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

Profits (losses) carried forward

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

Other reserves

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

IV.15 Payables and other liabilities

Payables and other liabilities are initially recognised at fair value net of transaction costs. They are subsequently valued at their amortised cost using the effective interest rate method (see Section 4.22).
Payables and other liabilities are defined as current liabilities unless the Group has the contractual right to settle its debts at least 12 months after the reporting date.

IV.16 Deferred taxes

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

IV.17 Employee benefits

Post-employment benefit plans

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

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

In compliance with IAS 19, the Finmeccanica Group uses the so-called ‘corridor’ approach in recognising actuarial losses and gains relating to defined benefit plans. This method makes it possible to dilute the effects of changes in the valuation parameters

over a number of financial years. Consequently, net actuarial losses and gains at the end of the prior period that exceed the greater of 10% of the present value of the obligation and 10% of the fair value of the benefit plan assets divided by the remaining working life of employees are recognised in each period.

Other long-term benefits and post-employment benefit plans

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

Benefits payable for the termination of employment and incentive plans

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

Equity compensation benefits

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

IV.18 Provisions for risks and charges

Provisions for risks and charges cover certain or probable losses and charges whose timing or amount was uncertain at the reporting date.

The provision is recognised only when a current obligation (legal or constructive) exists as a result of past events and it is probable that an outflow of economic resources will be required to settle the obligation. The amount reflects the best current estimate of the cost of fulfilling the obligation. The interest rate used to determine the present value of the liability reflects current market rates and includes the additional effects relating to the specific risk associated with each liability.

Risks for which the emergence of a liability is merely a possibility are reported in the section in the notes on commitments and risks and no provision is recognised.

IV.19 Leasing

Group entities as lessees in a finance lease

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

Group entities as lessors in a finance lease

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

The unsecured residual value is reviewed periodically for possible impairment.

Operating leases

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

IV.20 Revenue

Revenues generated by an operation are recognised at the fair value of the amount received and receivable, inclusive of volume discounts and reductions.

Revenues also include changes in work in process, the accounting policies for which were described in Section 4.10 above.

Revenues generated from the sale of goods are recognised when the enterprise has transferred to the buyer substantially all of the significant risks and rewards of ownership of the goods, which, in many cases, will coincide with the transfer of title or possession to the buyer; and when the value of the revenues can be reliably determined.

Revenues from services are recognised on a percentage-of-completion method when they can be reliably estimated.

IV.21 Government grants

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

IV.22 Financial income and expense

Interest is recognised on an accruals basis using the effective interest rate method, i.e. the interest rate that results in the financial equivalence of all inflows and outflows (including any premiums, discounts, commissions etc) that make up a given operation.

Financial expense is never capitalised.

IV.23 Dividends

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

IV.24 Emission rights

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

IV.25 Transactions with related parties

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

IV.26 Costs

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

IV.27 Treatment of income taxes applied in the preparation of interim reports and the seasonality of operations

Treatment of income taxes

In the interim financial statements, income taxes are estimated by applying the expected effective tax rate to the interim pre-tax result.

Cash flows relating to operations

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

V. SIGNIFICANT ISSUES

V.1 Non-recurring costs

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

consideration of the especially long life-cycle of the products being developed.

V.2 Financing for GIE ATR aircraft

In order to enhance its competitive position, in certain cases GIE ATR facilitates access to financing by its customers by providing specific guarantees to third parties (an approach taken by its direct competitors), an activity that in the past it also conducted through special purpose entities.

Where, due to the effect of the guarantees provided or the content of other contractual provisions, it is felt that substantially all risks and benefits attaching to aircraft sale contracts have not transferred to customers, the sale is not recognised as such in the annual and/or interim accounts. Rather, the entire operation is recognised as a lease, postponing the recognition of profits until such time as the risks no longer obtain by way of recognition under deferred income and carrying the aircraft among the Group's assets, undergoing normal depreciation. If, however, the operation is structured in a manner in which substantially all risks and benefits are transferred to the customer, it is booked as a loan or a finance lease, with the sale being recognised upon delivery and the financial component being recognised under financial income on an accruals basis. If contracts envisage a buy-back clause or a residual value guarantee, the operation is recognised as a sale only if the present value of the guarantees can be considered immaterial with respect to the overall value of the transaction; otherwise, the aircraft is carried under the Group's assets and depreciated. All likely risks associated with operations carried out by GIE ATR are measured on the basis of a prudent valuation conducted by management and are either deducted directly from the carrying value of the asset or are recognised under provisions for risks and charges.

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

In order to hedge exposure to changes in flows of receipts and payments associated with long-term construction contracts denominated in currencies other than the functional currency, the Group enters into specific hedges for the expected individual cash flows in respect of the contracts. The hedges are entered into at the moment the commercial contracts are finalised, except where the award of the contracts is felt to be highly likely as a result of existing framework contracts. Exchange-rate risk is normally hedged with

plain vanilla instruments (forward contracts); in some cases, however, in order to protect the Group against the persistent adverse trend in the US dollar, we have entered into more highly structured operations that, while substantively hedging the positions, do not qualify for hedge accounting under IAS 39. In these cases, as in all cases where hedges prove to be ineffective, changes in the fair value of such instruments are taken immediately to the income statement as financial items, while the underlying is valued as if it were exposed to exchange rate variations. Hedges in the former case are carried as cash flow hedges, considering as ineffective the part relating to the premium or discount in the case of forwards or the time value in the case of options, which is recognised under financial items. The effects of this recognition policy are reported in Section 8 ‘Net financial income and expense’. Hedges in the former case are carried as cash flow hedges, considering as ineffective the part relating to the premium or discount in the case of forwards or the time value in the case of options, which is recognised under financial items.

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

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

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

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

contract management and risk analysis tools designed to identify, monitor and quantify the risks associated with such contracts. The amounts posted in the financial statements and in the interim reports represent management's best estimate at the reporting date using said procedures.

In addition, the Group's operations regard sectors and markets where many disputes are settled only after a considerable period of time, especially in cases where the customer is a government entity, making it necessary for management to estimate the outcome of such disputes. The main potential loss situations classified as 'probable' or 'possible' (no provision is recognised in the annual and/or interim accounts for the latter) are discussed further on.

V.6 Disclosure on Employee Severance Pay (Finance Act of 2007 and enabling acts)

Starting from 1 January 2007, the Finance Act and the related enabling acts introduced changes concerning the rules governing employee severance pay, including giving the employee the choice of electing where the benefit will accrue.

Specifically, the employee may direct new funds allocated as severance pay towards pre-selected pension schemes or may elect that the funds remain with the company (in this case, the company will make severance pay contributions into a treasury account set up with INPS, the national social security institute). Currently, given the uncertainty as to the interpretation of the recently-issued rules, the different possible interpretations of the qualification of the accruing severance pay in accordance with IAS 19, the consequent changes in the actuarial calculations relating to accrued severance pay, as well as the impossibility of estimating choices of employees as to the destination of the accruing fund (for which the individual employee has until 30 June), making any assumption about changes to the actuarial calculation of severance pay accrued at 31 March 2007 would be premature.

VI. SIGNIFICANT NON-RECURRING EVENTS OR TRANSACTIONS

On 30 March 2007 Finmeccanica completed the purchase of 25% of Selex Sensors and Airborne Systems S.p.A. from BAE Systems for about €mil. 400. The value of the

investment is reflected in the net financial indebtedness at the end of 2006. Therefore, the transactions had no impact on the balance sheet for the period.

VII. EFFECTS OF CHANGES IN THE ACCOUNTING STANDARDS ADOPTED

VII.1 Non-recurring costs

Non-recurring costs were previously classified by the Group among inventories. In 2006, the regulations implementing Law 808/1985 underwent profound changes. Specifically, within the scope of programmes eligible for intervention under Law 808, special rules were carved out for those involving national security. For these programmes, the obligations on the part of the entities receiving the incentives of the interventions translate into royalties to be paid to the Distributing Agency based on sales made. Similar treatment is expected for programmes of European interest. Generally, the obligation to repay the amount without interest stands for the other programmes.
As a result of these changes to the law and especially the specific methods for performing the obligations of the entities receiving the incentives of the interventions associated with each category of programmes, the payables pursuant to Law 808 were reallocated in the balance sheet. Payables for "civil" programmes were classified among other current and non-current liabilities, based on the assumed date of repayment, while interventions relating to national security programmes or those of European interest were taken against the correlating non-recurring costs, recognised among intangible assets.

The primary changes compared with balance sheet and income statement at 31 March 2006 were:

- the reclassification of non-recurring costs among intangible assets, due to the overall redefinition of the accounting treatment of these items and in adherence with the practices developed following the introduction of the IFRSs;

- the reclassification of payables pursuant to Law 808 for "civil" programmes that were classified among other current or non-current liabilities, based on the assumed date of repayment, while interventions relating to national security programmes were taken against the correlating non-recurring costs, recognised among intangible assets. In the event where interventions exceeded capitalised costs, the difference was classified among other liabilities;
- the recognition of non-current receivables from the MED with regard to the current value of interventions pursuant to Law 808 relating to national security projects where receipt of payment is deferred;
- the recognition of payments for royalties relating to sales already made but not yet paid to the Distributing Agency;
- the increase in non-current assets and liabilities. In the past, these items where entirely classified within working capital.

In order to provide a better comparison of the income statement and the statement of cash flows for the same period of 2006, it should be noted that:

- the capitalisation of non-recurring costs were recognised in the first quarter of 2007 income statement as a reduction of costs. In the first quarter of 2006, this value was treated as a separate component of revenue, within the value of production (change in work in progress, semi-finished and finished goods);
- the cash flows relating to these expenses were recognised among investments in the first quarter of 2007 statement of cash flows. In the first quarter of 2006, these figures where treated as "change in other operating assets and liabilities", within the cash flow generated by operating assets.

VIII. SEGEMENT INFORMATION

<u>Primary frame of reference</u>

The Group operates in a variety of industry segments: helicopters, defence electronics, aeronautics, space, defence systems, energy, transportation and other activities.

For a more detailed analysis of the main programmes, outlooks and operating indicators for each segment, see the Report on Operations in the business segment section. The results for each segment at 31 March 2007, as compared with those of the same period of the previous year, are as follows:

	31 March 2007									
	Helicopters	**Defence Electron-ics**	**Aero-nautics**	**Space**	**Defence Systems**	**Energy**	**Transportation**	**Other activities**	**Eliminations**	**Total**
Revenue from external customers	718	601	320	160	210	217	339	36		2,601
Revenue from other segments	2	79	92	6	28	1	(9)	11	(71)	139
Operating result	75	6	20	1	1	11	9	(22)		101
Financial income and expense - net										(21)
Share of result of associates								1		1
Tax expense										(63)
Profit (loss) from discontinued operations										
Profit (loss) for the period										18
Group share of net result										12
Minority share										6
Investments	40	42	213	6	10	2	6	3		322

	31 March 2006									
	Helicopters	**Defence Electron-ics**	**Aero-nautics**	**Space**	**Defence Systems**	**Energy**	**Transportation**	**Other activities**	**Eliminations**	**Total**
Revenue from external customers	575	595	333	140	208	201	340	56		2,448
Revenue from other segments	3	113	75	-	6	-	-	5	(67)	135
Operating result	44	42	15	9	7	7	16	(40)		100
Financial income and expense - net										342
Share of result of associates	-	(1)	(1)	-	-	-	-	(2)		(4)
Tax expense										(55)
Profit (loss) from discontinued operations										-

Profit (loss) for the period									383
Group share of net result									379
Minority share									4
Investments	15	72	66	4	70	3	5	2	237

The assets and liabilities attributable to the segments at 31 March 2007 and 31 December 2006 are as follows:

31 March 2007

	Helicopters	Defence Electronics	Aeronautics	Space	Defence Systems	Energy	Transportation	Other activities	Eliminations	Total
Assets	5,298	6,436	4,442	1,125	2,295	1,053	1,920	2,997	(3,196)	22,370
Liabilities	3,204	3,703	4,142	675	1,670	995	1,816	4,148	(3,340)	17,013

31 December 2006

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

Secondary frame of reference

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

	31-Mar-07	31-Mar-06
Europe	2,062	1,925
North America	315	264
Other	363	394
	2,740	2,583

Assets are geographically distributed as follows:

	31-Mar-07	31-Dec-06
Europe	21,667	22,819
North America	591	351
Other	112	101
	22,370	23,271

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

	31-Mar-07	31-Mar-06
Europe	303	235
North America	13	2
Other	6	-
	322	237

IX. NOTES TO THE QUARTERLY FINANCIAL STATEMENTS AT 31 MARCH 2007

To give additional information on the Group state of affairs, statements of reclassification for the 'Income Statement', the 'Balance Sheet', the 'Net debt' and 'Cash flow statement' have been prepared.

For ease of understanding and comparability, below are the main changes in the scope of consolidation:

- Alenia North America- Canada Co and Global Military Aircraft Systems LLC, consolidated during the same period of last year using the equity method, were consolidated on a line-by-line basis;
- Lmatts LLC and Global Aeronautica LLC, consolidated during the same period of last year using the equity method, were consolidated using the proportional method;
- Alenia Composite S.p.A consolidated during the same period of last year using the equity method, was consolidated on a line-by-line basis;
- on 29 March 2007, under agreements with BAE Systems, Finmeccanica purchased the control of the remaining 25% of Selex Sensors and Airborne Systems S.p.A.;
- on 4 October 2005 52.7% of the share capital of Datamat S.p.A was purchased. After the PPO launched at the end of 2005 and ended in January 2006, the percentage owned rose up to 89%. Later on, Finmeccanica carried out a number

of additional acquisitions, bringing its interest to more than 98%, including treasury treasures held by the company;

- Seicos S.p.A, consolidated during the same period of last year using the equity method, was consolidated on a line-by-line basis starting from the 2006 financial statements;
- Energy Service Group Ltd was consolidated on a line-by-line basis starting from 28 July 2006, after the purchase of the remaining 55% of the share capital;
- Thomassen Turbine Systems BV was consolidated on a line-by-line basis, starting from the 2006 financial statements, after its purchase;
- the LFK GmbH group, purchased on 1 March 2006 from the joint venture MBDA, was consolidated using the proportional method (25%) as from that date;
- Westland Technologies Canada Ltd was deconsolidated following its closure starting from 14 June 2006;
- the following mergers were carried out last year:
  - with date of efficacy 1 July 2006 Westland do Brasil - Commercio e Representacoes Ltda was merged into Sobrahel - Societade Brasileira Ltda, which changed its corporate name to AgustaWestland do Brasil Ltda;

The 'Income Statement' includes figures for the first quarter and for the comparative period as well, but from the date of purchase and until the date of sale (or date of efficacy of the deed).

The 'Balance Sheet' at 31 December 2006 does not include figures for the Groups and companies which were consolidated starting from 2007.

Always with reference to data comparability, the first three months of 2007 have been marked by changes in the euro against the main currencies of interest for the Group. Specifically, the currency exchange rates at 31 March 2007 and the average exchange rates for the period showed, for the main currencies, these changes from 2006: final exchange rates for the period (euro/US dollar +1.11% and euro/pound sterling +1.22%); average exchange rates for the period (euro/US dollar +8.27% and euro/sterling pound – 2.32%).

Below are the exchange rates adopted for the currencies that are most significant for the Group:

	At 31-Mar-07		At 31-Dec-06	At 31-Mar-06	
	average exchange rate for the period	closing exchange rate for the period	closing exchange rate for the year	average exchange rate for the period	closing exchange rate for the period
US Dollar	1.31049	1.33180	1.31700	1.20205	1.21040
Pound Sterling	0.67054	0.67980	0.67150	0.68610	0.69640

The table below shows the consolidated results for the first three months of 2007.

€mil.		For the 3 months at 31 March		Year
		2007	2006	2006
Revenue	*	2,740	2,583	12,472
Purchase and personnel costs	**	(2,544)	(2,569)	(11,121)
Depreciation and amortisation		(105)	(85)	(482)
Write-downs		(4)	(3)	(23)
Restructuring costs	***	(3)	(6)	(10)
Change in work in progress, semi-finished and finished goods		14	165	(24)
Other net operating income (costs)	****	3	15	66
EBIT		101	100	878
Net financial income (expense)	*****	(20)	338	394
Income taxes		(63)	(55)	(243)
NET RESULT BEFORE DISCONTINUED OPERATIONS		18	383	1,029
Net result from discontinued operations		-	-	(9)
NET RESULT		18	383	1,020
of which:				
. Group		*12*	*379*	*988*
. minority interests		*6*	*4*	*32*

Notes on the income statement reclassification:

(*) Includes "revenues" and "revenues from related parties"

(**) Includes "costs from related parties", "costs for goods", "costs for services", and "personnel costs" (net of restructuring costs), net of "capitalized costs for internal production".

(***) Includes the restructuring costs classified as "personnel costs" and "other operating costs".

(****) Includes the net amount of the item 'other operating revenues', 'other operating revenues from related parties and 'other operating costs' (less restructuring costs).

(*****) Includes 'financial income and expense' and 'financial income and expense from related parties' and 'effect of accounting for equity investments with equity method'.

- 'revenues' of €mil. 2,740 rose by some 6% from the year-earlier period (€mil. 2,583). The increase is mainly due to: Helicopters, Space, Defence Systems and Energy;

- 'purchase and personnel costs' fell from €mil. 2,569 of the same period in 2006 to €mil. 2,544 in 2007. In particular, these include:

	31 Mar-07	31 Mar-06
Purchase of materials	1,152	971

Change in inventories	(76)	(29)
Purchase of services	714	720
Costs of rents and operating leases	60	54
Purchases and services from related parties	11	16
Total costs of purchases and services	1,861	1,732
Wages and salaries	655	613
Social security contributions	176	170
Costs for staff severance pay	22	21
Costs related to other defined-benefit plans	21	21
Costs related to defined-benefit plans	8	7
Employee disputes	-	2
Other costs	15	14
Total personnel costs	897	848
Capitalisation of internal construction costs	(214)	(11)
Total	2,544	2,569

The performance of costs of purchases (down 1 %) was affected mainly by the different recognition of items related to 'non-recurring costs'. Starting from the 2006 financial statements, as described in the section entitled "effects of changes in the accounting standards adopted", 'non-recurring costs' and the related items are classified differently than in past periods. Capitalisation of these costs was therefore recognised in the first quarter of 2007 as a reduction in costs, while, in the first quarter of 2006, this amount was set out as a separate revenue component within the value of production (change in work in progress, semi-finished and finished goods). The 'costs of purchases and services' (not including 'capitalisation of internal construction costs") like 'revenues', due to the change in the scope of consolidation and to the performance of the segment activities.

The increase in personnel costs from €mil. 848 in the first three months of 2006 to the €mil. 897 in the first three months of 2007 is due to the change in the scope of consolidation, especially for foreign companies, to social security liabilities payable by enterprises in connection with the pension benefits due legally and contractually to UK employees, to medium/long-term incentive policies for management introduced within the Group and to the impact of the increase in average pound sterling/euro exchange rate.

The average workforce was 57,769 from 55,959 in the year-earlier period, an increase of 1,810 due to the change in the scope of consolidation and in particular, to increases reported in the Aeronautics, Helicopters, Energy and Transportation segments, offset by a decrease in Defence Electronics.

The workforce at 31 March 2007 was 58,685, up 626 from 58,059 at 31 December 2006 due to the change in the scope of consolidation in addition to positive turnover in the Aeronautics, Helicopters and Transportation segments especially.

Costs for personnel reorganisation/restructuring are reported as restructuring costs;

- depreciation and amortisation rose mainly due to the different accounting treatment of 'non-recurring costs' (with a related increase in amortisation of intangibles), the change in the scope of consolidation and the completion of the process of allocating the purchase price of assets in the Helicopters, Defence Electronics and Space sectors. Depreciation and amortisation for the period of €mil. 105 (€mil. 85 in the same period of 2006), include €mil. 74 of depreciation for property, plant and equipment (€mil. 71 in the same period of 2006) and €mil. 31 of amortisation of intangible assets (€mil. 14 in the same period of 2006);

- write-downs of receivables were €mil. 4 (€mil. 3 in the same period of the prior year);

- net restructuring costs were €mil. 3 (€mil. 6 in the same period of the prior year). Specifically, the net balance is the result of an increase relating to the introduction of a reorganisation plan in the Defence Systems segment (€mil. 6) and a decrease in the shares of the reconversion and restructuring provision made available as a result of the integration process begun some time ago between the Italian and British companies in the Helicopters sector (€mil. 5). Other net costs relate to the Defence Electronics and Other Activities sectors;

- other net operating income and costs include net income of €mil. 3 (€mil. 15 of net income in the same period of 2006) and break down as follows:

	31-Mar-07	31-Mar-06
Grants for training, research and development	7	6
Net exchange rate differences on operating items	1	-
Indirect taxes	(9)	(5)
Net adjustment of receivables and payables in foreign currency at the end-of-period exchange rate	1	2
Gains from the sale of non-current assets	1	18
Insurance reimbursements	2	6
Transfers (accruals) of provisions	4	(8)
Other operating income (costs)	(4)	(4)
Total	3	15

Specifically, the 'gain from the sale of assets' in the first quarter of 2006 mainly relates to the disposal of the production site of Chelmsford (UK) by Selex Communications Ltd;

- EBIT stood at €mil. 101 substantially in line with the year-earlier period (€mil. 100). In particular, this result is attributable to the Helicopters, Aeronautics and Energy sectors. These improvements are balanced by a deterioration in other sectors;

- 'net financial income and expense' of €mil. 20 of net financial expense (including transactions with related parties which yields a net financial expense of €mil. 3) represents a decrease of €mil. 358 from the year-earlier period (€mil. 338 of net financial income including transactions with related parties which yields a net financial expense of €mil. 3). The item also includes the positive effect of the valuation of equity investments with the equity method of €mil. 1 compared with a negative effect of €mil. 4 in the first quarter of 2006. Specifically:

	31-Mar-07			31-Mar-06		
	Income	Expense	Net	Income	Expense	Net
Income from equity investments and securities	1	-	1	366	-	366
Discounting of receivables, payables and provisions	1	-	1	-	(1)	(1)
Interest	28	(33)	(5)	14	(34)	(20)
Commission income/expense (including						

commissions on non-recourse items)	-	(2)	(2)	-	(1)	(1)
Fair value adjustments through profit or loss	12	(15)	(3)	29	(27)	2
Premiums paid/received on forwards	5	(16)	(11)	2	(2)	-
Exchange rate differences	60	(58)	2	57	(58)	(1)
Income/expense from related parties	1	(4)	(3)	-	(3)	(3)
Other net financial income and expense	2	(3)	(1)	2	(2)	-
	110	(131)	(21)	470	(128)	342

In 2006, 'income from equity investments and securities' included €mil. 364 in capital gains from the stock market placement of the Ansaldo STS Group (52.174% of the share capital).

The item 'interest' includes results of the Group's financial management, including premiums received/paid on interest rate hedges (interest rate swap).

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

	31-Mar-07			31-Mar-06		
	Income	**Expense**	**Net**	**Income**	**Expense**	**Net**
Swaps and forex options	4	(3)	1	4	-	4
Interest rate swaps	2	(7)	(5)	2	(11)	(9)
Options on STM	-	-	-	1	-	1
Ineffective portion of hedging swap	4	(2)	2	12	(6)	6
Option embedded in the exchangeable bond	2	(2)	-	10	(10)	-
Other equity derivatives	-	(1)	(1)	-	-	-
	12	(15)	(3)	29	(27)	2

Income and expense from options on STM refers to the fluctuations in the fair value of the option embedded in the exchangeable bonds with STM shares as underlying (no fluctuation in the first quarter of 2007) and the offsetting option with the same underlying and same key parameters as that embedded in the exchangeable bonds issued. As a result of this transaction, the Group is in an essentially neutral position with regard to further variations in the fair value of the call option sold (income of €mil. 2 and expense of €mil. 2).

The 'effects of the valuation using the equity method' mainly relate to:

	31-Mar-07	31-Mar-06
AvioGroup S.p.A. results	-	(2)
Net results of other holdings	1	(2)
	1	(4)

- 'income tax expense' was €mil. 63 compared with €mil. 55 for the same period of 2006.

  In particular, this is the algebraic sum of:

	31-Mar-07	31-Mar-06
Corporate income tax (IRES)	33	27
Regional business tax (IRAP)	27	26
Benefit under consolidated tax mechanism	(27)	(20)
Other income taxes	11	14
Tax related to previous periods	-	-
Provisions for tax disputes	1	1
Deferred tax (assets) liabilities - net	18	7
	63	55

Income from adopting the consolidated taxation mechanism for IRES purposes (a tax introduced by Legislative Decree 344/2003) from 1 January 2004 was considered in the calculation of income taxes. According to this mechanism, there is only one taxable income for all the Group companies included in the scope of consolidation.

This option makes it possible to offset the tax results (taxable income and losses in the consolidation period) of the participating companies. As a result, the quarterly report includes the benefit resulting from the tax losses for the period up to the limit of the taxable income included in the consolidated tax base. This income was then allocated to all the consolidated companies reporting a fiscal loss.

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

- 'net result from discontinued operations' was separately indicated in the income statements. Accordingly, the item includes the result for the period of the operations sold or being sold:
  - for the first three months of 2007, the results of the operations being sold as held by the Group in the bus manufacturing industry.

	31-Mar-07	31-Mar-06
Revenue	18	28
Costs	(18)	(28)
Net financial income	-	-
Tax expense	-	-
	-	-

The table below shows an analysis of consolidated balance sheet at 31 March 2007.

€mil.	31-Mar-2007	31-Dec-2006	31-Mar-2006
Non-current assets	10,109	9,897	7,785
Non-current liabilities (*)	(3,248)	(3,275)	(2,044)
	6,861	6,622	5,741
Inventories	3,237	3,095	5,765
Contract work in progress	3,233	2,823	2,732
Trade receivables	3,757	3,856	3,528
Trade payables	(3,196)	(3,561)	(3,073)
Advances from customers	(5,546)	(5,529)	(4,425)
Provisions for short-term risks and charges	(551)	(571)	(541)
Other net current assets (liabilities)	(468)	(547)	(3,283)
Net working capital	466	(434)	703
Net capital employed	7,327	6,188	6,444
Group shareholders' equity	5,304	5,276	4,868
Shareholders' equity of minority interests	85	81	137
Shareholders' equity	5,389	5,357	5,005
Net debt (cash)	1,970	858	1,481
Net (assets) liabilities held for sale (***)	(32)	(27)	(42)

Notes on the reclassified balance sheet:

(*) Includes all non-current liabilities except financial liabilities to related parties (which are included among non-current liabilities to related parties) and non-current financial debt.

(**) Includes tax receivables, other current receivables from related parties (included among current receivables from related parties) and other current assets, net of tax payables, other payables to related parties (included among current liabilities to related parties), and other current liabilities.

(***) Includes the net of non-current assets held for sale and liabilities directly related to assets held for sale.

'Non-current assets' (€mil. 10,109 at 31 March 2007 from €mil. 9,897 at 31 December 2006) show a net increase of €mil. 212:

	31-Mar-07	**31-Dec-06**
Intangible assets	5,430	5,317
Property, plant and equipment	2,774	2,660
Investment properties	1	2
Equity investments	141	140

Financial assets at fair value	862	857
Securities held to maturity	18	16
Receivables	430	426
Deferred taxes	447	470
Other assets	6	9
	10,109	9,897

This rise is specifically due to:

- the recognition of additional goodwill (€mil. 10) arising from the exercise of the put and call options over 25% of the Selex Sensors and Airborne Systems group, previously held by BAE Systems Ltd, and subsequent adjustments to the price;

- the recognition of the relevant goodwill deriving from the subsequent purchase of Datamat S.p.A. shares (€mil. 5);

- the increase (€mil. 26) in property, plant and equipment arising from the consolidation on a line-by-line basis of Alenia North America - Canada Co and Global Military Aircraft Systems LLC and on a proportional basis of Lmatts LLC and Global Aeronautics LLC;

- the increase (€mil. 101) in 'non-recurring costs' due to capitalisation during the period;

- the valuation of the interest held indirectly in STMicroelectronics NV (STM) (6.6% at 31 March 2007) as 'financial assets held at fair value', which broke down as follows:

31 December 2006	840
Fair value adjustment at 31 March 2007	22
31 March 2007	862

The increase due to fair value adjustment had a specific shareholders' equity reserve as a contra-item;

- due to investing activities (specifically €mil. 114 in aeronautics for property, plant and equipment) and opening of receivables and repayments and depreciation and amortisation for the period;

- due to a net decrease stemming from the exchange rate differences due to the translation of financial statements in foreign currency (mainly pound sterling).

'Non-current liabilities' (€mil. 3,248 at 31 March 2007 from €mil. 3,275 at 31 December 2006) show a net decrease of €mil. 27:

	31-Mar-07	31-Dec-06
Severance pay and other employee liabilities	1,231	1,238
Provisions for risks and charges	355	365
Deferred taxes	342	340
Other liabilities	1,320	1,332
	3,248	3,275

This rise is specifically due to:

- the net decrease of 'severance pay and other employee liabilities' (€mil. 7) resulting from the use of the relative provision, net of accruals for the period, mainly in the Defence Electronics and Helicopters sectors, from 'defined benefit plans' having been reviewed by the British companies of AgustaWestland and by Selex Sensors and Airborne System Ltd, in addition to the decrease stemming from the exchange rate differences due to the translation of financial statements in foreign currency (mainly pound sterling);

- the net decrease of €mil. 10 in 'provisions for risks and charges', in particular in provision for product guarantees (€mil. 3) net of transfers and uses of the 'provision for guarantees given' and 'other' €mil. 13;

- the increase in deferred tax liabilities of €mil. 2;

- the net decrease of €mil. 12 of 'other liabilities', mainly due to deferred income;

Specifically, 'other payables' includes the payables to the Ministry of Economic Development (MED) for royalties (€mil. 48 compared with €mil. 46 at 31 December

2006) accrued pursuant to Law 808/1985 for "national security" and similar projects, in addition to payables for disbursement received from the Ministry of Economic Development supporting development of non-national security and similar programmes eligible for the incentives under Law 808/85 (€mil. 564, unchanged from 31 December 2006). The item also includes deferred income of €mil. 198 (€mil. 207 at 31 December 2006).

'Net working capital' shows a positive net value of €mil. 466 compared with a negative net value at 31 December 2006 of €mil. 434. More specifically:

- 'inventories' came to €mil. 3,237 compared with €mil. 3,095 in the prior year:

	31-Mar-07	31-Dec-06
Raw materials, supplies and consumables	1,609	1,543
Work in progress and semi-finished goods	752	800
Finished goods and merchandise	144	134
Advances to suppliers	732	618
	3,237	3,095

Inventories are shown net of impairment charges of €mil. 419 (€mil.418 at 31 December 2006);

- 'contract work in process' amounted to €mil. 3,233 as compared with €mil. 2,823 at 31 December 2006; 'advances from customers' were €mil. 5,546 from €mil. 5,529 at 31 December 2006:

	31-Mar-07	31-Dec-06
Contract work in progress (gross)	6,746	6,184
Advances from customers	(3,513)	(3,361)
Contract work in progress (net)	3,233	2,823

Advances from customers (gross)	13,235	12,996
Contract work in progress	(7,689)	(7,467)
Advances from customers (net)	5,546	5,529

- ‘trade receivables and payables’ of €mil. 3,757 and €mil. 3,196 respectively as compared with €mil. 3,856 and €mil. 3,561 respectively at 31 December 2006 relate to:

	31-Mar-07		31-Dec-06	
	Receivables	Payables	Receivables	Payables
Related parties	358	52	377	75
Other third parties	3,399	3,144	3,479	3,486
	3,757	3,196	3,856	3,561

- ‘provisions for short-term risks and charges’ of €mil. 551 decreased by a net €mil. 20 as compared with €mil. 571 at 31 December 2006. The reduction relates to uses and reversals of: the conversion and restructuring provision for Helicopters (€mil. 5) and Defence Systems (€mil. 2), the provisions for penalties and product guarantees (€mil.8), provision for bad debts (€mil. 4) and other provisions (€mil. 9). The most significant allocations regard the provisions for product guarantees (€mil.6) and conversion and restructuring (€mil. 2).

With regard to the risk provisions, the Group’s operations regard industries and markets where many disputes are settled only after a considerable period of time, especially in cases where the customer is a government entity.

Of course, in application of related accounting standards, provisions have been made for any obligations related to probable and quantifiable risks. Likewise, to the best of our knowledge, regarding other disputes against the Group, no specific allocation has been made since the Group reasonably believes that such disputes may be resolved satisfactorily and without any significant impact on the results.

The situations below are mentioned here solely for the purposes of full disclosure.

Of particular note:

- the dispute in which Finmeccanica has been asked to cover the contractual commitments assumed upon the sale of the former subsidiary Finmilano S.p.A. to Banca di Roma (now Capitalia) originated from the assessment ordered by the Rome Office of Direct Taxes of Finmilano S.p.A. regarding the disallowance of the tax deductibility of the capital loss originating in 1987 on the sale of a non-recourse 'deferred' receivable at a price below the nominal value. In essence, the Italian tax authorities felt that this sale was actually a financing transaction and that the loss, in the same manner as a finance cost, should not have been deducted in its entirety in 1987, but should have been recognised over subsequent years as implicit interest in the transaction.
  After the Court of Cassation (the supreme court of appeal) - in allowing the appeal filed by the tax authorities - had returned the parties to the court of first instance, the latter once again upheld the company's complaint. This ruling was once again appealed to the Court of Cassation. It should be noted that substantial charges to be paid by Finmeccanica are not currently foreseeable. In agreement with the bank, it has been deemed that there is insufficient justification to accept the settlement of pending disputes pursuant to Article 16 of Law 289/2002, partly in light of the fact that the significant financial outlay that this would have required does not make sense from a cost-benefit point of view;

- the dispute resulting from the notice to settle the registry fee of about €mil. 10, which was received by Finmeccanica in July 2001 and due on the capital increase approved in 1998. Although the tax liability had already been recognized in the related financial year, the company felt it was unnecessary to meet the tax demand because it was unjustified both in law and in fact. In fact, in addition to being received after statutory deadline, the notice contained a request for a tax related to a tax base that was partially inconsistent with applicable laws. The Tax Commission for the Province of Rome upheld the company's dispute in its ruling filed in December 2002. The ruling was appealed by the company in relation to the failure to order the

tax authorities to reimburse costs. In the first half of 2004, the tax authorities in turn filed a cross-appeal of the same ruling, but only with regard to the decision that confirmed the termination of the office's assessment power in the matter. No objection was raised, however, with regard to the substance of the original ruling establishing the partial lack of justification of the amount requested by the revenue office. In a ruling filed in October 2004, the appeal court rejected the company's primary appeal regarding the lack of reimbursement of costs, but at the same time declared that the cross appeal filed by the tax authorities was inadmissible in that it was filed after the ordinary statutory deadlines. In particular, the Regional Tax Commission in Rome upheld the complaint filed by the company regarding the fact that the tax authorities had erroneously deemed the suspension of the procedural deadlines defined by Article 16 of Law 289/02 (facilitated settlement of pending disputes) to be applicable, given that the case did not fall within the scope of this law. The sentence of the court of second instance has been appealed to the Court of Cassation by the tax authorities;

- the dispute initiated by Telespazio S.p.A against the Agenzia delle Entrate, Rome District 4 challenging a tax assessment regarding direct income taxation (IIDD) for the year 2000, which contained a demand for a total of about €mil. 30 consisting of additional taxes, penalties and interest. The notice of assessment, served on 27 November 2006, relates to a tax audit completed in 2001 in which the Tax Authority challenged the deductibility of the loss regarding receivables from a foreign company taken by Telespazio SpA within the context of a non-recourse sale carried out following many fruitless attempts to recover these receivables. Specifically, the Tax Authority, deeming the actions undertaken by the Company to forcibly collect the receivables and therefore the evidence of the foreign debtor's solvency or lack thereof to be insufficient, found that the requirements of certainty and precision under the law were not met to allow the loss to be fully deducted, regardless of the fact that the loss was conclusively realised by Telespazio S.p.A. within the context of the non-recourse sale of the receivables arguing that sale per sé guarantees certainty only of the legal loss of the receivable but not the financial loss. The case is currently pending before tax court of first instance and no provision has been made in the

financial statements since, in the Company's opinion, it can prove that the transaction was accounted for properly;

- the dispute initiated by Telespazio S.p.A against the Agenzia delle Entrate, Rome District 4 challenging a tax assessment for the purposes of direct income taxation (IIDD) and regional business taxation (IRAP) for the year 2001 containing an adjustment of about €mil. 9.7 in taxable income at the time the tax statement was prepared. Considering that the adjustment, for IIDD purposes, results in a reduction by an amount equal to the final tax loss in 2001 and that this loss was fully used by the Company in 2006, the total amount owed to the Tax Authority would be about €mil. 7 plus additional taxes, penalties and interest. The notice of assessment, served on 27 November 2006, relates to a tax audit completed in 2003 in which the Tax Authority challenged Telespazio S.p.A.'s reserving tax treatment until the completion of the Astrolink contract. Specifically, in November 2001, the customer Astrolink at its discretion terminated a long-term contract triggering Telespazio's right to compensation under the contract equal to the costs (plus 20% and in any event "be agreed" with the customer) that Telespazio would incur as a result of the early termination. Since it was not possible in 2001 to determine and agree upon the total amount of these costs (and the corresponding compensation revenues), the Company prudentially allocated €mil. 48.5 in the 2001 financial statements to a provision for risks and charges, as it deemed that amount to not be tax deductible. The auditors, starting, instead, with the assumption that Telespazio could have calculated the amount of compensation due from the counterparty as early as 2001 since the costs that it would have incurred as a result of the early termination of the contract were determinable, challenged the failure to account for revenues in the amount of €mil. 58.2 and also gave full tax effect to the amount of €mil. 48.5 in the provision for risks and charges which Telespazio, instead treated as fully taxed. As a result, the Tax Authority determined that Telespazio had €mil. 9.7 more in taxable income in 2001 for direct income taxation and regional business taxation purposes. The case is currently pending before tax court of first instance and no provision has been made in the financial statements since, in the Company's opinion, it can prove that the transaction was accounted for properly.

Beyond the merits, it should be pointed out that it is currently impossible to estimate the substantive costs to be borne by the Finmeccanica Group considering that the liability, if it should be found to exist, would be neutralised by the guaranteed issued by Telecom Italia within the scope of the contract selling its shares of Telespazio in November 2002;

- the dispute initiated by So.Ge.Pa. SpA against the Agenzia delle Entrate, Rome District 4 challenging a tax assessment for the purposes of direct income taxation (IIDD) and regional business taxation (IRAP) for the year 2001 containing a demand for a total of €mil. 18 in additional taxes, penalties and interest. The tax claim, served on 27 December 2006, traces back to a tax audit completed in 2004 against ALS S.p.A., a Finmeccanica Group company absorbed by So.Ge.Pa. in 2006, in which the tax inspectors – without including any formal comments – merely notified the tax office responsible for the assessment of possible violations in applying the regulations concerning the tax appraisal of work in progress inventories within the context of the long-term contract for the provision and launching of the Atlantic Bird1 satellite obtained in 2000. Specifically, the warning originates from the fact the company had, over the years, accounted for these inventories based on the percentage completed (calculated using the cost-to-cost method), thereby rendering the settlement and payments received over the medium-term upon the achievement of various milestones irrelevant since they are not, under the contract, final settlements and therefore recognising as revenues (and therefore taxable) the entire amount of the inventories only when ownership of the satellite was transferred in 2002 upon acceptance in orbit of the satellite by the customer as contractually agreed. By contrast, the tax inspectors asked the competent tax office to assess whether, in reality, under the contract, the various milestones could have been treated using the Work Status (WS) process, so as to include in the tax assessment of work-in-progress inventories the payments received based on the achievement of the WS objectives, regardless of the amounts recognised in the financial statements, on the assumption that the object of the contract could be divided into individual, "autonomous" lots for which each payment represents a final settlement of payments owed.

The tax officials, receiving the auditors' report and without carrying out any further analysis of the matter although it involves a rather complex contractual relationship, issued the notice of assessment against the company. The case is currently pending before tax court of first instance and no provision has been made in the financial statements since, in the Company's opinion, it can prove that the transaction was accounted for properly;

- the appeal, together with ENEL and other parties, filed with the Regional Administrative Court of Lombardy of the resolution of the Italian Electricity and Gas Authority regarding the method of calculating interest due on amounts to be paid, as compensation, in relation to the termination of the Italian national nuclear energy programme.
  Interest due calculated using a different calculation method is around €mil. 13.Previous rulings by the Lombardy Regional Administrative Court do not support the resolutions of the Authority. Accordingly, it is reasonable to expect a favourable outcome for Finmeccanica;

- on 6 July 2001, Finmeccanica and its subsidiary Alenia Spazio S.p.A. (formerly ALS S.p.A., now SO.GE.PA S.p.A.) received notice of a summons to appear before the Texas Federal Court to respond to a request for damages resulting from the alleged violation of agreements as part of the Gorizont programme, which is related to events dating back to 1998-1999 when Alenia Spazio operated as a division of Finmeccanica (on 9 July 2001, Alenia Spazio alone received a second summons to appear before the court for the same issue).
  Based on an examination of the case files by U.S. lawyers, the company feels there are valid reasons to contest the substance of the demands of the plaintiffs. The pre-trial issue of the lack of jurisdiction of the Texan Court raised by Finmeccanica and ALS in both suits was given a favourable outcome by the various degrees of jurisdiction. Regarding the dispute against Finmeccanica and ALS, on 8 June 2006 the plaintiff filed a Petition for Writ of Certiorari to the Federal Supreme Court of the United States to obtain a review of all the papers of the case. With ruling dated 2 October 2006, the Federal Court of the Unites States rejected this Petition. Accordingly, both cases commencing in Texas can be considered as closed;

- arbitration is under way to settle a dispute between Consorzio Trevi - of which the subsidiary AnsaldoBreda S.p.A. is a member with a 40% stake - and Trenitalia S.p.A. in relation to the application of penalties for the late delivery of ETR 500 trains. Consorzio Trevi has contested the penalties and has requested reimbursement of the significant additional costs incurred. The arbitration board arranged for the issues involved in the arbitration to be examined by an independent expert. The expert's report was filed on 10 January 2005 and is in favour of Consorzio Trevi. However, on 19 October 2005 the arbitration board arranged, upon request of Trenitalia, for a supplementation of the expert's report; this was filed on 31 January 2006. The findings of this supplementation of report do not provide clear indications on the amount of Trenitalia's delays; these indications had been clearly reported in the former report. For this reason, Consorzio Trevi has confirmed its own reservations concerning the lawfulness of the supplementation of report and demanded to file its own considerations on this matter. On 13 March 2006 the parties filed their final pleadings. The arbitration award is expected to be filed by May 2007;

- on 1 October 2003, the European Commission notified the Ministry of Foreign Affairs of the formal proceedings initiated for an investigation against the Italian State, pursuant to Article 11 of the EU Treaty, in relation to subsidies granted by the Italian Government to the companies Alenia Aeronautica S.p.A., Aermacchi S.p.A., and Agusta S.p.A., based on Law 808/85, for six research and development projects. The Commission considers these subsidies to be state aids. The preliminary assessment of the Commission was that these subsidies were not notified to the Commission at the time, even though they were each in excess of the ECU 20 million threshold (1 ECU being equal to 1 euro). On 22 January 2004, the decision to open proceedings was published in the EU Official Journal.

  The Italian authorities submitted their own observations to the Commission on 30 January 2004.

  In response to requests of third parties, the Commission requested further information from the Italian Government, which was provided in the latter part of May 2004. Further exchanges of requests and information between the Commission and the Italian Government continued in the second half of the year. With its letter of

22 June 2005 C(2005)1813, received by the Permanent Representation of Italy in the EU on 24 June, the European Commission informed the Italian Government of its decision to extend the scope of the current proceedings to an additional six projects of the aforementioned companies that had initially been excluded by the Commission itself. The Italian Authorities submitted their reply to the Commission on 29 November 2005. On 19 December 2005 the Commission served on the Italian Government further considerations filed by a third anonymous party, and the Government replied accordingly on 24 February 2006.At the moment, this procedure deeply affects the application principles of Law no. 808/85; Finmeccanica will follow the issue with special attention with the assistance of local counsel. At present, information is being exchanged between the Italian Government and the Commission before the latter issues its final decision, which is expected happen by September 2007;

- In November 1997 in relation to a contract commissioned by Prepa, the Puerto Rican Electric Power Authority, the company Abengoa awarded to Ansaldo Energia a sub-supplier contract for expansion work on the San Juan, Puerto Rico power plant.
  In connection with the contract between Abengoa and Prepa, American International Insurance Company of Puerto Rico ("AIIP"), a member of the AIG group, issued a performance bond and a payment bond, each in the amount of US$mil. 125, in favour of Prepa which Ansaldo Energia, as a supplier, counter-guaranteed for US$mil. 36 each.
  In 2000, Abengoa unilaterally terminated its contract without informing Ansaldo Energia and filed suit against the customer in the Court of Puerto Rico seeking compensation for damages it allegedly suffered.
  In 2001, Ansaldo Energia initiated arbitration proceedings in Paris seeking a finding that Abengoa breached the contract by terminating its agreement with Prepa without notifying Ansaldo Energia in advance. The arbitration finding, issued in March 2003, came out in favour of Ansaldo Energia.
  In order to avoid any enforcement of the aforementioned guarantees, on 13 May 2005, Ansaldo Energia brought an action against Abengoa, AIG and AIP before the Court of Milan, requesting that its counter-guarantees be found void, or, in the

alternative, that it be held harmless by Abengoa. AIIP asked that Ansaldo Energia be held jointly liable to hold harmless AIG in the event it loses the case.

In the opinion of its legal team, even if the court does not accept Ansaldo Energia's arguments and, if the counter-guarantees are enforceable, the company could, in any case, initiate an action against Abengoa, a company that is absolutely solvent, even based on the aforementioned arbitration award.

- 'other net current assets (liabilities)' totalled €mil. 468 of net current liabilities, down €mil. 79 from the prior year (€mil. 547 of net current liabilities at 31 December 2006):

	31-Mar-07		**31-Dec-06**	
	Assets	**Liabilities**	**Assets**	**Liabilities**
Employees	26	379	26	337
Prepaid expenses and deferred income	82	103	80	100
Government grants	78	-	83	-
Direct taxes and others to the Tax Office	500	301	469	322
Social security	12	173	7	201
Payable to Min. of Econ. Dev. Law 808/1985	39	57	38	58
Payable to Min. of Econ. Dev. for monopoly rights Law 808/1985	-	16		15
Related parties	45	13	35	19
Derivatives	120	91	147	104
Other	218	455	213	489
	1,120	1,588	1,098	1,645

Other liabilities of €mil. 455 (from €mil. 489 at 31 December 2006) also include:

- €mil. 43 (€mil. 33 at 31 December 2006) due to EADS NV from GIE/ATR - consortium owned by Alenia Aeronautica S.p.A. and EADS NV;
- €mil. 36 (unchanged from 31 December 2006) due for the repurchase of a G222 aircraft;
- €mil. 43 (€mil. 41 at 31 December 2006) due in respect of contractual penalties;
- €mil. 30 (€mil. 38 at 31 December 2006) due for commissions;
- €mil. 27 (€mil. 24 at 31 December 2006) due for royalties.

The table below sets out the asset and liability positions related to derivative instruments:

	31-Mar-07		31-Dec-06	
	Assets	Liabilities	Assets	Liabilities
Forward forex instruments	95	57	115	69
Forex options	2	2	1	-
Interest rate swaps	1	19	7	21
Options on STM	13	-	13	-
Exchangeable bond option	9	9	11	11
Other equity derivatives	-	4	-	3
	120	91	147	104

Forward forex instruments

The notional value of the forward transactions totalled €mil. 3,103, of which €mil. 2,207 is related to contracts to sell and €mil. 896 to contracts to buy, primarily in USD.

The Group hedges its own contracts for purchases or sales denominated in a currency different from the functional currency using forward contracts of amounts, maturities, and key parameters that are similar to the underlying position. Under Group procedures, derivative instruments are purchased with the intent to hedge certain or highly probably commitments and, as such, are designated as hedging instruments at the time of purchase. The effectiveness of the hedge is tested at least at each interim or year-end reporting date using mathematical and statistical methods. In the event that, due to its nature or following such tests, a derivative instrument held should be found to no longer be an effective hedge, the fair value of the instrument is immediately recognized through profit or loss. In the event the designation of the instrument as a hedge should continue to be supported by the tests of actual and future effectiveness, the cash-flow hedge accounting method of recognition is adopted. The change in the fair value of forward instruments is due to the depreciation of the US dollar against the euro: the exchange rate rose from 1.3170 at 31 December 2006 to 1.3318 at 31 March 2007.

Forex options

At 31 March 2007 forex options are held in the notional amount of €mil. 403, carried out by the Group Parent primarily on behalf of its subsidiaries. Given their nature and the

particularly restrictive requirements of IAS 39, these instruments do not qualify for hedge accounting. From 31 December 2004 to now almost all of these transactions have been closed. The fair value of the instruments included in the portfolio is nil (positive in the amount of €mil. 2 and negative for €mil. 2). During the quarter income of €mil. 1 and expense of €mil. 2 were recorded.

Interest rate swaps

At 31 March 2007, the Group held interest rate swaps totalling €mil. 830. The main instruments are as follows:

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

(a) The transaction was carried out to benefit from low short-term interest rates without, however, exposing the Group to the risk of any subsequent increases. As such, the exposure was converted to a floating rate through 19 December 2005 and back to fixed (5.80% average) after that date.

The transaction was measured at fair value through profit or loss, thereby generating a profit of €mil. 1 in the quarter. At 31 March 2007, the fair value of the instrument was a negative €mil. 10.

(b) The transaction was carried out during 2005 in order to earn short-term benefits from low interest rates. The instruments purchased also include a number of interest rate options that enable the Group to protect portion of the debt portfolio exposed to floating rates and to switch to floating for additional portions of the debt.

The transaction was measured at fair value through profit or loss, thereby generating a loss of €mil. 6 in the quarter. At 31 March 2007 the fair value of the instrument was a negative €mil. 1.

(c) The transaction makes it possible to limit exposure to future changes in the reference interest rate (6-month Euribor) and has been recognised as a cash-flow hedge. At 31 March 2007, the fair value of the instrument was a positive €mil. 1.

This item also includes other minor transactions with a total negative fair value of €mil. 5 and a floating/fixed interest rate swap carried out by the helicopter-related joint venture ATIL, the fair value of which was a negative €mil. 3 at 31 March 2007, and recognised as a cash-flow hedge.

The transactions recognised as cash-flow hedges have resulted in a negative reserve at 31 March 2007 in the amount of €mil. 2 (€mil. 3 at 31 December 2006), whereas those that have been recognised at fair value through profit or loss have produced net financial expense of €mil. 5.

Options on STM

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

31-Dec-06	New operations	Completed operations	Fair value delta	31-Mar-07
13	-	-	-	13

During 2006 transactions were made on an additional 15,000,000 shares, which extended the hedge to 45,000,000 STM shares at 31 March 2007. The fair value of the instruments is a positive €mil. 13 at 31 March 2007 (€mil. 13 at 31 December 2006).

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

Exchangeable bond options

These include the liability related to the call option embedded in the exchangeable bonds. On 1 June 2005 the Group purchased a call option with the same key parameters in order to hedge future changes in the value of the option sold.

Other equity derivatives

Following the stock exchange placement of 60% of the shares of Ansaldo STS, Finmeccanica undertook the obligation to deliver, without compensation, shares to subscribers who held shares through 28 March 2007. The fair value of this obligation at 31 March 2007 amounts to €mil. 4 (€mil. 3 at 31 December 2006) and generated an expense of €mil. 1 for the quarter.

- 'Net capital employed' and 'net assets held for sale' of €mil. 7,327 (€mil. 6,188 at 31 December 2006) and €mil. 32 (€mil. 27 at 31 December 2006) respectively are covered by shareholders' equity (€mil. 5,389 as compared with €mil. 5,357 at 31 December 2006) and net debt (€mil. 1,970 as compared with €mil. 858 at 31 December 2006).

Below is the consolidated net debt at 31 March 2007, as compared with that for 31 March and 31 December 2006.

	31-Mar-07	31-Dec-06	31-Mar-06
Short-term financial payables	202	159	129
Medium/long-term financial payables	1,851	1,865	1,875
Cash and cash equivalents	(472)	(2,003)	(686)
BANK DEBT AND BONDS	1,581	21	1,318
Securities	(19)	(21)	(21)
Financial receivables from Group companies	(36)	(26)	(13)
Other financial receivables	(386)	(452)	(302)
FINANCIAL RECEIVABLES AND SECURITIES	(441)	(499)	(336)
Financial payables to Group companies	406	500	286
Other short-term financial payables	308	722	106
Other medium/long-term financial payables	116	114	107
OTHER FINANCIAL PAYABLES	830	1,336	499
NET DEBT (CASH)	1,970	858	1,481
Net debt (cash and cash equivalents) of discontinued operations	8	6	12

Net Group debt at 31 March 2007 was €mil. 1,970, as compared with net Group debt at 31 December 2006 of €mil. 858, and net Group debt of €mil. 1,481 at 31 March 2006.

With particular regard to the application of IAS 32 and 39, payables include the following effects:

- for the €mil. 500 Finmeccanica Finance S.A. bond issue, bearing a 0.375% coupon, due August 2010, exchangeable for STM shares, IAS 39 requires splitting the liabilities between the financial debt component and the embedded call option component. The debt component is measured by applying the market interest rate at the issue date in place of the nominal interest rate, while the option component, excluded from the financial position, is subject to periodic measurement at fair value. At 31 March 2007 this valuation method led to posting

a debt €mil. 64 less than the face value of the bond; this differential will gradually come down as the maturity date draws near;

- inclusion in the financial position of liabilities in respect of the unpaid portion (€mil. 10) of part of trade receivables assigned without recourse to factoring companies in such a way as to make it prudent to recognise them as financial debt under IAS/IFRS.

Consistent with the approach adopted in the presentation of the accounts for 2006, at 31 March 2007 it was decided – in view of the fact that a significant part of these transactions are designed to hedge 'underlying' commercial positions – not to recognise as debt the balance entries resulting from the fair value measurement of the derivatives on the date that the accounts were closed: at 31 March 2007 these contra-items showed a negative balance.

Taking account of these adjustments, as well as the operational events described below, the Group's net financial debt went from €mil. 858 at 31 December 2006 to €mil. 1,970 at 31 March 2007.

The figure at 31 March 2007 deteriorated by €mil. 1,112 compared to 31 December 2006 and confirms the traditional performance of inflows and outflows, showing great sums in cash used in the first part of each year. This performance was also affected by the investment activity carried out during the quarter and offsets advance receipt of trade receivables on several contracts entered into by Group companies during the last few days of December 2006.
Therefore, free operating cash flow (FOCF) for the period came to negative €mil. 1,107.
The indebtedness figure recognised at 31 March includes the payment of €mil. 6.5 in January to complete the obligatory public offering on the remaining shares of Datamat launched in the final months of last year which resulted in its delisting. The Group expects to complete the process to obtain 100% of the company during the second quarter of 2007.

Also in March, Finmeccanica exercised the call option provided for in agreements with BAE Systems (BAE) to purchase the remaining 25% of Selex Sensors and Airborne Systems S.p.A. (Selex). It paid about €mil. 400 to BAE and as a result now owns 100% of Selex. The transaction only reduced the Group's cash and cash equivalents without having any impact on Group net financial debt, since the effects on debt were already included in the figures for 2006 and recognised among "other financial payables".

As regards the composition of debt, bank debt did not change substantially from €mil. 2,024 at 31 December 2006 to €mil. 2,053 at 31.3.07, mainly due to an increase in short-term debt. However, there was a very significant decrease in cash and cash equivalents which fell from €mil. 2,003 at December 2006 to €mil. 472 at 31 March 2007. This liquidity was used to finance ordinary operations and investment and other strategic areas, especially the acquisition of the remaining shares of Selex Sensors and Airborne Sytems S.p.A., which was reflected in a decrease in the item "other financial payables" which went from €mil. 1,336 at 31 December 2006 to €mil. 830 at 31 March 2007.

The item 'other financial receivables' totalled €mil. 441, down from €mil. 499 at 31 December 2006, and includes about €mil. 377 in respect of the portion of financial receivables that the joint ventures MBDA and Thales Alenia Space hold vis-à-vis the other partners in pursuance of cash pooling agreements made previously. In accordance with the consolidation method used, these receivables, like all the other items, are included in the Group's scope of consolidation on a proportional basis.
The item 'financial payables to Group companies' includes the debt of €mil. 372 of Group companies toward the joint ventures, for the unconsolidated portion.

	For the 3 months ended 31 March	
	2007	**2006**
Cash and cash equivalents at 1 January	2,003	1,061
Gross cash flow from operating activities	255	225
Changes in working capital	(839)	(706)
Changes in other operating assets and liabilities	(203)	(114)
Cash flow generated from (used in) operating activities	(787)	(595)

Cash flow from ordinary investing activities	(320)		(81)	
Free operating cash-flow		**(1,107)**		**(676)**
Strategic investments	(6)		302	
Payment of call option to BAE Systems	(400)		-	
Changes in other financial assets	44		124	
Cash flow generated from (used in) investing activities	(682)		345	
Capital increases	5		15	
Cash flow from financing activities	(63)		(138)	
Cash flow generated from (used in) financing activities	(58)		(123)	
Translation differences	(4)		(2)	
Cash and cash equivalents at 31 March	472		686	

The first three months of 2007 closed with a net decrease in cash and cash equivalents of €mil. 1,531. This can be attributed to the following factors:

- cash flow from operations was a negative €mil. 1,107, in line with the year-earlier period (which registered a negative cash flow of €mil. 676 This was the result of seasonal factors in receipts for the business segments, which are usually concentrated in the last months of the year, an increase in production volumes and increased investments made. For comparative purpose, please note the different accounting treatment for "non-recurring costs".

A breakdown of gross cash flow from operations is provided below:

	31-Mar-07	**31-Mar-06**
Net profit	18	383
Depreciation, amortisation and impairment	109	88
Tax expense	63	55
Accrued (transferred) to funds	(4)	8
Loss associated with discontinued activities		
Cost of staff severance pay, defined-benefit plans and stock grants	50	47
Effects of the measurement of equity investments on the equity method	(1)	4
Gains from the sale of non-current assets	(1)	(18)
Gains from realisation of operating receivables		
Gain on public offering of Ansaldo STS	-	(364)
Financial charges	21	22
	255	225

- cash flow from investing activities was a negative €mil. 682 (as compared to a positive €mil. 345 at 31 March 2006), which includes, in particular, the payment of the call option to BAE Systems for the acquisition of the residual 25% of Selex Sensors and Airborne Systems S.p.A. and the expense of €mil. 6 to complete the Datamat transaction. The figure in 2006 included the receipt of €mil. 398 arising from the sale of the stake in Ansaldo STS S.p.A.;
- cash-flow from financing activities was a negative €mil. 58 (as compared to a negative €mil. 123 at 31 March 2006).

X. FINANCIAL RISK MANAGEMENT

This section describes the operating criteria adopted to manage foreign exchange risk, interest rate risk and equity risk relating to listed shares held.

The application of IFRSs by Finmeccanica involves the adoption of fair value to measure the total portfolio of derivatives. In this respect, the IFRS and related interpretations effectively make a distinction between derivatives considered to be for hedging purposes, for which it is possible to apply hedge accounting, with changes in fair value recognized in the balance sheet, and those for which hedge accounting is not possible and which must be recognized at fair value in the income statement as well as in the balance sheet.

Exchange rate risk management is governed by the directive issued by Finmeccanica in December 2002. The goal of the directive remains that of creating uniformity in management criteria based on industrial - not speculative -strategies so as to contain risks within specific limits by carefully and constantly assessing all foreign currency positions. The methodology adopted calls for the systematic hedging of commercial cash flows resulting from the assumption of contractual commitments of a specific nature as either buyer or seller, thereby ensuring current exchange rates at the date of acquisition of multi-year contracts and neutralizing the effects of exchange rate fluctuations. Therefore, at the moment of receiving payment from a customer (or making payment to a vendor), which takes place at the current exchange rate on that day, the related hedging

transactions are extinguished in order to offset the effects of the difference between the current exchange rate and the rate of the hedging instrument. These transactions are carried out almost exclusively with banks by Finmeccanica's Group Finance Department and then matched with the companies of the Group. The companies that have the greatest need for such hedging transactions are: Alenia Aeronautica and its subsidiaries; Ansaldo Energia; Oto Melara; Selex Sensors Airborne Systems and its subsidiaries; Alcatel Alenia Space Italia; Ansaldobreda; AgustaWestland and its subsidiaries, Selex Communications and its subsidiaries; and Selex Sistemi Integrati. At 31 March 2007 Finmeccanica had outstanding foreign exchange transactions with highly rated financial counterparties in the interest of other Group companies totalling €mil. 3,506 (for an increase of approximately 20% from 31 December 2006), of which €mil. 3,103 for swap and forward transactions (divided between those sold €mil. 2,207 and those purchased for €mil. 896) and €mil. 403 for foreign exchange options.

As a result, the Finmeccanica group recognizes the fair value of foreign exchange derivatives as follows:

- forward instruments qualifying for hedge accounting, the fair value of which totalled a positive €mil. 38 at 31 March 2007;
- options not qualifying for hedge accounting, the overall fair value of which came to nil (€mil. 2 of positive fair value and €mil. 2 of negative fair value).

In addition, the Finmeccanica Group recognises in the income statement the fair value of the ineffective portion of forwards, i.e. the premium points the value of which represents a gain of €mil. 1.

The fair value of forward instruments represents the change in the value of instruments hedging commercial risks and was mainly affected by the great volatility of the euro/US dollar exchange rate, which was 1.3318 at 31 March 2007 from 1.3170 at 31 December 2006, indicating a depreciation of the dollar against the euro. The change in the dollar during the quarter did not have a significant impact on the net fair value of the instruments in the portfolio, which went from a positive €mil. 46 at 31 December 2006 to a positive €mil. 38 at 31 March 2007. This change is not adequately expressed through trading activities since hedging is carried out for the entire life-cycle and on the total amount of the contracts underlying the derivatives transactions while the contracts themselves are recognised in the financial statements only with regard to work in

progress and trade receivables and/or payables. As a result, there is inevitable volatility that impacts equity.

Another significant case is that of premium points which represent the expression of the difference in the interest rate between the currency being hedged (e.g. US dollar) and the currency used in the financial statements. This difference, added to the spot rate, provides the forward value of a swap or forward operation and, in the case of currency sales, generates a cost (pay the US dollar interest rate and receive the euro interest rate). In applying international accounting standards, this component is ineffective and therefore fair value changes are recognized in income statement.

The depreciation of the dollar since 2006 and the risks of further weakening led to an increase in the level of attention from Finmeccanica and the Group companies on new expected orders and the participation in new tenders where the reporting currency is the dollar. Under IASs/IFRSs, any hedging transaction would be recognised using hedge accounting in respect of orders that are deemed highly likely, not in respect of all the potential orders. The Group is currently considering possible hedges for highly-probable orders, perhaps even using non-IAS compliant instruments.

Therefore, the Finmeccanica Group does not have any financial transactions of a speculative nature, in the sense that none of its transactions add risk to that which is already implicit to its business. On the contrary, in compliance with the Group directive, all existing financial transactions have the specific objective of eliminating or minimizing exchange risks related to operations.

The *management of interest rate risk* is consistent with the long-standing practice of reducing the impact of fluctuations in interest rates while seeking to minimise related financial expense. To that end, at 31 March 2007 Finmeccanica had outstanding interest rate swaps for medium and long-term financing with highly rated financial counterparties totalling €mil. 830. Thanks to these transactions, it was possible to earn benefits from low costs of floating rates, especially in 2004-2005, with the debt structure mainly including fixed rates starting from 2006. This policy shields the company from possible increases in interest rates. At 31 March 2007, the total fair value of the interest rate derivatives portfolio came to a negative net balance of €mil. 18 as compared with the negative €mil. 14 of 31 December 2006. The transactions designated as a hedge had a positive change in

fair value for the period of €mil. 1 (from a negative €mil. 3 to a negative €mil. 2). At the same date, transactions not eligible for hedge accounting had a negative change in fair value for the period of €mil. 5 (from a negative €mil. 11 at 31 December 2006 to a negative €mil. 16).
The restrictive IFRS standards and related interpretations make it necessary to consider certain transactions as speculative even when they are essentially intended to contain finance costs mitigating the risk adding a percentage of variable interest to the composition of the debt.
During 2006, the European Central Bank has adopted an anti-inflationary stance, raising official rates by a total of 1.25%. This fostered market expectations for additional increases, which have already been partially discounted in current rates (6-month Euribor at 3.85% from 2.63% 12 months ago).

The *management of price risk on equity* concerns hedges with derivative instruments of the indirect investment held in STMicroelectronics NV (STM). At 31 March 2007 options were in place for an underlying position of 45 million of STM shares. These hedges are classified as trading operations, with changes in fair value recognized in the income statement. The recognition of the fair value through profit or loss of these instruments had no impact on income. However, the intrinsic value of the derivatives in being at the same date, i.e. the value calculated as it was the maturity date of the derivatives, was a positive €mil. 18.
The strategy implemented using put spreads and the sale of calls allows Finmeccanica to limit the negative impact of a partial depreciation of STM shares while leaving open the possibility of benefiting, within certain limits, from any appreciation in the shares and exposing the Company to potential costs/lost revenues in the event this limit is exceeded.
The equity investment is treated as an asset held for sale and therefore the change in value between the start and end of the period (from € 14,064 to € 14,43 per share) was a positive €mil. 22 and only had impact on the balance sheet.
It should also be noted that the management of derivatives on STM shares has permitted the Group to receive about €mil. 63 between 2004 and 2007, improving its portfolio position.

Under IFRS, the option sold to bondholders on exchangeable STM bonds with a maturity of August 2010 is accounted for separately from the underlying bonds. It should also be noted that, in 2005, Finmeccanica acquired a virtually identical option on the open market to hedge the option sold to bondholders thereby neutralising the effects while at the same time freeing up the 20 million underlying STM shares. At 31 March 2007, the change in the fair value of these options was €mil. 2, negative for one, positive for the other and therefore there was no net impact on the income statement.

Finally, with regard to the placement of 60% of the shares of Ansaldo STS on the stock market in April 2006, Finmeccanica make a commitment to grant, for no further compensation, to subscribers to retained possession of the shares for at least 12 months, one share for every 20 held in the case of the public-at-large and Finmeccanica shareholders, and one share for every 10 held for employees.

The final accrual date for which the right to receive the free shares was 28 March 2007. Subscribers must submit a request to receive the shares by 30 April 2007, else the right lapses. The grant shall be made within 30 days following 30 April 2007. The fair value of this commitment at 31 March 2007 was a cost of €mil. 1 (from €mil. 3 to €mil. 4). It is expected that Finmeccanica will purchase these shares directly on the open market.

XI. TRANSACTIONS WITH RELATED PARTIES

In general, commercial relations with related parties are carried out at arm’s length, as is settlement of the interest-bearing receivables and payables when not governed by specific contractual conditions. The following table summarises the situation:

(millions of euros) *Receivables at 31 March 2007*	**Non-current financial receivables**	**Other non-current receivables**	**Current financial receivables**	**Trade receivables**	**Other current receivables**	**Total**
Subsidiaries						
Ansaldo Invest Denmark A/S (in liq.)			3			3
Finmeccanica UK Ltd			3			3
Ansaldo Argentina S.A.				1	1	2
Finmeccanica Inc.			1			1
Alifana Due S.c.r.l.				1		1
IGS S.p.A. (in liq.)			1			1
Alenia Improvement S.p.A.				1		1
Ansaldo Electric Drives S.p.A.			1			1
Oto Melara North America Inc.			1			1
Other companies with unit amount of less than €mil. 1				1		1
Associates						
Eurofighter Jagdflugzeug GmbH				86		86
Iveco Fiat/Oto Melara S.c.a.r.l.				60		60
NH Industries S.a.r.l.				15		15
Galileo Vacuum Systems S.p.A.			12	1		13
Ansaldo Trasmissione e Distribuzione S.p.A.	5		6	1		12
Eurosysnav S.A.S.				11		11
Orizzonte - Sistemi Navali S.p.A.				9		9
Euromids S.A.S.				6		6
Macchi Hurel Dubois S.A.S.				5		5
Elettronica S.p.A.				5		5
Nahuelsat S.A.	2			1		3
Remington Elsag Law Enforcement Systems LLC				3		3
I.M. Intermetro S.p.A.				3		3
Nicco Communications S.A.S.				2		2
Metro 5 S.p.A.				2		2
Consorzio Start S.p.A.				2		2
Advanced Air Traffic Systems Sdn Bhd				2		2
Contact S.r.l.				1		1
Industrie Aeronautiche Rinaldo Piaggio S.p.A. (Amm. Str.)				1		1
Eurofighter Simulation Systems GmbH				1		1
Comlenia Sendirian Berhard				1		1
Thomassen Service Gulf LLC				1		1
Joint ventures (*)						
MBDA S.A.S.				53		53
GIE ATR					43	43
Alcatel Alenia Space S.A.S.			1	24		25
Aviation Training International Ltd	11		1			12
Telespazio S.p.A.				2	1	3
Consortiums (**)						
Trevi - Treno Veloce Italiano				21		21
Saturno				20		20
C.I.S. DEG				6		6
Filobus Vesuvio				3		3
Thamus			3			3
Telaer				2		2
CREO - Centro Ricerche Elettroniche			2			2
SESM - Soluzioni Evolute per la Sistemistica e i Modelli			2			2
Ferroviario Vesuviano				2		2
CMS Italia				1		1
Sistemi Navali Selenia-Elsag				1		1
Total	**18**	**-**	**37**	**358**	**45**	**458**

(millions of euros) ***PAYABLES AT 31 March 2007***	**Non-current borrowings**	**Other non-current payables**	**Current borrowings**	**Trade payables**	**Other current payables**	**Total**
Subsidiaries						
Alifana Due S.c.r.l.				4		
Finmeccanica UK Ltd				3		
Finmeccanica Inc.				1		
Selex Sensors and Airborne Systems Electro Optics (overseas) Ltd				1		
Associates						
Eurosysnav S.A.S.			20			2
Ansaldo Trasmissione & Distribuzione S.p.A.			10		1	1
Iveco Fiat/Oto Melara S.c.a.r.l.					6	
Metro 5 S.p.A.					5	
Pegaso S.c.r.l.				4		
Eurofighter Jagdflugzeug GmbH				3		
Advanced Air Traffic Systems Sdn Bhd				3		
Elsag Gest S.p.A.				2		
Libyan Italian Advanced Technology Company			1			
Bell Agusta Aerospace Company LLC				1		
Sistemi Dinamici S.p.A.				1		
Eurofighter International Ltd			1			
Other companies with unit amount of less than €mil. 1				1		
Joint ventures (*)						
MBDA S.A.S.			347	13		36
Telespazio S.p.A.			25	1		2
GIE ATR				4		
Alcatel Alenia Space S.A.S.				4		
Other companies with unit amount of less than €mil. 1					1	
Consortiums (**)						
SESM - Soluzioni Evolute per la Sistemistica e i Modelli				1		
CMS Italia				1		
Sistemi Navali Selenia-Elsag			1			
Telaer				1		
Thamus				1		
Other consortiums with unit amount of less than €mil. 1				2		
Total	**-**	**-**	**405**	**52**	**13**	**47**

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

(millions of euros) ***RECEIVABLES AT 31 December 2006***	**Non-current financial receivables**	**Other non-current receivables**	**Current financial receivables**	**Trade receivables**	**Other current receivables**	**Total**
Subsidiaries						
Ansaldo Invest Denmark A/S (in liq.)			3			3
Alifana Due S.c.r.l.				3		3
Finmeccanica UK Ltd			2			2
Ansaldo Argentina S.A.				1		1
Finmeccanica Inc.			1			1
IGS S.p.A. (in liq.)			1			1
Alenia Improvement S.p.A.				1		1
Ansaldo Do Brasil Equipamentos Eletromecanicos Ltda					1	1
Ansaldo Electric Drives S.p.A.			1			1
Other companies with unit amount of less than €mil. 1				1		1
Associates						
Eurofighter Jagdflugzeug GmbH				79		79
Iveco Fiat/Oto Melara S.c.a.r.l.				58		58
NH Industries S.a.r.l.				14		14
Eurosysnav S.A.S.				11		11
Galileo Vacuum Systems S.p.A.			9	1		10
Orizzonte - Sistemi Navali S.p.A.				9		9
Macchi Hurel Dubois S.A.S.				8		8
Ansaldo Trasmissione e Distribuzione S.p.A.	5			1		6
Elettronica S.p.A.				5		5
Remington Elsag Law Enforcement Systems LLC				4		4
Euromids S.A.S.				4		4
I.M. Intermetro S.p.A.				3		3
Consorzio Start S.p.A.				2		2
Eurofighter Simulation Systems GmbH				2		2
Comlenia Sendirian Berhard				2		2
Nicco Communications S.A.S.				1		1
Eurofighter Aircraft Management GmbH				1		1
Advanced Air Traffic Systems Sdn Bhd				1		1
Industrie Aeronautiche Rinaldo Piaggio S.p.A. (Amm. Str.)				1		1
Thomassen Service Gulf LLC				1		1
Other companies with unit amount of less than €mil. 1				2		2
Joint ventures (*)						
Gie - ATR					33	33
MBDA S.A.S.				45		45
Alcatel Alenia Space S.A.S.			2	23		25
Aviation Training International Ltd	11		1			12
Telespazio S.p.A.				1	1	2
Consortiums (**)						
Saturno				35		35
Trevi - Treno Veloce Italiano				24		24
CMS Italia				14		14
C.I.S. DEG				6		6
Filobus Vesuvio				3		3
Telaer				2		2
CREO - Centro Ricerche Elettroniche			2			2
Thamus			2			2
S3Log				2		2
SESM - Soluzioni Evolute per la Sistemistica e i Modelli			2			2
Ferroviario Vesuviano				2		2
Ferroviario S. Giorgio Volla				2		2
Contact				1		1
Sistemi Navali Selenia-Elsag				1		1
Total	**16**	**-**	**26**	**377**	**35**	**454**

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

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

(millions of euros) 31 March 2007	**Revenues**	**Other operating revenues**	**Costs**	**Financial income**	**Financial expense**
Subsidiaries					
Alifana Due S.c.r.l.			3		
Elsag Gest S.p.A.			1		
Finmeccanica UK Ltd			1		
Finmeccanica Inc.			1		
Associates					
Eurofighter Jagdflugzeug GmbH	68				
Iveco Fiat/Oto Melara S.c.a.r.l.	23		1		1
Macchi Hurel Dubois S.A.S.	5				
Euromids S.A.S.	4				
Eurofighter Simulation Systems GmbH	4				
Orizzonte Sistemi Navali S.p.A.	1				
Eurosysnav S.A.S.	1				
N.H. Industries S.a.r.l.	1				
Elsag Gest S.p.A.			1		
Nicco Communications S.A.S.	1				
Elettronica S.p.A.	1				
Pegaso S.c.r.l			1		
Consorzio START S.p.A.			1		
Thomassen Service Gulf LLC	1				
Other companies with unit amount of less than €mil. 1	1			1	
Joint ventures (*)					
GIE ATR	20				
MBDA S.A.S.	11				3
Alcatel Alenia Space S.A.S.	8		1		
Telespazio S.p.A.	1				
Consortiums (**)					
Consorzio Saturno	12				
CMS Italia	1				
C.I.S. DEG	1				
Total	**165**	**-**	**11**	**1**	**4**

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

(millions of euros) 31 March 2006	**Revenues**	**Other operating revenues**	**Costs**	**Financial income**	**Financial expense**
Subsidiaries					
Finmeccanica UK Ltd			1		
Associates					
Eurofighter Jagdflugzeug GmbH	66				
Iveco Fiat/Oto Melara S.c.a.r.l.	23				1
Eurosysnav S.A.S.	19				
Eurofighter Simulation Systems GmbH	9				
Euromids S.A.S.	4				
N.H. Industries S.a.r.l.	3				
Nicco Communications S.A.S.	1				
Other companies with unit amount of less than €mil. 1					
Joint ventures (*)					
MBDA S.A.S.	13				2
GIE ATR	11				
Alcatel Alenia Space S.A.S.	3				
Telespazio S.p.A.			1		
Consortiums (**)					
CMS Italia	1		13		
C.I.S. DEG	1				
OPTEL	1				
TREVI	1		1		
Other consortiums with unit amount of less than €mil. 1	1				
Total	**157**	**-**	**16**	**-**	**3**

(*)Amounts refer to the portion not eliminated in consolidation

(**)Consortiums over which the Group exercises considerable influence or which are subject to joint control

4. Performance by division

HELICOPTERS

€ millions	31 March 2007	31 March 2006	31 December 2006
New orders	712	1,836	4,088
Order backlog	8,496	8,536	8,572
Revenues	720	578	2,727
EBIT	75	44	290
R.O.S.	10.4%	7.6%	10.6%
Working capital	427	426	392
Net invested capital	2,117	2,131	2,085
R.O.I (*)	14.2%	8.3%	13.9%
Research and development	71	97	356
Employees (no.)	8,999	8,599	8,899

(*) calculated on invested capital at period-end

Finmeccanica is, together with AgustaWestland NV and its subsidiaries, a leader in the extremely restricted circle of systems designers in the world helicopter industry with EADS (Eurocopter) and United Technologies (Sikorsky).

The quarter saw a number of particularly significant commercial developments in the military segment, including:

- the announcement by the executive committee of the Turkish government that negotiations have begun with AgustaWestland, in partnership with Turkish Aviation Industry (TAI), regarding the ATAK (Tactical Reconnaissance and Attack Helicopter) programme for the leadership of Turkish ground forces. The estimated value of this programme, based on a request for 51 A129 helicopters, is

in excess of €mil. 1,200. The AgustaWestland proposal contains significant industrial benefits for Turkey, as may important local aerospace firms will be involved in the programme. Final assembly, delivery and acceptance will also take place in Turkey.

- the announcement of an important Memorandum of Understanding between AgustaWestland and the *rotorcraft* division of Boeing Integrated Defense System regarding the preparation of the bid that will commit the two manufacturers to supply CH-47F helicopters to replace the current Chinook helicopter fleet used by the Italian Army. In addition, the parties agreed that should further of these helicopters be sold in Italy and in the UK, AgustaWestland will act as prime contractor while Boeing will take on the role of primary supplier.
- The agreement with the UK Ministry of Defence to upgrade EH 101 Merlin helicopters, which will be acquired from the fleet of EH 101 in service with the Royal Danish Air Force. The agreement also includes the purchase of a further 6 new EH 101 Merlin helicopters that will be delivered by the UK Ministry of Defence to the Royal Danish Air Force to replace the original helicopters. The contract is expected to be carried out in the second quarter of 2007.

In the civil and government sector, too, AgustaWestland demonstrated excellent performance given its ability to penetrate markets where the competition is increasingly selective thanks to the availability of a modern, competitive product portfolio. In the first quarter of 2007, it recorded orders for 92 helicopters worth €mil. 511. Of note in that regard are the following:

- orders for an additional 28 AW139 helicopters, totalling €mil. 266, including the provision of 14 helicopters to Saudi Arabian Oil Company; The portfolio of orders for the AW139 continues to grow, with over 150 helicopters currently on order.

Within the commercial segment, orders were also obtained for a further 64 helicopters, of which 30 A109 Grand (5 of which were purchased by Sloane Helicopters), 12 A109 Power and 22 A119 helicopters, for a total of €mil. 218. With regard to the A119

helicopters, contracts were concluded with the Spanish aeronautics group FAASA for 6 helicopters and with the Libyan Red Crescent for 5 helicopters.

Total volume of **new orders** at 31 March 2007 came to €mil. 712 a decline from the same period of 2006 (€mil.1,836) when two important orders were received from the UK Ministry of Defence worth a total of about €mil. 1,200.

As a result of the volume of new orders for the first quarter, the value of the **order backlog** at 31 March 2007 came to €mil. 8,496, in line with the figure at 31 December 2006 (€mil. 8,572).
The orders at 31 March 2007 can be broken down into 69% for helicopters, 27% for support activities and 4% for engineering. The order backlog guarantees coverage of over 3 years of production.

Revenues at 31 March 2007 amounted to €mil. 720, with an increase of 25% over 31 March 2006 (€mil. 578). This improvement is attributable to greater volumes in the commercial sector (A109, AW139, A119) (43%), to the start of production on the VH 71 contract for the President of the United States (30%) and support activities (27%) primarily related to the integrated support contracts (IOS) with the UK Ministry of Defence.

The quarter saw deliveries for a total of 32 helicopters compared with 28 delivered during the same period of last year.

EBIT at 31 March 2007, in the amount of €mil. 75, increased by €mil. 31, 70% over the same period of the previous year (€mil. 44).
This significant improvement is due, in part, to the aforementioned growth in volumes, as well as to the effect of efficiency enhancement actions undertaken last year as part of the process of integrating British and Italian activities.

As a result, **ROS** came to 10.4% up by 3 percentage points from 31 March 2006 (7.6%) and in line with the figure at 31 December 2006 (10.6%).

Net invested capital reached €mil. 2,117 at 31 March 2007 from €mil. 2,085 at 31 December 2006, an increase of €mil. 32 due to the rise in current assets as a result of the expansion of production volumes noted earlier; this is reflected in the figure for **working capital,** which came to €mil. 427 at 31 March 2007, from €mil. 392 at 31 December 2006.
Return on investment (**ROI**) reached 14.2% at 31 March 2007, increasing both over the figure at 31 March 2006 (8.3%) and that at 31 December 2006, owing primarily to the increase in EBIT.

Research and development expenditure at 31 March 2007, amounting to €mil. 71 (€mil. 97 at 31 March 2006), primarily concerned:

- research as part of programmes financed through Law 808/85, which include the development of technologies for a new helicopter of the 6/7-tonne class named the A149 and development of multi-role versions of BA 609 convertiplane for national security;
- research into upgrading products, where activities continued on the customisation of the AW139 and Agusta Grand helicopters;
- research and development into variants of base models in connection with government/military and civil contracts.

The AgustaWestland had 8,999 employees at 31 March 2007, up by 100 employees over 31 December 2006 (8,899). This rise was necessary in order to meet the technical/production needs related to the increase in business volumes.

DEFENCE ELECTRONICS

€ millions	31 March 2007	31 March 2006	31 December 2006
New orders	502	629	4,197
Order backlog	7,418	7,530	7,676
Revenues	680	708	3,747
EBIT	6	42	300
R.O.S.	0.9%	5.9%	8.0%
Working capital	1,061	998	734
Net invested capital	3,187	2,378	2,778
R.O.I. (*)	0.8%	7.1%	10.8%
Research and development	127	117	541
Employees (no.)	19,074	19,660	19,185

(*) calculated on invested capital at period-end

The division includes activities concerning the manufacture of avionics equipment and systems, unmanned aircraft, radar systems, land and naval command and control systems, air traffic control systems, integrated communications systems and networks for land, naval, satellite and avionic applications, and private mobile radio communications systems and IT and security activities.

In addition to the production of electronic equipment and systems for defence and security, the division also continued its intensive efforts concerning the provision of large-scale integrated systems based on complex architectures and network-centric approaches.

The goal is to meet the increasingly pressing needs of customers to possess large-scale systems that integrate a variety of functions, platforms and sets of sensors in order to

ensure effective performance in the surveillance, control, and protection of critical areas and infrastructures.

To that end, Selex Sistemi Integrati has begun numerous sales campaigns, particularly in export markets, in order to promote large-scale homeland protections systems, especially for applications related to border control and security management in conjunction with major events. This effort leverages all of the skills of the various group companies and takes advantage of the consolidated presence of a number of these companies in the various countries concerned.

At 31 March 2007, **new orders** totalled €mil. 502, a 20% decrease from the first quarter of 2006, primarily due to lower orders for command and control systems. The main new orders during the period include the following:

- Avionics: various orders for systems for countermeasure, additional orders for the EFA programme as well as orders for devices for space programmes;
- Land and naval command and control systems: orders of air-traffic control and management abroad and logistics;
- Integrated communications systems and networks: additional orders for communication systems of the EFA and for activities within the scope of the European programme to supply MIDS (Multifunctional Information Distribution System) interface units, as well as various orders for military communications and security systems by Romania;
- Information technology and security: signing of the framework agreement resulting from the tender held by CNIPA (National Centre for IT in the Government) for the creation and management of website services, awarded to the joint venture by Datamat, Elsag, Telecom Italia and Engineering Italia;

In addition, Selex Sistemi Integrati competed the acquisition of an order (worth over €mil. 250) to extend the homeland security system used by the Algerian National Police Force. This project, which also involves Selex Communications and Elsag as co-suppliers, is being developed within the context of the range of large-scale integrated systems based on complex architectures. The system is comprised of an network of

sensors integrated into a communications infrastructures and managed through a set of command and control centres.

The **orders backlog**, net of work in progress, came to €mil. 7,418 compared with €mil. 7,676 at 31 December 2006, a decrease of €mil. 258 is due essentially to ordinary acquisition and order volumes and client billing. The composition of the backlog is attributable for 50% to the avionics segment, while radar and command and control systems and the communications field both contribute about 20% each, with information technology comprising about 10%.

Revenues came to €mil. 680 at 31 March 2007, a decrease by 4% or €mil. 28 in absolute terms. Specifically:

- avionics: the continuation of activities relating to DASS production and the production of avionics equipment and radar for the EFA programme, as well as systems for countermeasures;
- radar and command and control systems: the continuation of activities relating to contracts with the Italian Navy, to international cooperation contracts, as well as air traffic control programmes both in Italy and abroad;
- integrated communications systems and networks: activities relating to the development and manufacture of equipment for EFA and the provision of communication systems for the military;
- IT and security: activities relating to security, automation, IT, and defence systems and services.

EBIT at 31 March 2007 came to €mil. 6, a decrease of €mil. 36 over the same figure posted for the first quarter in 2006. This decline is the result of lower volumes and a contingent situation involving a mix of less profitable activities than in the past relating to command and control systems and information technology. The result in the first quarter of 2006 also benefited from the gains from the sale of property by Selex Communications Ltd.

ROS at 31 March 2007 came to 0.9%, down from the 5.9% recorded at 31 March 2006.

Net invested capital at 31 March 2007 came to €mil. 3,187, up €mil. 409 compared with 31 December 2006 (€mil. 2,778) mainly owning to an increase in **working capital** (up €mil. 327 over the figure posted at the end of 2006), which reflects higher payments to suppliers than trade collections in the first quarter of the year.

Research and development costs at 31 March 2007 came to €mil. 127, as compared with €mil. 117 at 31 March 2006, and include in particular the continuation of development for the EFA programme and radar for surveillance systems, the fine-tuning of the Falco UAV system, the development of naval and land-based command and control systems, the completion of development of radar systems for air traffic control, and the completion of the TETRA network.

At 31 March 2007, there were 19,074 employees, a decrease of 111 employees from 31 December 2006, mainly related to the rationalisation of the Italian portion of the avionics segment.

AERONAUTICS

€ millions	31 March 2007	31 March 2006	31 December 2006
New orders	667	431	2.634
Order backlog	7,866	6,935	7,538
Revenues	412	408	1,908
EBIT	20	15	203
R.O.S.	4.9%	3.7%	10.6%
Working capital	(776)	(417)	(1,034)
Net invested capital	232	154	(249)
R.O.I. (*)	n.s.	n.s.	n.s.
Research and development	122	103	486
Employees (no.)	12,687	11,364	12,135

(*) calculated on invested capital at period-end

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

The Aeronautics division includes Alenia Aeronautica S.p.A. (production of military aircraft for combat, transport and special missions, as well as civil applications such as aerostructures and regional turboprop aircraft) and its subsidiaries, including: Alenia Aermacchi S.p.A. (production of military training aircraft and engine nacelles for civil aeronautics), Alenia Aeronavali S.p.A. (aircraft conversions and maintenance), and the GIE-ATR consortium, in which a 50% equity stake is held (marketing and assembly of ATR aircraft).

During the first three months of 2007 the principal activities in the military division were as follows:

- Alenia Aeronautica: continuation of EFA development, production and logistics; production of the C27J aircraft, particularly production for the Italian air force, to which the first aircraft was delivered in January 2007, and for Greence, Lithuania and Bulgaria; the continuation of upgrades to the Tornado aircraft and the modernisation of avionics (ACOL) of the AMX; design and planning activities for the JSF aircraft commissioned by Lockheed Martin; production and logistics for ATR 42 MP crafts for the Italian *Guardia di Finanza* and harbour office; and new testing for the UAV prototype;
- Alenia Aermacchi: the production and logistical support for the MB339 and SF260 training aircraft, further development of the new M346 training aircraft;
- Alenia Aeronavali: development and production for the B767 tanker programme; the overhaul and logistical support for the B707 Tanker, AWACS and return to airworthiness of the G222 aircraft.

The civil activities of Alenia Aeronautica mainly involved the following:

- Boeing: production of components for fuselages and control surfaces for the B767 and B777 aircraft. Development and sales activities continued for the new B787, the manufacturing of which started at the end of 2006 in the new facilities at Grottaglie (central sections of the fuselage) and Foggia (horizontal tail wings). On 22 March 2007, the first two sections of the fuselage (central and central-back sections) of the B787 were delivered and transported to the South Carolina (USA) facilities of Global Aeronautica LLC (a joint venture between Alenia North America Inc and Vought Aircraft Industries Inc.) to be assembled with the other sections of the fuselage manufactured.
- Airbus: the design of components for the central section of the fuselage of the A380, of the tail cone AND mechanical wing components for the A340, and of a fuselage section for the A321;
- GIE ATR, in partnership with EADS-ATR: the production of the ATR 42 and 72 turboprops;
- Dassault Aviation: the fuselage section of the Falcon 2000 Extended Range and the engine nacelles for the Falcon 900EX.

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

New orders at 31 March 2007 came to €mil. 667, with an increase by €mil. 236 from the €mil. 431 of 31 March 2006. The main orders received during the first quarter of 2007 were the following:

- the military segment: the EFA Future Enhancements order to further develop the weapons system to improve the performance and operational capacity of the craft;
- the civil segment: orders for the GIE-ATR consortium, which received orders for 24 aircraft (of which 11 from Spanish airlines, 6 from the Philippine company Cebu Air and 3 from the Indian Jet Airways) and the additional lots for the B767, A321, Falcon programmes, engine nacelles, and the transformation of MD11 aircraft.

The **order backlog** at the end of March 2007 came to €mil. 7,866 made up principally of the following programmes: EFA (46%), B787 (21%), C27J (4%) AMX (3%). The backlog grew by €mil. 328 compared to end of 2006 (€mil. 7,538), and is expected to continue expanding over the medium/long term.

Revenues at 31 March 2007 totalled €mil. 412, broadly in line with the figure of €mil. 408 recorded in the same period of the previous year. The decline in military production, mainly due to numerous delays in providing equipment, was offset by a rise in civil activities. This growth, which had been predicted, was largely due to the increase in deliveries and production of the ATR craft, the production of the B787 (begun at the end of 2006) and the A321.

EBIT at 31 March 2007 came to €mil. 20, an increase of €mil. 5 over the €mil. 15 posted for the first three months of the previous year. The improvement both in absolute terms and average profitability (ROS of 4.9% as compared to 3.7% at 31 March 2006) is attributable to Alenia Aeronautica that was offset by the worsening of Alenia Aeronavali

S.p.A. for which a plan for reorganisation and efficiency improvements was launched at the end of 2006.

Working capital at 31 March 2007 came to a negative €mil. 776, up €mil. 258 compared with 31 December 2006 (a negative €mil. 1,034). The growth, which was physiological in the first quarter, is mainly due to the increase in net inventories, which were affected by a number of delays in invoicing and higher advances to suppliers, and to decreased trade payables.

Net invested capital at 31 March 2007 came to €mil. 232, an increase of €mil. 481 over the negative €mil. 249 at 31 December 2006, due to the developments in working capital, as noted above, and the increase in capital assets as a result of larger investments, particularly plant and equipment for B787 production and non-recurrent activities conducted during the period concerning programmes being developed.

Research and development costs for the first three months of 2007 came to €mil. 122, up from the €mil. 103 of the same period of 2006. This results reflects the significant commitment to activities of programmes such as B787, C27J, M346, second tranche EFA activities, Tornado, AMX, Unmanned Air Vehicles (UAVs), A380, engine nacelles, and B767 tankers.

The **number of employees** at 31 March 2007 stood at 12,687, representing an increase of 552 over the 12,135 employees at 31 December 2006. This increase was mainly due to new hires by Alenia Aeronautica in order to meet the needs of higher workloads, and by Alenia Composite with regard to rising production of the B787 at the Grottaglie facility.

SPACE

millions €	31 March 2007	31 March 2006	31 December 2006
New orders	121	218	851
Order backlog	1,251	1,237	1,264
Revenues	166	140	764
EBIT	1	9	44
R.O.S.	0.6%	6.4%	5.8%
Working capital	(20)	20	(66)
Net invested capital	364	342	318
R.O.I. (*)	1.1%	10.5%	13.8%
Research and development	11	9	64
Employees (no.)	3,252	3,214	3,221

(*) calculated on invested capital at period-end

Note that all figures refer to the two joint ventures (Thales Alenia Space S.A.S. and Telespazio Holding S.r.l) consolidated on a proportionate basis at 33% and 67% respectively.

New space alliance between Finmeccanica and Thales: on 4 April 2007 the European Commission approved the transfer by Alcatel-Lucent to Thales of stakes in the Alcatel Alenia Space joint venture (renamed Thales Alenia Space, with Finmeccanica S.p.A. holding 33% and Thales 67%) and in Telespazio (Finmeccanica with 67% and Thales with 33%). Thus, with the final approval by the competent authorities, ended the second phase of the collaboration agreement between Thales and Alcatel-Lucent announced on 5 April 2006, which led to the creation of the new space alliance between Finmeccanica and Thales.

Finmeccanica operates in the space industry through Telespazio Holding S.r.l. (satellite services), which is based in Italy and has its main industrial facilities in Italy, France and Germany and in which Finmeccanica holds a 67% stake, as well as through Alcatel

Alenia Space S.A.S. (manufacturing), which is based in France and has its main industrial facilities in France, Italy, Belgium and Spain and in which Finmeccanica holds a 33% stake.
More specifically, Telespazio Holding focuses on defence and security services, satellite navigation and earth observation, the provision of telecommunications networks and services, the management and orbital control of satellites and of terrestrial centres, and multimedia and high value applications.
Thales Alenia Space S.A.S. focuses on the design, development and production of space systems, satellites, orbital infrastructures, space transport systems, equipment, instruments, and terrestrial systems for civil and military applications.

From a commercial perspective, during the first three months of 2007 **new orders** came to €mil. 121, down €mil. 97 from the same period in 2006 (€mil. 218), thanks above all to delays in the receipt of significant new orders in the commercial and institutional telecommunications satellites market. The most significant new orders for the period were:

- in the commercial segment: the second lot in the provision of 48 low-earth orbit (LEO) satellites for the Globalstar second-generation constellation; the renewal of the multi-year contracts for TV services, particularly for Sky; and new orders for the provision of telecommunications satellite services;
- in the institutional segment: new orders for satellite orbit management, especially for the Artemis satellite by ESA, and terrestrial centre management;
- in the military segment: the first lot of the order for the Armasat programme;
- in the earth observation segment: the contracts related to the Cosmo programme for the launch of the fourth satellite; the first lot for the GMES programme for territorial control and security; new orders for the provision of monitoring and territorial management services;
- in the navigation and infomobility segment: additional orders related to the Galileo (the in-orbit validation phase) and EGNOS programmes;

- in the science programmes segment: the additional lot related to the Herschel/Plank and Bepi-Colombo programmes and new orders in the on-board equipment and transport infrastructures sector.

The **order backlog** at 31 March 2007 came to €mil. 1,251, a decrease of €mil. 13 over the same figure at 31 December 2006 (€mil. 1,264). The order backlog, based on the amount of work ready to begin, guarantees coverage of approximately 82% of the expected production for the next nine months. The backlog at 31 March 2007 breaks down into manufacturing activities for 63% (50% satellites and *payload*, 13% infrastructure and equipment) and satellite services for the remaining 37%.

Revenues for the first three months of 2007 came to €mil. 166, up €mil. 26 from the same period in 2006 (€mil. 140) due to higher production levels in the manufacturing segment. The principle sources of production revenues were:

- project activities related to the Turksat 3A, Ciel 2, BW Satcom, as well as the satellites of the Globalstar constellation, and phase 1 of the third-generation Meteosat programme;
- the continuation of activities relating to:
  - earth observation programmes, in particular the Cosmo-SkyMed and Pleiades HR programmes;
  - commercial satellites, including the StarOne C1/C2, AMOS 3, Thaicom 5, Chinasat 6B, Galaxy 17 and Rascom satellites;
  - the Syracuse III and Sicral 1B military telecommunications satellites;
  - the Herschel/Plank, Alma and Goce science programmes;
  - the Galileo and EGNOS navigation programmes;
- the continuation of the programmes connected with the International Space Station;
- the development of equipment and devices, in particular for the Koreasat 5 satellite, and the payloads for the Arabsat 4A/4B/4R, Express AM33/34 and AMC21 satellites, and Kompsat radar;

- the provision of telecommunications satellite services, and, in the television sector, the resale of satellite capacity and provision of value-added broadcasting services using the digital platform;
- the provision of earth observation services and products, orbital satellite management, and terrestrial infrastructure management.

EBIT at 31 March 2007 came to €mil. 1, down €mil. 8 from the figure at 31 March 2006 (€mil. 9) mainly due, in France, to higher costs for specific programmes and to a greater incidence of labour costs.
As a result, **ROS** fell sharply from 6.4% in the first quarter of 2006 to 0.6% at 31 March 2007.

Net invested capital at 31 March 2007 came to €mil. 364, an increase of €mil. 46 over 31 December 2006, primarily attributable to **working capital** (a negative €mil. 20 at 31 March 2007) posting an increase for the first three months of the year of €mil. 46 over 31 December 2006 (a negative €mil. 66) due primarily to growth in net inventories and trade receivables related to lower receipts on trade receivables and the reduction in trade payables.

Research and development costs for the first three months of 2007 came to €mil. 11, up about €mil. 2 from the same period in 2006 (€mil. 9). Key activities in this area included:
- research and development phases for programmes such as:
  - Syracuse 3 and Sicral 1B programmes (SAR radar, altimeter e radiometer);
  - dual-use civil and military navigation systems (Cosmo);
  - science programmes (Alma, Spirale/Melissa, Bepi-Colombo, Goce, and Herschel/Plank);
- development of:
  - platforms and solutions for advanced telecommunications, satellite navigation /infomobility (Galileo);
  - GIS platforms (Geodatabase);
  - platforms for LEO applications;

- the development of production technology for mobile and/or broadband applications in particular,
- architectures and technologies for radar and optical instrumentation;

- studies relating to:
  - future experiments on board the International Space Station;
  - capsules, orbital infrastructure and manned re-entry craft.

The **number of employees** at 31 March 2007 came to 3,252, with an increase of 31 employees over the 3,221 at 31 December 2006 due to higher expected production in the manufacturing segment and the development of satellite services abroad.

DEFENCE SYSTEMS

€ millions	31 March 2007	31 March 2006	31 December 2006
New orders	132	89	1,111
Order backlog	4,133	3,731	4,252
Revenues	238	214	1,127
EBIT	1	7	91
R.O.S.	0.4%	3.3%	8.1%
Working capital	(302)	(245)	(374)
Net invested capital	159	237	104
R.O.I. (*)	2.5%	11.8%	n.s.
Research and development	54	40	279
Employees (no.)	4,213	4,334	4,275

(*) calculated on invested capital at period-end

Note that the figures relating to the MBDA joint venture are consolidated on a proportionate basis at 25%.

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

New orders for the first three months of 2007 came to €mil. 132, an increase over the figure of the same period in 2006 (€mil. 89) mainly due to a higher volume of orders in the missiles segment. The increase in orders during the first quarter of 2007 is primarily attributable to:

- in missile systems: orders to upgrade the batteries of Aspide anti-air defence missiles, for activities relating to Patriot systems and for the provision of Mistral anti-air defence missiles;
- in the land, sea, and air weapons systems: orders for four 76/62 SR cannons and for machine guns from Malaysia and numerous logistics orders;
- in the underwater systems: orders for FREMM logistics activities and for export.

The **order backlog** at 31 March 2007 came to €mil. 4,133, 70% of which related to missile systems, for a decrease of €mil. 119 over 31 December 2006 (€mil. 4.252).

Revenues at 31 March 2007 came to €mil. 238, with an 11% increase over the first three months of 2006 attributable to the missile systems and, in particular the consolidation of German activities (consolidated since 1 March 2006).

Revenues benefited from the following activities:

- activities relating to the production of Storm Shadow air-to-surface missile systems and SCALP EG; the production of MICA air-to-air missiles as well as customer support activities;
- land, naval and aeronautical weapons systems: the provision of PZH 2000 howitzers to the Italian Army; and the production of Hitfist turrets kits for Poland and Hitfist turrets for Ireland;
- underwater systems: activities relating to the new Black Shark heavy torpedo and the production of MU90 and A244 light torpedoes; activities related to logistics.

EBIT at 31 March 2007 came to €mil. 1, a decrease from the first quarter of 2006 primarily due to higher costs associated to the restructuring plan for the missile segment.

ROS at 31 March 2007 was 3 percentage points lower than that of the same period in 2006.

Working capital came to a negative €mil. 302 at 31 March 2007 due principally to advances from MBDA customers, an increase of €mil. 72 over 31 December 2006, consistent with the performance in the first quarter which featured a delay in payments to suppliers and receipts on trade receivables. **Net invested capital** at 31 March 2007 came to €mil. 159 (from €mil. 104 at 31 December 2006).

Research and development spending for the first three months of 2007 came to €mil. 54, a 35% increase over the same period in 2006. Some of the key activities included the continuation of development of the Meteor air-to-air missile, guided munitions in the land naval and aeronautical weapons segment, the Black Shark heavy torpedo and the A244 light torpedo in the underwater systems segment.

The **number of employees** at 31 March 2007 came to 4,213, a decrease of 62 from 31 December 2006 mainly due to continuation of restructuring activities in the missile segment.

ENERGY

€ millions	31 March 2007	31 March 2006	31 December 2006
New orders	145	576	1,050
Order backlog	2,396	2,709	2,468
Revenues	218	201	978
EBIT	11	7	63
R.O.S.	5.0%	3.5%	6.4%
Working capital	(239)	(275)	(282)
Net invested capital	(209)	(274)	(254)
R.O.I. (*)	n.s.	n.s.	n.s.
Research and development	3	3	17
Employees (no.)	2,864	2,525	2,856

(*) Calculated on invested capital at period-end

In light of the acquisitions carried out in 2006, the energy sector is comprised of Ansaldo Energia S.p.A. and its subsidiaries: Ansaldo Nucleare S.p.A., Ansaldo Ricerche S.p.A., Sagem S.r.l., Asia Power Project Private Ltd, Energy Service Group GmbH, Thomassen Turbine Systems BV.

In the first quarter of 2007 **new orders** came to €mil. 145, down from the result of the same period in 2006, due to the failure to acquire turnkey facilities. The main new orders for components include the provision of a gas turbine and related alternator for the Algeciras plant (lotto 2) and Vlore plant, respectively; the service segment recorded significant new orders in the renewable sources sector, relating to the restoration of four hydroelectric assemblies, two hydroelectric generators and a hydroelectric plant. These types of acquisitions show the current market situation resulting from increasing focus on alternative energy sources. Finally, again with regard to service, at the end of the first quarter of 2007, there was a €mil. 19 increase in foreign flow agreements, compared with

the same period of 2006, strengthening Ansaldo Energia's international presence as an independent service provider.

The **order backlog** at 31 March 2007 came to €mil. 2,396, as compared to €mil. 2,468 at 31 December 2006.

Revenues came to €mil. 218 at 31 March 2007, an 8% improvement over the same period of the previous year (€mil. 201). This increase is due mainly to new systems orders for Algeciras and Amman East. During the first quarter, key contracts included those relating to the 800MW combined-cycle plants for Sparanise, Rosignano and Rizziconi.

EBIT at 31 March 2007 came to €mil. 11, an increase over the figure of €mil. 7 for the same period of the previous year, due to the afore-mentioned increase in production volumes.
ROS came to 5.0%, an improvement of 1.5 percentage points over the first quarter of 2006.

Working capital came to a negative €mil. 239 at 31 March 2007, down from December 2006 (€mil. 282) due mainly to failure to collect advances from customers relating to the systems orders that characterised the first quarter of 2006. As a result, **net invested capital** deteriorated, coming to a negative €mil. 209, compared to a negative €mil. 254 at 31 December 2006.

Research and development costs (entirely expensed) came to €mil. 3 and are in line with the result for the same period of the previous year; were related primarily to the continuation of the activities called for by the plan for technological independence.

The **number of employees** at 31 March 2007 came to 2,864, as compared with 2,856 at 31 December 2006, due to normal turnover.

TRANSPORTATION

€ millions	31 March 2007	31 March 2006	31 December 2006
New orders	170	484	2,127
Order backlog	4,540	4,090	4,703
Revenues	330	340	1,368
EBIT	9	16	15
R.O.S.	2.7%	4.7%	1.1%
Working capital	116	165	61
Net invested capital	362	379	312
R.O.I. (*)	9.9%	16.9%	4.8%
Research and development	14	10	40
Employees (no.)	6,784	6,409	6,677

(*)Calculated on invested capital at period-end

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

At 31 March 2007, the three business divisions showed the following performance::

- Signalling: new orders fell with respect to the same period of last year mainly due to lower acquisitions of orders by the Italian subsidiary Ansaldo Segnalamento Ferroviario S.p.A., which, in the first quarter of 2006, received a significant volume of automated train control systems (SCMT) orders were received (€mil. 71), and an EBIT substantially in line with that of the first quarter of 2006 (ROS at 9.8%);
- Systems: commercial performance in decline compared with the same period of last year which benefited from the extension of the operation and maintenance

contract for the Copenhagen driverless metro (€mil. 127), and EBIT rose over the same period of 2006 (ROS at 9.5%);

- Vehicles: volumes ordered fell from the first quarter of 2006; financial performance continues to be characterised by operating losses, and is affected by industrial problems addressed in an intervention plan that has been introduced affecting the main corporate processes.

New orders acquired in the first three months of 2007 totalled €mil. 170, a decrease of €mil. 314 over the same period of the previous year (€mil. 484), reflecting a decrease in orders in all business segments. The key orders during the period included the following:

- Signalling: two orders placed by the mining firm Rio Tinto, one by Fortescue Metals Group and contracts as part of the agreement signed with the Australian Rail Track Corporation (ARTC) in Australia, orders relating to the Chambers Street station of the New York subway, two orders from China concerning the Binhai West extension and Shanghai Line 2 CAB, for onboard equipment from Korea;
- Systems: order related to Alifana Inferiore to equip 15 Metrocampania Nordest electric trains with technological signalling systems;
- Vehicles: service orders.

At 31 March 2007, the **order backlog** for the division totalled €mil. 4,540, a decrease of €mil. 163 over the same figure at 31 December 2006 (€mil. 4,703).

Revenues at 31 March 2007 came to €mil. 330, a decrease of €mil. 10 over 31 March 2006 (€mil. 340), mainly attributable to the Vehicles division. Among the noteworthy orders in the Transportation division were the following:

- Signalling: high-speed train orders and automated train control systems (SCMT), both wayside and on-board, for Italy; second phase of the Channel Tunnel Rail Link; the project for the realisation of the Optimizing Traffic Planner (OTP) system and the Next Generation Computer Aided Dispatch System (CAD) for Union Pacific Railroad; and the manufacture of components;

- Systems: the metro systems of Copenhagen, Naples Line 6, Genoa and Brescia, the Alifana regional line; and high-speed rail orders in Italy;
- Vehicles: trains for the Madrid metro; high-volume passenger trains for Morocco; trains for regional service for Ferrovie Nord Milano; high-speed trains for the Dutch-Belgian railways; DMU trains for the Danish railways; trams for the city of Los Angeles; E402 locomotives and ETR500 Politensione trains for Trenitalia; and service and revamping activities.

EBIT at 31 March 2007 came to €mil. 9, a decrease of €mil. 7 over 31 March 2006 (€mil. 16), mainly due to problems in the Vehicles division. **ROS** for the sector decreased as a result to 2.7%, from 4.7% in the first quarter of 2006.

Working capital at 31 March 2007 came to €mil. 116, an increase of €mil. 55 over the same figure at 31 December 2006 (€mil. 61), with improvements attributable to an increase in net inventory in Vehicles.

Net invested capital at 31 March 2007 came to €mil. 362, an increase of €mil. 50 over the result recorded at 31 December 2006 (€mil. 312), reflecting the aforementioned increase in working capital.

Research and development costs at 31 March 2007 came to €mil. 14, up €mil. 4 from the same figure at 31 March 2006 (€mil. 10), which is essentially attributable to the Signalling segment. In particular, these activities concerned Signalling projects, aimed primarily at meeting the new requirements emerging both in the railway segment (level 2 of the European Rail Traffic Management System, or ERTMS rbc) and the mass transit segment (Communications Based Train Control, or CBTC), as well as the development of certain on-board equipment (the next-generation cab).

The **number of employees** at 31 March 2007 stood at 6,784, an increase of 107 compared with 31 December 2006 (6,677), principally due to hiring in the Signalling division, in Australia and India.

OTHER ACTIVITIES

€ millions	31 March 2007	31 March 2006	31 December 2006
New orders	10	19	99
Order backlog	316	419	346
Revenues	47	61	229
EBIT	(22)	(40)	(128)
R.O.S.	n.s.	n.s.	n.s.
Working capital	199	31	135
Net invested capital	1.061	1.054	745
R.O.I. (*)	n.s.	n.s.	n.s.
Research and development	-	-	-
Employees (no.)	812	865	811

(*) calculated on invested capital at period-end

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

The division also includes Fata S.p.A. (for which the reorganisation process begun in 2005 has been completed) which operates in the area of plants for the processing aluminium and steel flat rolled products and engineering design in the electricity generation area for engineering, procurement and construction (EPC) activities.

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

* * * * *

This division's figures also include those of the Corporate division of Finmeccanica S.p.A., which for some years has been undergoing an extensive transformation process, altering its focus from a financial company to that of an industrial company. This process, which is not yet complete, received a boost during 2006 with a commitment from management to press on with a series of actions concerning industrial, technological and commercial integration. The Group will then be able to benefit from an additional impetus in improving its own productivity through processes to increase efficiency and rationalisation.

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

- further strengthening of the mechanisms for the coordination of companies, including through development of specific Central Management structures, so that the individual parts could operate through a single policy, not just in financial terms, but particularly in industrial terms, involving the key processes of product engineering, technology and commercial strategy;
- the assignment of specific objectives to the companies: firstly, the constant growth of EBIT, thanks to increased volumes and continuous efficiency-enhancement efforts, such as the optimisation of procurement, the rationalisation of production sites, as well as company restructuring leading to the containment/reduction of working capital and general and administrative costs and maximizing sales, with the consequent strengthening of production margins.

The constant focus on trends in working capital in addition to the above will make it possible to generate the significant cash flows needed to finance the high level of investment in product development;

- review of processes from a Group perspective, in particular those that could have an effect on the optimisation of areas with possible synergies, such as information technology and real estate management;
- the issuance of specific directives aimed at the progressive alignment of cash flows with income and expenses;
- continued development of a process for the dissemination of a Group methodology for controlling and managing programmes, based on the integration of the international standards of life cycle management, phase review, project control, and risk management.

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

5. Outlook

Performance in the first three months of 2007 improved with respect to that in the same period of the previous year, in line with the forecasts made at that time. In the light of developments to date, there would appear to be no circumstances that would alter the forecasts made during the preparation of the 2006 annual report.

It is important to remember that the size of the orders backlog, defined based on its workability, is such as to guarantee 89% coverage of expected production for the next period.

As a result, during 2007 we expect overall growth in Group revenues of between 4% and 10% with an increase in EBIT of between 8% and 14% over 2006.

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

for the Board of Directors
Pier Francesco Guarguaglini
Chairman and Managing Director